

ADTRAN INC

FORM 10-K (Annual Report)

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Industry	Communications Equipment
Sector	Technology
Fiscal Year	12/31

FORM 10-K
FOR ANNUAL AND TRANSITION REPORTS
PURSUANT TO SECTION 13 OR 15(d) OF THE
SECURITIES EXCHANGE ACT OF 1934

ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934 For the Fiscal Year Ended December 31, 1997

TRANSITION REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES
EXCHANGE ACT OF 1934 For the Transition Period from ___ to ___

Commission file number 0-24612

ADTRAN, Inc.

(Exact name of Registrant as specified in its charter)

Delaware
(State of incorporation)

63-0918200
(I.R.S. Employer
identification Number)

901 Explorer Boulevard, Huntsville, Alabama 35806-2807
(Address of principal executive offices, including zip code)

(256) 963-8000
(Registrant's telephone number, including area code)

Securities registered pursuant to Section 12(b) of the Act: None

**Securities registered pursuant to Section 12(g) of the Act:
Common Stock, \$.01 par value**

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes X 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 the 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. X

The aggregate market value of the Registrant's outstanding Common Stock held by non-affiliates of the Registrant on March 12, 1998 was \$568,848,69. There were 39,402,679 shares of Common Stock outstanding as of March 12, 1998.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Proxy Statement for the Annual Meeting of Stockholders to be held on April 27, 1998 are incorporated herein by reference in Part III.

ADTRAN, Inc.
Annual Report on Form 10-K

For the Fiscal Year Ended December 31, 1997

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PART I

ITEM 1. BUSINESS

Overview

ADTRAN, Inc. (the "Company") designs, develops, manufactures, markets and services a broad range of high-speed digital transmission products utilized by telephone companies ("Telcos") and corporate end-users to implement advanced digital data services over existing telephone networks. Most of the Company's Telco and customer premises equipment ("CPE") products are connected to the local loop ("Local Loop"). The Local Loop is the large existing infrastructure of the telephone network connecting end-users to a Telco's central office, the facility that provides the local switching and distribution functions ("Central Office"). The balance of the Company's products are used in the Telcos' Central Offices.

The Company's product lines, which are comprised of over 500 principal products, are built around a core technology developed by the Company to address the Local Loop and Central Office digital communications marketplace. These products include a comprehensive line of transmission, repeater, extension and termination products such as dataports, channel and data service units, and digital repeaters and extenders. The Company also offers a broad line of T-1 multiplexers providing modular flexibility to the CPE marketplace. A separate T-1 product line is sold to Telcos for use within their Central Offices. The Company has addressed the wireless marketplace with the introduction of a wireless spread spectrum microwave transceiver.

The Company's products address two market segments: (i) Telco products for use in the Local Loop or in Central Offices and (ii) CPE products for end-users. In 1997, sales of Telco and CPE products accounted for 64.8% and 35.2% respectively, of the Company's sales. The Company's Telco products deliver cost-effective digital services such as 56/64 Kbit/sec Digital Data Service ("DDS"), 128 Kbit/sec Integrated Services Digital Network ("ISDN") 64 Kbit/sec or 1.544 Mbit/sec Frame Relay service ("Frame Relay") and 1.544 Mbit/sec T-1 (24 Channel) service. In addition, the Company's High bit-rate Digital Subscriber Line ("HDSL") products permit T-1 transmission on up to 12,000 feet of unconditioned copper wireline while reducing the need for costly mid-span repeaters. The Company's CPE products provide end-users access to Telco digital services and often include additional features for specific end-user applications. The Company has introduced and shipped a number of HDSL, ISDN and other products which comply with international standards to increase its penetration of overseas markets. See "Business -Products."

The rapidly expanding requirements for digital transmission in the Local Loop are being driven by Internet access, small office/home office ("SOHO") users, video delivery and on-line data services, among other applications, all of which require and benefit from the speed, reliability and low cost of digital transmission. While the Telcos have, to a large extent, replaced their wireline data transmission network between Central Offices with fiber-optic and digital microwave links which allow for high speed digital transmission, the Local Loop remains predominantly characterized by low speed analog transmission over copper wirelines. As a result, there has been considerable impetus for Telcos to upgrade the Local Loop in the most cost effective manner available. Widespread replacement of the copper wireline Local Loop remains prohibitively expensive, so the Telcos have turned to manufacturers such as the Company for technologies that expand Local Loop capabilities to handle digital transmission without necessitating this costly replacement. Existing digital delivery technologies, including Frame Relay, ISDN and HDSL, are all experiencing rapid compound growth. Numerous higher speed digital technologies are under development or in the trial stage, including Asymmetric Digital Subscriber Line ("ADSL"), Switched Multi-megabit Data Services ("SMDS"), Asynchronous Transfer Mode ("ATM"), wireless transmission, hybrid fiber coax and cable modems.

The Company's core technologies expand the digital transmission capabilities of the Local Loop by enabling increased transmission speed and/or increased transmission distance. Ongoing research and product development activities are designed to enhance the distances covered by existing services as well as to develop new higher speed technologies. For example, during the first quarter of 1996, the Company demonstrated to the Telcos its new "Total Reach" delivery technology which increases the distance covered by ISDN services in the Local Loop from 18,000 feet to 30,500 feet. The same technology is being incorporated into 64Kbit/sec digital products for use in Frame Relay and DDS services. In addition, the Company is engaged in research, performance simulation, and design of higher speed digital technologies for the transport of data. Current issues for future higher speed digital technologies, including costs, power consumption and distances reachable, must be resolved for widespread acceptance and deployment of these technologies.

In developing its product families, the Company has continuously improved its design, purchasing and production processes to lower product costs and has consistently offered improved products at lower prices to customers. As a result, management believes that the Company is a leading provider of Local Loop and Central Office digital transmission products to Telcos. See "Company Strategy." The Company's customers include all seven Regional Bell Operating Companies ("RBOCs"), GTE Corporation, the three largest interexchange carriers, many of the 1,300 independent telephone companies as well as a number of worldwide electronics, communications and industrial companies. See "Business-Customers."

The Company was incorporated under the laws of Delaware in November 1985 and commenced operations in January 1986.

Recent Developments

The Company is continuing a project to expand its facilities in Huntsville, Alabama in phases over the next four years at a cost expected to exceed \$150,000,000 of which, almost \$50,000,000 had been incurred at December 31, 1997. Fifty million of this project was approved for participation in an incentive program offered by the Alabama State Industrial Development Authority (the "Authority"). That incentive

program enables participating companies such as the Company to generate Alabama corporate income tax credits that can be used to reduce the amount of Alabama corporate income taxes that would otherwise be payable. There can be no assurance that the State of Alabama will continue to make these corporate income tax credits available in the future, and the Company therefore may not realize the full benefit of these incentives. The Authority has issued \$50,000,000 of its taxable revenue bonds pursuant to such program and loaned the proceeds from the sale of the bonds to the Company. The Company will make payments to the Authority in amounts necessary to pay the principal of and interest on the Authority's Taxable Revenue Bond, Series 1995 (ADTRAN, Inc. Project), as amended, currently outstanding in the aggregate principal amount of \$50,000,000. Said bond matures on January 1, 2020, and bears interest at the rate of 45 basis points over the money market rate of First Union National Bank.

Company Strategy

The Company's growth strategy includes the following elements:

Focus on Local Loop and Central Office Digital Transmission Products. Upon commencing operations in 1986, the Company focused its product strategy upon capturing a significant market share for sales of Local Loop and Central Office digital transmission products to Telcos. This focus was the result of the recognition by the Company's founders of the significant opportunity created by the elimination of American Telephone & Telegraph Co.'s ("AT&T") monopoly position in the manufacture of telecommunications equipment. Having achieved a leading market share of Local Loop and Central Office digital transmission products, the Company intends to consolidate its position through an integrated program of new product development, customer service and product excellence.

Capitalize on Existing Leadership Position in the Telco Market. As a leader in the Telco market it serves, the Company intends to apply its sales and customer service resources to new market opportunities that arise as expanded services are provided by the Telcos in response to increasing subscriber demand. In this regard, the Company expects that its in-depth understanding of and experience with Local Loop and Central Office technology will provide it a competitive advantage. The Company is committed to replace most of its products with succeeding generations of products with lower costs, additional product features and improved serviceability.

Adapt Product Technology and Sales Force to CPE Market. Over the past six years, the Company has adapted product technology developed for Telco Central Offices for use in the Company's CPE product lines. As many of the technologies that are critical to success in the CPE market are identical to those already developed and refined for the Company's Telco products, the Company has realized a competitive advantage through leveraging these product development efforts and expertise in all of its markets. To sell its CPE products to the large number of end-users which comprise the market, the Company has built a dedicated sales force and an extensive nationwide network of re-sellers over the past six years. The Company intends to develop new distribution channels to address the worldwide market for its CPE products.

Expand into International Markets. While international sales are not currently substantial, international customers have begun to order, and the Company has shipped, international versions of the Company's Telco and CPE products. The Company has formed, and will continue to pursue, international distribution arrangements built upon core products and technology developed by the Company in an effort to further its penetration into international markets. The Company has also focused on developing E-1 technology, the predominant standard for data transmission outside of North America. In the future, the Company plans to add appropriate support capabilities and introduce new versions of its products that incorporate E-1 technology and that otherwise comply with relevant international standards. The Company's development process currently is conducted in accordance with ISO 9001, the international standard for quality management systems for design, manufacturing and service.

Invest in Engineering and Product Development. The Company expects to continue its relatively high levels of investment in developing innovative new products, and redesigning existing products, in order to reduce product costs and production cycle times, and in so doing will continue its efforts to be a low cost provider in the industry. New products are generally targeted at opportunities that promise rapid growth as product costs are reduced and feature sets are optimized. The Company will also continue to develop and expand its broad product line serving each of the Telco and CPE markets. The Company continuously monitors developing technologies and introduces products as defined standards and markets emerge. This diversification in products and markets will continue to be a key to the Company's business strategy.

Adapt to New Local Loop Media. New Local Loop connections continue to be implemented primarily with copper wirelines, although the Company anticipates an increased use of fiber-optic, coaxial and wireless communications in new installations over the next decade and more. To the extent such alternative connection methods become economically advantageous, and as such markets develop and grow, the Company intends to extend its technical and marketing experience to develop products meeting the demands of such markets.

Commit to Constant Improvements in Quality and Service. The Company believes its success to date has been due in large measure to its commitment to constantly improve product quality and customer service. This commitment has been formally recognized in awards received from several of its largest customers. In the future, product quality is expected to contribute significantly to the Company's efforts to reduce production cycle times and product costs.

Products

Core Product Technology. The Company's product lines, comprised of over 500 principal products, are built around core technologies developed by the Company to address the Central Office and Local Loop digital communications marketplaces. Central Office facilities, approximately 30,000 of which are located throughout North America, provide subscribers with access to a discrete portion of the network's bandwidth on a switched basis ("switched access") or on an exclusive basis ("private line"). Typically, access is available in unit multiples of

56 Kbit/sec (64 Kbit/sec in some locations) increments, although Telco multiplexing equipment can efficiently aggregate these basic increments into high speed channels up to T-1 rates (1.544 Mbit/sec), T-3 (45 Mbit/sec) or faster rates. Individual channels can also be subdivided to speeds as low as 2.4 Kbit/sec.

Each individual Local Loop circuit is served by a circuit assembly (consisting of a channel unit, U-Basic Rate Transmission Extender, or "U-BR1TE" or other similar products manufactured by the Company) that plugs into a Central Office channel bank or shelf. The speed and functionality of the circuit is determined by the type of circuit assembly deployed by the Telco. For each such circuit, Central Office facilities generally make available a corresponding physical mounting position in a channel bank or shelf, and plug-in circuit assemblies are installed in accordance with the service ordered by the subscriber. Other special plug-in circuit assemblies, such as those manufactured by the Company, are commonly employed to connect or bridge circuits within the Central Office. Individual communication channels (multiplexer time slots) are interconnected and switched as appropriate within the Central Office, and the resultant communications payload is then directed toward the proper destination. If the communications traffic needs to be delivered to another Central Office, it is directed toward the inter-office network, usually through a long distance carrier such as AT&T, MCI or Sprint. At the far-end connection, the process is reversed. Voice is converted into digital form by circuit assemblies within the RBOC's Central Office and treated like any other digital information until delivered to the far-end serving Central Office where it is returned to analog form in the Local Loop. However, when products such as those sold by the Company are utilized, data communications traffic remains in digital form end to end.

In recent years, the need for higher volume data communications has led to the development of "remote huts." Like the Central Office, remote huts provide subscriber access through plug-in circuit assemblies such as those manufactured by the Company, but they can take advantage of high capacity fiber-optic links to bring service to the local area economically. Remote huts are then connected by the Local Loop to end-users with products such as those sold by the Company. The Company also manufactures optional mid-span repeaters that extend the service range of the Local Loop, as well as optional termination units that are deployed to monitor and maintain service to the subscriber.

At the customer's premises, terminating equipment receives the transmitted signal from the Central Office and converts it to a form useful to end-user products such as LAN interconnection gear, video conferencing equipment, PBXs, personal computers and related equipment. In general, the Local Loop and related CPE products support bi-directional communications traffic.

Today, the Company's product lines consist of two groups of inter-related products, all evolving from the core product technology developed for the Local Loop:

- * Telco Central Office and Local Loop digital transmission products.

- * CPE products.

Telco Central Office and Local Loop Digital Transmission Products. Several hundred to several thousand circuit assemblies, such as those manufactured by the Company, are required at each Central Office, since each Local Loop generally requires a unit of this type to provide service to each subscriber. In 1997, the Company delivered more than 749,856 units of this product group, accounting for 76.7% of the Company's total units shipped. Telco products accounted for 64.8% and 68.7% of the Company's sales in 1997 and 1996 respectively. Sales of Telco products to original equipment manufacturers ("OEMs") are included in these percentages. The Company had in prior years reported Telco product sales to OEM customers in an OEM product section of Form 10-K, and were not part of the Telco product percentages. The Company now categorizes certain OEM sales as Telco product sales, as the OEM supply contracts are customer funded modifications of Telco products.

Typical of the different versions of Central Office channel assemblies manufactured by the Company are the various OCU dataports and related products, the fundamental building blocks for delivering DDS and Frame Relay services at 56/64 Kbit/sec rates to subscribers. The Company is also a leading industry supplier of mid-span DDS repeaters. In response to the Telco's need for a method to monitor transmission conditions and to detect problems for each individual circuit, the Company pioneered development of the Digital Data Station Termination ("DDST") product family. Both the OCU dataports and DDSTs are produced in relatively high volumes directly related to the increased demand for DDS and Frame Relay services.

The Company is the industry's primary supplier of U-BR1TEs, which are required to extend ISDN service from an ISDN capable switch at a hub Central Office to a serving Central Office or to remote Channel Banks. The Company also supplies a substantial portion of the industry's ISDN mid-span repeaters. Other ISDN products include a BR1TE Bank to mount multiple U-BR1TES, T-BR1TES, NT-1 interface units, Total Reach and outside plant housings for the repeaters.

Late in 1993, the Company commenced deliveries of its HDSL product family. The Company has chosen to develop its own custom integrated circuits so HDSL product performance, availability and cost can be carefully managed. Management believes that demand for this product family will increase steadily as more affordable versions increasingly become available to the Telcos.

The list price for the Company's Telco product family generally ranges from \$100 to \$1,000 per unit. The following table illustrates the breadth of the Company's Telco products and their applications:

Product or Product Family	Description	Application	Current Product Generation
DDST	Digital Data Station Terminations	Terminates DDS (up to 64 Kbit/sec); monitors and tests DDS lines	4th
DSO-DP	Digital Signal Zero Data Ports	Interconnects 2 channels in the Telco Central Office	5th
HDSL	High bit-rate Digital Subscriber Line Units	Delivers repeaterless T-1(1.544 Mbit/sec) up to 12,000 ft.	5th
LR 56/72	DDS Loop Repeaters	Extends DDS Circuit Range	4th
OCU-DP	Office Channel Units Data Ports	Provides DDS (up to 64 Kbit/sec)	8th
U-BR1TE	U-Basic Rate Transmission Extenders	Extends ISDN (up to 128 Kbit/sec) to Central Offices/remote huts without ISDN Switch	3rd
U-Repeater	ISDN Loop Repeaters	Extends ISDN Circuit Range	3rd
Total Reach ISDN	Extended Range ISDN	Delivers ISDN services (up to 128 Kbit/sec) up to 30,000 feet over a single copper pair	2nd
Tracer	Wireless T1 Transmission	Delivers two T1's over wireless digital spread spectrum microwave radio	1st
Total Reach DDS	Extended Range DDS	Delivers DDS services (up to 64 Kbit/sec) up to 40,000 feet over a single copper pair	1st

CPE Products. The Company's CPE products have evolved from technology developed for its Telco product line. As many of the technologies which are critical to success in the CPE market are identical to those already developed and refined for the Company's Telco products, the Company has realized a competitive advantage through leveraging these product development efforts and expertise in all of its markets. Since initial product deliveries in 1991, CPE product sales have accounted for 35.2% and 31.3% of the Company's sales in 1997 and 1996, respectively.

In most cases, a CPE product is purchased and installed by end-user customers in conjunction with a Telco's digital data transmission service. For example, a DSU is normally installed with each DDS loop. The Company's DSU product line was completely upgraded and revamped in 1993 with five new models that can terminate any standard DDS or Switched 56 digital service available in North America. In 1994, the product line was expanded to include lower cost versions as well as a family of shelf mount units. In 1995, products supporting synchronous data compression and versions supporting the simple network management protocol were added to the family. In 1996, the flagship products were once again redesigned to become more modular and flexible. In 1997, the Company introduced its "IQ Series" of DSU's/CSU's with control and monitor features for frame relay circuits. These design changes have substantially reduced the associated manufacturing costs while increasing the utility of the product to the marketplace. Customer acceptance of this product family has significantly increased the Company's DSU market share, and management believes that further gains are possible with the Company's recent enhancements of this product line.

Over the past three years, Frame Relay Services have met with increasing customer acceptance. As a result, the Company has introduced a family of Frame Relay Service units (FSU). These products are built from the core technologies utilized in the existing DSU and TSU product families.

The Company believes that its ISDN Service Unit (ISU) with sustained data transmission rates up to 128 Kbit/sec was the first product of its type when introduced in 1993. New versions of the product introduced by the Company have followed, including a model that automatically senses and adapts to virtually any far-end communications device, including modems, 2 wire or 4 wire DSUs, or another ISDN terminal adapter. The ISU product family was later extended to include the ISU 512, a device that allows multiple ISDN lines to be combined for use by

high speed video conferencing equipment. Recently, ADTRAN has solved one of the biggest obstacles in successful installation of new ISDN circuits with the introduction of its "Expert ISDN" technology. Expert ISDN allows CPE devices to automatically determine key parameters, such as Telco switch type and Service Profile Identifiers ("SPIDS"). Previously, these parameters were passed manually from the Telco to the user, who manually entered the information into the CPE device. ADTRAN's new ISDN terminal adapters, the Express XR and XRT, utilize this technology. Additionally, these products have been recognized by Computer Telephony Magazine as "Products of the Year" and received the "97 Design and Engineering" award at the Winter Consumer Electronics Show (CES).

Late in 1993, initial installations of the Company's T-1 Service Unit ("TSU") were successfully completed. Offering full or fractional T-1 access, the product line is designed for sophisticated users needing higher speed interconnection of LANs, remote offices, video delivery systems, graphic workstations and related equipment. Common plug-in modules are available for several of the Company's models, tailoring the units for multi-channel data communications. TSU order rates have increased steadily since the 1993 introduction and now comprise a significant portion of CPE sales. The TSU product line augments the Company's mature line of ACT Channel Banks that accommodate most commercially available channel units, including those offered by the Company's competitors. The Company's technical expertise was recognized in July of 1997, as ADTRAN's TSU 120 TSU/CSU received a Users Choice Award from Communications News Magazine in the T1/T3 networking category.

Late in 1997, the Company introduced its new ATLAS 800 Integrated Access System. The ADTRAN Total Access System, ATLAS, is a modular, highly scalable platform that provides robust solutions addressing the wide area communication needs of medium to large corporations as well as network access providers. ATLAS is a powerful host-site access platform that provides customers with a total integrated end-to-end solution.

The list price for the CPE product family generally ranges from \$500 to \$2,000 per unit. The following table illustrates the breadth of the Company's CPE products and their applications:

Representative CPE Products

Product or Product Family	Description	Application	Current Product Generation
Act Channel Bank	T-1 (1.544 Mbit/sec) Channel Banks, compatible with D-4 Channel Units	Provides user access to each of 24 channels in T-1 service	3rd
DSU	Data Service Units/ Channel Service Units	Connects data terminal equipment to DDS (up to 64 Kbit/sec); standard interface for data processing equipment	4th
SMART 16	Shelf-Mount Systems	Provides means for end-users to plug in multiple DSU, TSU and ISU circuit assemblies	2nd
ISU	ISDN Service Units	Connects data terminal equipment to ISDN (up to 128 Kbit/sec) network	3rd
TSU	T-1 Data Service Units/Channel Service Units	Connects data terminal equipment to T-1 (1.544 Mbit/sec) network	2nd
T1-CSU	T-1 Channel Service Units	Provides T-1 termination	3rd
NT-1	Network Termination	Provides ISDN termination	3rd
FSU	Frame Relay Service Unit	Provides Frame Relay circuit termination	1st
ATLAS	Integrated Access System	Consolidates voice, data and video into a single, scalable platform	1st

International Markets

The Company serves its international markets through a combination of direct sales and distribution agreements. The Company has formed, and will continue to pursue, international distribution arrangements built upon core products and technology developed by the Company in an effort to further its penetration into international markets. In addition, the Company has focused on developing E-1 technology which, though similar to T-1 technology, has a transmission rate of 2.048 Mbit/sec and is the predominant standard for data transmission outside of North America. The Company has tested, received orders for and shipped HDSL products incorporating E-1 technology. The Company anticipates that it will develop additional products incorporating E-1 technology. ISDN development work is underway to incorporate compatibility with European ISDN standards and specific in-country network interface requirements. Although the Company has not yet fully developed its potential in its international markets and related sales have been modest (8.7% of total sales in 1997), the Company believes that international markets present a significant opportunity for growth.

Research and Product Development

The markets for the Company's products are characterized by rapidly changing technology, evolving industry standards and continuing improvements in telecommunications service offerings of common carriers. If technologies or standards applicable to the Company's products, or common carrier service offerings based on the Company's products, become obsolete or fail to gain widespread commercial acceptance, the Company's business may be adversely affected. Moreover, the introduction of products embodying new technology, the emergence of new industry standards or changes in common carrier service offerings could adversely affect the Company's ability to sell its products. For instance, a large number of the Company's products have, to date, been designed to apply primarily to the delivery of digital communications over copper wireline in the Local Loop. While the Company has competed favorably by developing a high performance line of products, it expects that the increasing deployment of fiber-optic cable, coaxial cable and wireless transmission in the Local Loop (each of which uses a significantly different process of delivery) will require that it develop new products to meet the demands of these markets when such markets are sufficiently established. The Company's sales and profitability in the past have resulted to a significant extent from its ability to anticipate changes in technology, industry standards and common carrier service offerings, and to develop and introduce new and enhanced products. The Company's continued ability to adapt will be a significant factor in maintaining or improving its competitive position and its prospects for growth. Therefore, the Company will continue to make significant investments in product development, although there can be no assurance that the Company will have the resources necessary to continue this strategy successfully or to otherwise respond appropriately to changing technology, industry standards and common carrier service offerings. See "Management's Discussion and Analysis of Financial Condition and Results of Operations" in the Company's 1997 Annual Report to Stockholders.

As of December 31, 1997, the Company's product development programs were carried out by 252 engineers and engineering support personnel, comprising approximately 25% of the Company's employees. To date, all product development expenses have been charged to operations as incurred. From time to time, development programs are conducted by other firms under contract with the Company, and related costs are also charged to operations as incurred. During 1997, 1996 and 1995, product development expenditures totaled \$30,055,091, \$24,647,425, and \$19,131,457, respectively. Because the Company's product development activities are an important part of its strategy and because of rapidly changing technology and evolving industry standards, the Company expects to spend more in product development activities in 1998 than it did in 1997.

The Company's product development personnel are organized into teams, each of which is effectively dedicated to a specific product line or lines. However, because the Company services each of the Telco and CPE markets, and because all of the products in each of the markets share certain similarities, the benefits of the Company's product development efforts generally are not confined to a particular market, but can be leveraged to the Company's advantage in all of its markets. As of December 31, 1997, product development teams were assigned to the following product lines: Loop products, Network products, HDSL products, DSU and Frame Relay products, T-1 multiplexer products, ISDN Telco products, ISDN CPE products, strategic products and extended range products. In addition, engineering services and advanced technology groups provide support for all the product development teams. Each product development team is generally responsible for sustaining technical support of existing products, improving the cost or manufacturing of products, conceiving new products in cooperation with other groups within the Company and adapting standard products or technology under supply contracts to other firms. In particular, each product development team is charged with implementing the Company's engineering strategy of reducing product costs for each succeeding generation of the Company's products in an effort to be a low cost, high quality provider in the industry, without compromising functionality or serviceability. This strategy has involved setting a price point for the next generation of any given product with the aim of meeting that price point through innovative engineering. The key to this strategy is choosing an initial architecture for each product that enables engineering innovations to result in future cost reductions. Successful execution of this strategy also requires that the Company continue to attract and recruit outstanding engineers, and the continued success of the Company's recruiting program at Southeastern universities is critical to this effort.

The product development teams are supported by a research group that provides guidance in applicable digital signal processing technologies, computer simulation and modeling, CAD/CAM tool sets, custom semiconductor design and technological forecasting. As product and market opportunities arise, the organizational structure may be adjusted accordingly. The Company's development process is conducted in accordance with ISO 9001, which is the international standard for quality management systems for design, manufacturing and service.

The Company believes that its success in the past has been dependent upon the ability of its engineering team to establish and maintain a position of product and technological leadership, and its success in the future will be equally dependent upon the evolution of new forms of existing products and the development of new products fulfilling the needs of current and future customers. Therefore, the Company will continue to make significant investments in product development.

Customers

The Company's customer base includes each of the seven RBOCs and most of the major independent domestic Telcos. The major customers of the Company include:

Alltel Corporation	Hong Kong Telecom
Ameritech Corp.	NYNEX Corp.
Azteca Telecommunications	Pacific Bell
Bell Atlantic Network Services	Solunet, Inc.
BellSouth Corp.	Siemens Corp.
Bloomberg L.P.	Southwestern Bell Corp.
Cincinnati Bell	Sprint Corp
Cisco Systems, Inc.	Tech Data, Inc.
Eltrax	US West, Inc.
GTE Corp.	

Historically, a large percentage of the Company's sales have been to the seven RBOCs (31.7% in 1997) and other Telcos (33.0% in 1997). GTE and Sprint accounted for 19.5% and 10.0%, respectively, of the Company's total sales in 1997. No other customer accounted for 10% or more of the Company's sales in 1997.

A supplier such as the Company must first obtain product approvals from an RBOC or other Telco to sell its products to such RBOC or Telco. The Company, therefore, is involved in a constant process of submitting for approval succeeding generations of products as well as products that deploy new technology or respond to a new technology demand from an RBOC or other Telco. While the Company has been successful in the past in obtaining such approvals, there can be no assurance that such approvals or that ensuing sales of such products will continue to occur. Further, any attempt by an RBOC or other Telco to seek out additional or alternative suppliers or to undertake, as permitted under applicable regulations, the production of such products internally could have a material adverse effect on the Company's operating results. See "Government Regulation."

Marketing, Sales and Distribution

As of December 31, 1997, the Company's marketing, sales and distribution programs were conducted by 166 employees. The Company sells its Telco products in the United States directly to the Telcos through a field sales organization based in 39 locations (some of these work out of their homes) in the United States, Canada, and it sells its Telco products internationally through a Hong Kong sales office and various distribution arrangements with a geographically dispersed set of distributors. The Company sells its CPE products, both domestically and internationally, through a network of re-sellers. The Company has formed, and will continue to pursue, international distribution arrangements built upon core products and technology developed by the Company in an effort to further its penetration into international markets. Although the international market channel has not yet been fully developed and related revenue has been modest, the Company believes that international markets present a significant opportunity for growth, and the Company continues to focus effort on positioning itself to take advantage of such opportunity.

Sales to Telcos involve protracted product qualification and standardization processes that can extend for several months or years. Subsequent orders, if any, are generally placed under single or multi-year supply agreements that are generally not subject to minimum volume commitments. Telcos generally prefer having two or more suppliers of most products, so individual orders are generally subject to competition based on some combination of price, delivery and other terms. CPE products are sold under both exclusive and non-exclusive distribution agreements.

The Company's field sales organizations and distributors receive support from headquarters-based marketing, sales and customer support groups. Under certain circumstances, other headquarters personnel may become involved in sales and other activities. The Company believes that its success in the past has been dependent to a significant degree upon the ability of its sales and distribution teams to compete effectively in a highly competitive environment that includes firms with greater financial resources and more experience than the Company. The Company's success in the future will depend in part upon its ability to attract and retain qualified sales and marketing personnel who can compete and succeed in this environment.

Customer Service and Support

The Company maintains 24-hour, 7 day a week telephone support for all of its customers as customers often demand an immediate response to problems with installed products or with plans for new installations. The Company provides on-site support in those circumstances in which problems cannot otherwise be resolved. It has generally been the Company's policy to follow through with problem resolutions even after it is established that the Company's products are not the source of the difficulty. The Company provides direct installation and service of its products in North America utilizing its own resources or resources available under a nationwide services contract with TSS (formerly General Electric) for installation and service. International Business Machines Corporation ("IBM") purchased General Electric's service division in 1995 and General Electric assigned the Company's service contract to IBM under the terms of their sale agreement. The Company has approved the assignment. The Company also provides training to its customers (on both a paid and complimentary basis) relative to installation, operation and maintenance of the Company's products.

Substantially all of the Company's products carry a full ten year return-to-factory warranty. Warranty returns to date have been relatively insignificant (less than 1%). The Company believes that its low return rate is the direct result of its commitment to a rigorous product quality program that has garnered it special recognition by several key customers. The Company also offers annual maintenance agreements to its

customers which provide that, in exchange for an annual fee, the Company will provide on-site service, within a specified time, in response to any reported difficulties in the use or performance of the Company's products.

Manufacturing

The principal steps in the manufacturing process are the purchase and management of materials, assembly, testing, final inspection, packing and shipping. The Company purchases parts and components for assembly of all its products from a large number of suppliers through a worldwide sourcing program. However, certain key components used in the Company's products are currently available from only one source, and other key components are available from only a limited number of sources. In the past, the Company has experienced delays in the receipt of certain of its key components, which have resulted in delays in related product deliveries. The Company attempts to manage such risks through developing alternative sources, through engineering efforts designed to obviate the necessity of certain components, and by maintaining quality relationships and close personal contact with each of its suppliers. However, there can be no assurance that delays in deliveries of key components (including particularly integrated circuits as discussed in greater detail below) and consequent delays in product deliveries will not occur in the future. The inability to obtain sufficient key components as required, or to develop alternative sources if and as required in the future, could result in delays or reductions in product shipments which, in turn, could have a material adverse effect on the Company's customer relationships and operating results.

The Company relies on subcontractors in the United States, Mexico and Taiwan for assembly of printed circuit board assemblies, subassemblies, chassis, enclosures and equipment shelves. The Company subcontracts the assembly of a significant portion of its lower priced products to a company in Mexico. Such assembly typically can be done by subcontractors at a lower cost than if the Company assembled such items internally, which furthers the Company's goal of being a low cost, high quality provider in the industry. Subcontract assembly operations do, however, contribute significantly to production cycle times, but the Company believes it can respond more rapidly to uncertainties in incoming order rates by selecting assembly subcontractors having significant reserve capacity. This reliance on third-party subcontractors for the assembly of its products involves several risks, including the unavailability of or interruptions in access to certain process technologies and reduced control over product quality, delivery schedules, manufacturing yields and costs. These risks may be exacerbated by economic or political uncertainties or by natural disasters in foreign countries in which the Company's subcontractors may be located. The Company currently does not undertake any foreign exchange risks as it conducts all transactions with foreign vendors or customers in U.S. dollars.

The Company is heavily dependent on five subcontractors. To date, the Company believes that it has successfully managed the risks of such dependence on these subcontractors through a variety of efforts, which include seeking and developing alternative subcontractors while maintaining existing relationships. However, there can be no assurance that delays in product deliveries may not occur in the future because of shortages resulting from this limited number of subcontractors or from the financial or other difficulties of such parties. The inability to develop alternative subcontractors if and as required in the future could result in delays or reductions in product shipments which, in turn, could have a material adverse effect on the Company's customer relationships and operating results. While the Company believes that alternative sources of supply or alternative subcontractors could be developed if necessary, material delays or interruption of supply might, nevertheless, arise as a consequence of required retraining and other activities related to establishing and developing a new supply or subcontractor relationship and such material delays may have a material adverse effect on the Company's business and operating results.

Basically, final testing and shipment of products to customers occurs in the Company's Huntsville, Alabama facilities. The Company's facilities are certified pursuant to ISO 9001 and certain other telephone company standards, including those relating to emission of electromagnetic energy and safety specifications.

Backlog and Inventory

A substantial portion of the Company's shipments in any fiscal period relate to orders received in that period and firm purchase orders released in that fiscal period by customers under agreements containing non-binding purchase commitments. Further, a significant percentage of orders require delivery within 48 hours. These factors result in very little order backlog. The Company believes that because a substantial portion of customer orders are filled within the fiscal quarter of receipt, the Company's backlog is not a meaningful indicator of actual sales for any succeeding period. To meet this demand, the Company maintains a substantial finished goods inventory. The Company's inventory represented an acceptable range of 26% to 43% of working capital during 1997.

The Company's practice of maintaining sufficient inventory levels to assure prompt delivery of the Company's products increases the amount of inventory which may become obsolete. The obsolescence of such inventory may have an adverse effect on the Company's business and operating results.

Competition

The markets for the Company's products are intensely competitive. With the development of the worldwide communications market and the growing demand for related equipment, additional manufacturers have entered the markets in recent years to offer products in competition with the Company. Additionally, certain companies have, in recent years, developed the ability to deliver fiber-optic cable, coaxial cable and wireless transmission to certain office centers and other end-users. Competition would further increase if new companies enter the market or existing competitors expand their product lines. For instance, legislation has been enacted that lifts the restrictions which previously prevented the RBOCs from manufacturing telecommunications equipment. The RBOCs, which in the aggregate are the Company's largest customers, may increasingly become competitors of the Company in the markets served by the Company. See "Government Regulation" below.

The Company competes for customers on the basis of performance in relation to price, product features, adherence to standards, quality, reliability, development capabilities, availability and support. Some of the Company's competitors and potential competitors have greater financial, technological, manufacturing, marketing, and personnel resources than the Company.

With respect to Telco sales, product quality and availability and an established reputation for customer service are important competitive factors that can affect the Company's ability to have its products accepted and approved by the individual Telcos. The Company's Telco competitors include large established firms such as ADC Telecommunications, Inc., Lucent Technologies, Inc., PairGain Technologies, Inc., Pulse Communications, Inc. (a subsidiary of Hubbell Incorporated), Tellabs, Inc. and Teltrend, Inc., as well as smaller, specialized firms such as Conklin Instrument Corporation and Integrated Network Corporation.

With the introduction of its CPE product lines, the Company entered a market segment with entrenched competitors. Among the significant competitors for standard rate DSU market share are Motorola, Inc., Paradyne Corporation and Racal-Datacom, Incorporated. Market segment leaders for TSU products include ADC KENTROX, a subsidiary of ADC Telecommunications, Inc., Paradyne Corp., Digital Link Corporation and Verilink Corporation. The Company's T-1 multiplexer product line's key competitors include Newbridge Networks Corporation, Pulse Communications, Inc. and TELCO Systems, Inc. An increase in competition could reduce the Company's gross profit margins, may require increased spending by the Company on product development and sales and marketing, and may otherwise adversely affect the Company's business.

Government Regulation

The telecommunications industry is subject to regulation in the United States and other countries. Federal and state regulatory agencies, including the Federal Communications Commission (the "FCC") and the various state public utility commissions and public service commissions, regulate most of the Company's domestic Telco customers. While such regulation does not typically affect the Company directly, the effects of such regulation on the Company's customers may, in turn, adversely impact the Company's business and operating results. For instance, the sale of the Company's products may be affected by the imposition upon certain of the Company's customers of common carrier tariffs and the taxation of telecommunications services. In addition, regulatory policies affecting the availability of common carrier services (such as high speed digital transmission lines) and other terms on which common carriers conduct their business may impede the Company's penetration of certain markets. These policies are under continuous review and are subject to change. Governmental authorities also have promulgated regulations which, among other things, set installation and equipment standards for private telecommunications systems and require that all newly installed hardware be registered and meet certain governmental standards.

Other governmental authorities, such as federal and state courts and the United States Department of Justice, have been in the past, and will likely continue in the future to be, a major force in shaping the manner in which the telecommunications business is conducted and telecommunication services are provided. For instance, the United States telecommunications industry was also significantly impacted by the landmark Modification of Final Judgment (the "MFJ"), which governed the structure of the 1984 divestiture by AT&T of its local operating telephone company subsidiaries (the Divestiture"). The Divestiture increased competition in the U.S. telecommunications industry by (i) eliminating the monopoly power which AT&T had enjoyed for years in most U.S. local and long distance telephone service and equipment markets, and (ii) prohibiting the RBOCs which emerged from the Divestiture from engaging in certain lines of business, including the provision of long distance services and the manufacture of telecommunications equipment. The terms of the Divestiture provide, however, for the removal of the line of business prohibitions if the rationale therefor becomes outmoded by technical developments or changes in competitive conditions.

The Telecommunications Act of 1996 covers a broad range of topics that will dramatically affect the telecommunications industry. RBOCs now will be allowed to manufacture equipment three years after they are eligible to enter the long distance business. The RBOCs, which are among the Company's largest customers, may increasingly become competitors of the Company in the markets it serves. The Telecommunications Act of 1996 also provides for RBOCs to enter long distance markets under certain conditions and long distance carriers may now provide local service.

The Company's business and operating results may also be adversely affected by the imposition of certain tariffs, duties and other import restrictions on components which the Company obtains from non-domestic suppliers, or by the imposition of export restrictions on products which the Company sells internationally.

Proprietary Rights

The name "ADTRAN" and the Company's corporate logo are registered trademarks of the Company. A number of the Company's product identifiers and names are also registered. The Company also claims rights to a number of unregistered trademarks. The Company has obtained patents on thirteen inventions relating to its products and has several patent applications pending. The Company will seek additional patents from time to time related to its research and development activities. The Company protects its trademarks, patents, inventions, trade secrets, and other proprietary rights by contract, trademark, copyright and patent registration, and internal security. Management believes, however, that the Company's competitive success will not depend on the ownership of intellectual property rights, but primarily on the innovative skills, technical competence and marketing abilities of the Company's personnel. The telecommunications industry, nevertheless, is characterized by the existence of an ever increasing number of patents and frequent litigation based on allegations of patent infringement. From time to time, third parties may assert exclusive patent, copyright and other intellectual property rights to technologies that are important to the Company. While there are no outstanding infringement lawsuits pending by or against the Company, there can be no assurance that third parties will not assert litigation claims against the Company in the future, that assertions by such parties will not result in costly litigation, or that the Company

would prevail in any such litigation or be able to license any valid and infringed patents from third parties on commercially reasonable terms. Any infringement claim or other litigation against or by the Company could have a material adverse effect on the Company's business and operating results.

Employees

As of December 31, 1997, the Company had 1008 full-time employees in the United States, two in Canada and one in Hong Kong. Of the Company's total employees, 255 were in sales, marketing, distribution and service, 252 were in research and development, 376 were in manufacturing, and 128 were in administration. None of the Company's employees is represented by a collective bargaining agreement nor has the Company ever experienced any work stoppage. Management believes the Company's relationship with its employees is good.

ITEM 2. PROPERTIES

The Company's headquarters and principal administrative, engineering and manufacturing facilities are located in an office building containing 440,000 square feet located on approximately 22 acres of land in Huntsville, Alabama. The Company also leases 65,480 additional square feet to accommodate manufacturing and engineering activities. Plans are being made to expand its facilities in Huntsville by approximately 600,000 square feet (to accommodate a projected total of 3,000 employees) over the next four years at a cost expected to exceed \$150,000,000 of which almost \$50,000,000 had been incurred at December 31, 1997. See "Management's Discussion and Analysis of Financial Condition and Results of Operations - Liquidity and Capital Resources" in the Company's 1997 Annual Report to Stockholders and Note 6 of Notes to Financial Statements.

The Company also maintains 39 sales and service facilities, 36 located within the United States, two in Canada and one in Hong Kong, in the following locations: Huntsville, AL, Irvine, CA, San Francisco, CA, Denver, CO, Hartford, CT, Atlanta, GA, Chicago, IL, Batavia, IL, Darien, IL, Orland Park, IL, Leakwood, KS, Trenton, NJ, New York, NY, Cleveland, OH, Philadelphia, PA, Irving, TX, Washington, DC and Ontario and Quebec, Canada. In addition to the leases in Huntsville, AL, the facilities in Leakwood, KS, Irvine, CA, Denver, CO, Atlanta, GA, Irving, TX, Altamonte Springs, FL, Herndon, VA and Philadelphia, PA are leased under leases which expire at various times between 1998 and 20010. See Note 9 of Notes to Financial Statements.

ITEM 3. LEGAL PROCEEDINGS

The Company has been involved from time to time in litigation in the normal course of its business. The Company is not aware of any pending or threatened litigation matters which could have a material adverse effect on the Company.

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

No matter was submitted by the Company to vote of security holders during the fiscal quarter ended December 31, 1997.

ITEM 4(A). EXECUTIVE OFFICERS OF THE REGISTRANT

Set forth below, in accordance with General Instruction G(3) of Form 10-K and Instruction 3 of Item 401(b) of Regulation S-K, is certain information regarding the executive officers of the Company. Unless otherwise indicated, the information set forth is as of December 31, 1997

Mark C. Smith - Age 57

Mr. Smith is one of the co-founders of the Company.

1995 to present	Chairman of the Board and Chief Executive Officer
1986 - 1995	Chairman of the Board, Chief Executive Officer and President

Lonnie S. McMillian - Age 69

Mr. McMillian is one of the co-founders of the Company.

1996 to present Senior Vice President, Secretary and Director

1986 - 1996 Vice President - Engineering, Secretary, Treasurer and Director

Howard A. Thraikill - Age 59

1995 to present President, Chief Operating Officer and Director

October 1995 Executive Vice President, Chief Operating Officer
and Director

1992 - 1995 Executive Vice President, Chief Operating Officer

John R. Cooper - Age 50

1996 to present Vice President - Finance and Chief Financial Officer

1995 - 1996 President, Sauty Group

1991 - 1995 Partner, Coopers & Lybrand L.L.P.

Danny J. Windham - Age 38

1995 to present Vice President - CPE Marketing

1994 - 1995 Director of Marketing

1989 - 1994 Manager of Product Management

Thomas R. Stanton - Age 33

1995 to present Vice President - Telco Marketing

1994 - 1995 Sr. Director, Marketing, E.F. Johnson Company

1993-1994 Director, Marketing, E.F. Johnson Company

Peter O. Brackett - Age 56

1996 to present Vice President - Technology

1992 - 1996 Research Manager, Advanced Data Networking, Bellsouth

M. Melvin Bruce - Age 57

1996 to present Vice President - Engineering

1989 - 1996 Vice President, Research and Design, TCI

Robert A. Fredrickson - Age 47

1996 to present Vice President - Telco Sales

1996 Vice President, Broadband Business Development, DSC
Communications Corp.

1991-1996 Senior Director, Access Products, DSC Communications
Corp.

Steven L. Harvey - Age 37

1996 to present Vice President - CPE Sales

1995 - 1996 Executive Vice President, Data Processing Sciences

1991 - 1995 Vice President, Data Processing Sciences

1996 to present Vice President - Quality

1993 - 1996 Quality & Technical Resources Manager, Exide Electronics Corp.

Jude T. Panetta - Age 38

1994 to present Vice President - Manufacturing

1989 - 1994 Director of Manufacturing, Exide Electronics

There are no family relationships among the directors or executive officers.

All officers are elected annually by and serve at the pleasure of the Board of Directors of the Company.

PART II

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

The Company's Common Stock has been traded on the Nasdaq National Market under the symbol "ADTN" since the Company's initial public offering of Common Stock in August 1994. Prior to the initial public offering, there was no established trading market for the Company's Common Stock. As of March 12, 1998, the Company had approximately 625 shareholders of record and approximately 14,200 beneficial owners of shares held in street name.. The following table shows the high and low closing sale prices per share of Common Stock as reported by Nasdaq for the periods indicated:

1997 Quarters	High	Low
First	\$53-1/4	\$22-1/2
Second	\$35-5/8	\$20-7/8
Third	\$44	\$23
Fourth	\$45-1/2	\$26
1996 Quarters	High	Low
First	\$54-3/4	\$26-1/2
Second	\$73-1/2	\$45
Third	\$75-1/4	\$47-1/2
Fourth	\$52-1/4	\$33-1/2

The Company has operated with a policy of retaining earnings, presently intends to retain all future earnings for use in the development of its business and does not anticipate paying any cash dividends in the foreseeable future.

ITEM 6. SELECTED FINANCIAL DATA

The following selected financial data concerning the Company for and as of the end of each of the years in the five year period ended December 31, 1997 are derived from the financial statements of the Company, which financial statements have been audited by Coopers & Lybrand L.L.P., independent accountants. The selected financial data is qualified in its entirety by the more detailed information and financial statements, including the notes thereto, included elsewhere in this report. The financial statements of the Company as of December 31, 1997 and 1996 and for each of the years in the three year period ended December 31, 1997, and the report of Coopers & Lybrand L.L.P. thereon, are included elsewhere in Item 8 of this report.

	1997	Year Ended December 31,		1994	1993
		1996	1995		
	(in thousands, except per share data)				
Income Statement Data					
Sales:					
Telco (1)	\$171,838	\$171,902	\$121,311	\$87,888	\$58,994
CPE (1)	93,497	78,219	60,167	35,552	13,417
Total sales	265,335	250,121	181,478	123,440	72,411
Cost of sales	130,254	129,953	93,007	63,187	36,769
Gross profit	135,081	120,168	88,471	60,253	35,642
Selling, general and administrative expense	44,973	34,308	27,260	17,347	11,898
Research and development expenses	30,055	24,647	19,131	13,774	10,033
Operating income	60,053	61,213	42,080	29,132	13,711
Interest income	4,175	2,542	3,205	440	7
Interest expense	(1,839)	(895)	(1,105)	(448)	(424)

Other income (expense)	438	642	111	(25)	(13)
Income before income taxes (2)	62,827	63,502	44,291	29,099	13,281
Provision for income taxes (2)	22,618	23,682	14,833	6,288	0
Net income (2)	40,209	39,820	29,458	22,811	13,281
Pro forma provision for income taxes (2)	0	0	0	4,202	4,825
Pro forma net income (2)	40,209	39,820	29,458	18,609	8,456
Pro forma net income per share assuming dilution(2)(3)(4)	1.02	1.01	.75	.51	.25
Earnings per common share - basic(2)(3)	1.03	1.03	.80	.56	.27
Weighted average shares outstanding assuming dilution(3) (4)	39,565	39,549	39,249	36,199	34,098
S corporation distributions(2)				\$5,483	\$5,494

	1997	1996	At December 31, 1995	1994	1993
	(in thousands)				
Balance Sheet Data:					
Working capital	\$149,184	\$140,510	\$122,466	\$66,368	\$19,795
Total assets	282,401	210,207	165,767	94,347	46,304
Total debt	50,000	20,000	20,000	0	10,100
Stockholders' equity	212,037	172,879	130,743	85,233	29,757

(1) Represents sales of the Company's Telco and CPE products. These amounts are not derived from the Company's audited financial statements.

(2) Effective July 1, 1994, the Company converted from an S corporation to a C corporation for income tax purposes. As an S corporation, the Company was not subject to income taxes but paid quarterly cash distributions to fund the income tax liabilities passed through to the stockholders. The Company also paid a cash distribution of \$3,121,816 to its stockholders in December 1992 in an amount approximately equal to their original investment in the Company's Common Stock. As a C corporation, the Company is subject to income taxes at corporate tax rates. The pro forma income statement data herein presents the provision for income taxes, net income and net income per share as if the Company had been subject to corporate income taxes for all periods presented.

(3) Reflects a 3-for-2 split of the Company's Common Stock which was effected on August 1, 1994, and a 2-for-1 split of the Common Stock which was effected on May 12, 1995.

(4) Assumes exercise of dilutive stock options calculated under the treasury stock method. See Notes 1, 10, and 13 of Notes to Financial Statements.

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

The Company designs, develops, manufactures, markets and services a broad range of high-speed digital transmission products utilized by Telcos and corporate end-users to implement advanced digital data services over existing telephone networks. The Company currently sells its products to Telcos (including all of the RBOCs), and private end-users in the CPE market.

The Company's sales have increased in each year due primarily to increases in the number of units sold to both new and existing customers. These annual sales increases reflect the Company's strategy of increasing unit volume and market share through the introduction of succeeding generations of products having lower selling prices and increased functionality as compared both to the prior generation of a product and to the products of competitors. An important part of the Company's strategy is to engineer the reduction of the product cost of each succeeding product generation and then to lower the product's price based on the cost savings achieved. As a part of this strategy, the Company seeks in most instances to be a low cost, high quality provider of products in its markets. The Company's success to date is attributable in large measure to its ability to initially design its products with a view to their subsequent re-design, allowing efficient enhancements of the product in each succeeding product generation. This strategy has enabled the Company to sell succeeding generations of products to existing customers as well as to increase its market share by selling these enhanced products to new customers.

While the Company has experienced increased sales in each year, the Company's operating results have fluctuated on a quarterly basis in the past, and operating results may vary significantly in future periods due to a number of factors. The Company operates with very little order backlog. A substantial majority of its sales in each quarter results from orders booked in that quarter and firm purchase orders released in that quarter by customers under agreements containing nonbinding purchase commitments. Furthermore, most Telcos typically require prompt delivery of products; this results in a limited backlog of orders for these products and requires the Company to maintain sufficient inventory levels to satisfy anticipated customer demand. If near term demand for the Company's products declines or if significant potential sales in any quarter do not occur as anticipated, the Company's financial results will be adversely affected. The Company currently does not undertake any foreign exchange risks, as all transactions with foreign vendors or customers are conducted in currency of the United States. Operating expenses are relatively fixed in the short term; therefore, a shortfall in quarterly revenues could impact the Company's financial results significantly in a given quarter. Further, maintaining sufficient inventory levels to assure prompt delivery of the Company's products increases the amount of inventory which may become obsolete and increases the risk that the obsolescence of such inventory may have an adverse effect on the Company's business and operating results. The Company's operating results may also fluctuate as a result of a number of other factors, including increased competition, customer order patterns, changes in product mix, product warranty returns and announcements of new products by the Company or its competitors. Accordingly, the Company's historical financial performance is not necessarily a meaningful indicator of future results, and, in general, management expects that the Company's financial results may vary from period to period. See Note 14 of Notes to Financial Statements.

On August 16, 1994, the Company completed an initial public offering of Common Stock, receiving net proceeds (after deduction of underwriting discounts and other offering expenses) of \$37,867,963 from the sale of 2,300,000 shares of Common Stock (on a pre-split basis). The Company used the offering proceeds to repay the full amount of principal and interest owed on certain revenue bonds issued to construct and equip the Company's headquarters and manufacturing facility in Huntsville, Alabama and to repay all amounts outstanding under its bank line of credit and for general working capital purposes. On June 29, 1995, the Company and certain stockholders of the Company (the "Selling Stockholders") sold a total of 3,125,100 shares of Common Stock to the public. Of the 3,125,100 shares offered, 500,000 shares were offered by the Company and 2,625,100 shares were offered by the Selling Stockholders. The Company received net proceeds (after deduction of underwriting discounts and other offering expenses) of \$15,705,362 from the sale of 500,000 shares of Common Stock at the public offering price of \$33 per share. The Company did not receive any of the proceeds from the sale of shares by the Selling Stockholders. The Company has used and expects to continue to use the proceeds of the public offerings for working capital and other general corporate purposes, including product development activities to enhance its existing products and develop new products and expansion of sales and marketing activities.

The Company intends to retain all earnings for use in the development of its business and does not anticipate paying any cash dividends in the foreseeable future.

When used in this 1997 Annual Report, the words "believe," "anticipate," "think," "intend," "will be," and similar expressions identify forward-looking statements. Such statements are subject to certain risks and uncertainties which could cause actual results to differ materially from those projected. Readers are cautioned not to place undue reliance on these forward-looking statements which speak only as of the date hereof. Readers are also urged to carefully review and consider the various disclosures made by the Company which attempt to advise interested parties of the factors which affect the Company's business, including the disclosures made in other periodic reports on Forms 10-K, 10-Q and 8-K, when appropriate, filed with the Securities and Exchange Commission.

Results of Operations

The following table presents selected financial information derived from the Company's statements of income expressed as a percentage of sales for the years indicated.

Percentage of Sales Sales:	Years Ended December 31,		
	1997	1996	1995
Telco	64.8%	68.7%	66.8%
CPE	35.2	31.3	33.2
Total sales	100.0	100.0	100.0

Cost of sales	49.1	51.9	51.3
Gross profit	50.9	48.1	48.7
Selling, general and administrative expenses	17.0	13.7	15.0
Research and development expenses	11.3	9.9	10.5
Operating income	22.6	24.5	23.2
Interest income	1.6	1.0	1.8
Interest expense	(0.7)	(0.4)	(0.6)
Other income (expense)	0.2	0.3	0.0
Income before provision for income taxes	23.7	25.4	24.4
Provision for income taxes	8.5	9.5	8.2
Net income	15.2%	15.9%	16.2%

1997 Compared to 1996

Sales

The Company's sales increased 6.1% from \$250,120,836 in 1996 to \$265,334,768 in 1997. The increased sales resulted from increased sales volume to existing customers and from increased market penetration. Sales to Telcos remained basically unchanged from \$171,901,851 in 1996 to \$171,837,883 in 1997. Telco sales as a percentage of total sales decreased from 68.7% in 1996 to 64.8% in 1997. Sales of CPE products increased 19.5% from \$78,218,985 in 1996 to \$93,496,885 in 1997. The increase in sales of CPE products is attributable to increased demand for T1 Service Unit (TSU) products and Integrated Services Digital Network (ISDN) products. Cost of Sales Cost of sales increased only slightly, 0.2% from \$129,953,371 in 1996 to \$130,253,531 in 1997, primarily as a result of the increase in sales. As a percentage of sales, cost of sales decreased from 51.9% in 1996 to 49.1% in 1997. This decrease was primarily attributable to manufacturing efficiencies and product design enhancements. An important part of the Company's strategy is to reduce the product cost of each succeeding product generation and then to lower the product's price based on the cost savings achieved. This sometimes results in variations in the Company's gross profit margin due to timing differences between the lowering of product selling prices and the full recognition of cost reductions. In view of the rapid pace of new product introductions by the Company, this strategy may result in variations in gross profit margins that, for any particular financial period, can be difficult to predict.

Selling, General and Administrative Expenses Selling, general and administrative expenses increased 31.1% from \$34,308,436 in 1996 to \$44,973,175 in 1997 due to additional sales and support expenditures necessary as a result of the Company's expanded sales base and increased dollar amounts of these expenses associated with the ongoing introduction and marketing of enhanced products, increased distribution activities associated with the CPE market, and general expansion into international markets. As a percentage of sales, selling, general and administrative expenses increased from 13.7% in 1996 to 17.0% in 1997.

Research and Development Expenses

Research and development expenses increased 21.9% from \$24,647,425 in 1996 to \$30,055,091 in 1997. This increase was due to increased engineering costs associated with new product introductions and feature enhancement activities. As a percentage of sales, research and development expenses increased from 9.9% in 1996 to 11.3% in 1997. The Company continually evaluates new product opportunities and engages in intensive research and product development efforts. To date, the Company has expensed all product research and development costs as incurred. Additionally, the Company also frequently invests heavily in up-front market development efforts prior to the actual commencement of sales of a major new product. As a result, the Company may incur significant research and development expenses and selling, general and administrative expenses prior to the receipt of revenues from a major new product group. The Company is presently incurring both research and development expenses and selling, general and administrative expenses in connection with its new products and its expansion into international markets.

Interest Expense

Interest expense increased 105.5% from \$894,657 in 1996 to \$1,838,814 in 1997. This increase was due to interest cost incurred as a part of the cost of acquiring certain assets. The Company currently pays interest on \$50,000,000 of revenue bond proceeds of which \$20,000,000 was loaned to the Company in January 1995, and \$30,000,000 was loaned to the Company in April 1997. The proceeds were used to expand the Company's facilities in Huntsville, Alabama. See "Liquidity and Capital Resources."

Net Income

As a result of the above factors, net income increased 1.0% from \$39,819,904 in 1996 to \$40,209,272 in 1997. As a percentage of sales, net income decreased from 15.9% in 1996 to 15.2% in 1997.

1996 Compared to 1995

Sales

The Company's sales increased 37.8% from \$181,478,065 in 1995 to \$250,120,836 in 1996. The increased sales resulted from increased sales volume to existing customers and from increased market penetration. Sales to Telcos increased 41.7% from \$121,311,131 in 1995 to \$171,901,851 in 1996 due primarily to increased sales of Integrated Services Digital Network (ISDN) products and increased sales of High bit-rate Digital Subscriber Line (HDSL) products. Telco sales as a percentage of total sales increased from 66.8% in 1995 to 68.7% in 1996 primarily as a result of increased sales volume of ISDN and HDSL products during the 1996 period. Sales of CPE products increased 30.0% from \$60,166,935 in 1995 to \$78,218,985 in 1996. The increase in sales of CPE products is attributable to increased demand for Digital Data Service (DDS) products, T1 Service Unit (TSU) products, and Integrated Services Digital Network (ISDN) products.

Cost of Sales

Cost of sales increased 39.7% from \$93,006,672 in 1995 to \$129,953,371 in 1996, primarily as a result of the increase in sales. As a percentage of sales, cost of sales increased from 51.3% in 1995 to 51.9% in 1996. An important part of the Company's strategy is to reduce the product cost of each succeeding product generation and then to lower the product's price based on the cost savings achieved. This sometimes results in variations in the Company's gross profit margin due to timing differences between the lowering of product selling prices and the full recognition of cost reductions. In view of the rapid pace of new product introductions by the Company, this strategy may result in variations in gross profit margins that, for any particular financial period, can be difficult to predict.

Selling, General and Administrative Expenses Selling, general and administrative expenses increased 25.9% from \$27,259,610 in 1995 to \$34,308,436 in 1996 due to additional sales and support expenditures necessary as a result of the Company's expanded sales base. However, the larger sales base caused selling, general and administrative expenses as a percentage of sales to decrease from 15.0% in 1995 to 13.7% in 1996.

Research and Development Expenses

Research and development expenses increased 28.8% from \$19,131,457 in 1995 to \$24,647,425 in 1996. This increase was due to increased engineering costs associated with new product introductions and product cost and feature enhancement activities. As a percentage of sales, however, research and development expenses declined from 10.5% in 1995 to 9.9% in 1996. The Company continually evaluates new product opportunities and engages in intensive research and product development efforts. To date, the Company has expensed all product research and development costs as incurred.

Interest Expense

Interest expense decreased 19.0% from \$1,105,156 in 1995 to \$894,657 in 1996. This decrease was due to capitalization of the interest cost as a part of the cost of acquiring certain assets. The Company currently pays interest on \$20,000,000 of revenue bond proceeds loaned to the Company in January 1995, which proceeds are being used to expand the Company's facilities in Huntsville, Alabama. See "Liquidity and Capital Resources."

Net Income

As a result of the above factors, net income increased 35.2% from \$29,457,727 in 1995 to \$39,819,904 in 1996. As a percentage of sales, net income decreased from 16.2% in 1995 to 15.9% in 1996.

Liquidity and Capital Resources

The Company is continuing a project to expand its facilities in Huntsville, Alabama in phases over the next four years at a cost expected to exceed \$150,000,000, of which almost \$50,000,000 had been incurred at December 31, 1997. Fifty million of this project has been approved for participation in an incentive program offered by the Alabama State Industrial Development Authority (the "Authority"). That incentive program enables participating companies such as the Company to generate Alabama corporate income tax credits that can be used to reduce the amount of Alabama corporate income taxes that would otherwise be payable. There can be no assurance that the State of Alabama will continue to make these corporate income tax credits available in the future, and the Company therefore may not realize the full benefit of these incentives. The Authority has issued \$50,000,000 of its taxable revenue bonds pursuant to such program and loaned the proceeds from the sale of the bonds to the Company. The Company will make payments to the Authority in amounts necessary to pay the principal of and interest on the Authority's Taxable Revenue Bond, Series 1995 (ADTRAN, Inc. Project), as amended, currently outstanding in the aggregate principal amount of \$50,000,000. Said bond matures on January 1, 2020, and bears interest at the rate of 45 basis points over the money market rate of First Union National Bank.

The Company's working capital position improved from \$140,509,802 as of December 31, 1996 to \$149,183,578 as of December 31, 1997. This improvement in the Company's working capital position was due primarily to increased earnings. The Company has used, and expects to continue to use, the remaining proceeds of its earlier public offerings for working capital and other general corporate purposes, including (i) product development activities to enhance its existing products and develop new products and (ii) expansion of sales and marketing activities. Inventory decreased 3.5% for the twelve months ended December 31, 1997 due to overall efficiencies in manufacturing operations.

On March 31, 1997, the Board of Directors authorized the Company to re-purchase up to 1,000,000 shares of the Company's outstanding common stock. As of December 31, 1997, the Company had re-purchased 100,000 shares of its common stock at a total cost of \$2,200,000.

Capital expenditures totaling \$29,661,438 in 1996 and \$18,220,850 in 1997 were used to expand the Company's headquarters and to purchase equipment.

At December 31, 1997, the Company's cash on hand of \$45,340,961, short-term investments of \$37,833,240 and \$10,000,000 available under a bank line of credit placed the Company's potential cash availability at \$93,174,201. The Company's \$10,000,000 bank line of credit bears interest at the rate of 87.5 basis points over the 30 day London inter-bank offered rate and expires on May 1, 1998. The Company anticipates renewing the \$10,000,000 bank line of credit upon its expiration. The Company intends to finance its operations in the future with cash flow from operations, the remaining net proceeds of its earlier public offerings, amounts available under the bank line of credit, borrowed revenue bond proceeds and possible additional public financings. These available sources of funds are expected to be adequate to meet the Company's operating and capital needs for the foreseeable future.

Year 2000 Compliance

The Company is in the process of reviewing current software and hardware to assess the impact of the year 2000 issue. Initially, the Company has determined that most of the Company's current business process software and hardware are year 2000 compliant. The Company is in the process of implementing new business process software which has been determined to be year 2000 compliant as well. This implementation should be completed in 1998. The Company expects to complete its year 2000 analysis by the end of 1998 and does not believe that costs associated with bringing the Company's computer systems into full compliance with year 2000 will result in material costs to the Company. The Company's products are year 2000 compliant as well and therefore, the Company does not believe that they have any material exposure to contingencies related to the year 2000 issue for products it has sold. The Company is also in the preliminary stages of assessing the impact of the year 2000 issue on its major vendors and suppliers to determine the extent to which the Company is vulnerable to those third parties' failure to remediate their own year 2000 issues. Based on information presently available, the Company does not anticipate any material impact on its financial condition or results of operations from the effect of the year 2000 issue on the Company's internal systems or those of its major suppliers and customers. However, there can be no guarantee that the systems of other companies on which the Company's system rely will be timely converted, or that a failure to convert by another company would not have a material adverse impact on the Company.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The following financial statements are contained in this report.

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Financial Statements for Years Ended December 31, 1997, 1996 and 1995	
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Report of Independent Accountants
To the Board of Directors and Stockholders
ADTRAN, Inc.

We have audited the accompanying balance sheets of ADTRAN, Inc. as of December 31, 1997 and 1996, and the related statements of income, changes in stockholders' equity, and cash flows for each of the three years in the period ended December 31, 1997. These financial statements 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, the financial statements referred to above present fairly, in all material respects, the financial position of ADTRAN, Inc. as of December 31, 1997, and 1996, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 1997, in conformity with generally accepted accounting principles.

/s/ Coopers & Lybrand L.L.P.
COOPERS & LYBRAND L.L.P.
Birmingham, Alabama
January 13, 1998

BALANCE SHEET

December 31, 1997 and 1996

	1997	1996
ASSETS		
Current Assets:		
Cash and cash equivalents	\$45,340,961	\$44,839,131
Short-term investments	37,833,240	32,555,930
Accounts receivable, marked to market, less allowance for doubtful accounts of \$893,389 and \$872,724 in 1997 and 1996, respectively	40,906,887	33,825,560
Other receivables	343,463	362,578
Inventory	39,369,103	40,792,646
Prepaid expenses	1,148,288	2,261,338
Deferred income taxes	2,458,136	1,598,750
Total current assets	67,400,078	156,235,933
Property, plant and equipment, net	64,801,132	53,971,213
Other assets	200,000	0
Long-term investments	50,000,000	0
Total assets	\$282,401,210	\$210,207,146

LIABILITIES AND STOCKHOLDERS' EQUITY

Current liabilities:		
Accounts payable	\$9,121,270	\$9,350,266
Accrued salaries	1,927,364	2,454,194
Accrued income taxes	4,579,345	1,803,706
Accrued taxes other than income taxes	180,611	338,997
Accrued interest payable	0	59,594
Warranty liability	1,435,259	1,026,156
Compensated absences	972,651	693,218
Total current liabilities	18,216,500	15,726,131
Bonds payable	50,000,000	20,000,000
Deferred income taxes	2,147,635	1,602,116
Total liabilities	70,364,135	37,328,247
Stockholders' equity:		
Commonstock, par value \$.01 per share; 200,000,000 shares authorized; 39,381,264 shares issued in 1997 and 38,769,514 in 1996	393,813	387,695
Additional paid-in capital	90,582,615	90,172,863
Retained earnings	123,260,647	82,318,341
Less 100,000 shares treasury stock, at cost	(2,200,000)	0
Total stockholders' equity	212,037,075	172,878,899
Total liabilities and stockholders' equity	\$282,401,210	\$210,207,146

The accompanying notes are an integral part of these financial statements.

STATEMENTS OF INCOME

for the years ended December 31, 1997, 1996 and 1995

	1997	1996	1995
Sales	\$265,334,768	\$250,120,836	\$181,478,065
Cost of sales	130,253,531	129,953,371	93,006,672
Gross profit	135,081,237	120,167,465	88,471,393
Selling, general and administrative expenses	44,973,175	34,308,436	27,259,610
Research and development expenses	30,055,091	24,647,425	19,131,457
Income from operations	60,052,971	61,211,604	42,080,326
Other income (expenses):			
Interest income	4,175,032	2,542,417	3,204,902
Interest expense	(1,838,814)	(894,657)	(1,105,156)
Other	437,639	642,432	111,219
	2,773,857	2,290,192	2,210,965
Income before income taxes	62,826,828	63,501,796	44,291,291
Provision for income taxes	22,617,556	23,681,892	14,833,564
Net income	\$40,209,272	\$39,819,904	\$29,457,727
Weighted average shares outstanding assuming dilution (1)	39,565,497	39,548,654	39,249,101
Earnings per common share assuming dilution (1)	\$1.02	\$1.01	\$0.75
Earnings per common share - basic	\$1.03	\$1.03	\$0.80

The accompanying notes are an integral part of these financial statements.

(1) Assumes exercise of dilutive stock options calculated under the treasury stock method.

STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY for the years ended December 31, 1997, 1996 and 1995

	Common Stock					
	Number of shares	Par Value (\$.01 Per Share)	Additional Paid-In Capital	Retained Earnings	Treasury Stock	Total Stockholders' Equity
Balance, December 31, 1994	18,073,598	\$180,736	\$73,545,813	\$11,506,784	\$0	\$85,233,333
Stock options exercised through issuance of common stock:						
Various prices per share	460,619	4,606	342,283			346,889
Issuance of common stock in June 1995 through a public offering of shares, net of offering costs	500,000	5,000	15,700,362			15,705,362
Issuance of shares to effect stock split, (see Note 8)	18,428,058	184,281	(184,281)			
Net Income				29,457,727		29,457,727
Balance, December 31, 1995	37,462,275	\$374,623	\$89,404,177	\$40,964,511	\$0	\$130,743,311
Stock options exercised through issuance of common stock:						
Various prices per share	1,307,239	13,072	768,686			781,758
Income tax benefit from exercise of non-qualified stock options				1,533,926		1,533,926
Net income				39,819,904		39,819,904
Balance, December 31, 1996	38,769,514	\$387,695	\$90,172,863	\$82,318,341	\$0	\$172,878,899
Stock options exercised through issuance of common stock:						
Various prices per share	611,750	6,118	409,752			415,870
Purchase of treasury stock: 100,000 shares					(2,200,000)	(2,200,000)
Income tax benefit from exercise of non-qualified stock options				733,034		733,034
Net Income				40,209,272		40,209,272
Balance, December 31, 1997	39,381,264	\$393,813	\$90,582,615	\$123,260,647	(\$2,200,000)	\$212,037,075

The accompanying notes are an integral part of these financial statements.

STATEMENTS OF CASH FLOW

for the years ended December 31, 1997, 1996 and 1995

	1997	1996	1995
Cash flows from operating activities:			
Net income	\$40,209,272	\$39,819,904	\$29,457,727
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	7,342,518	4,890,303	3,052,798
Provision for warranty claims	1,435,259	2,110,614	776,908
Loss on sale of property, plant, and equipment	(9,884)	40,572	8,842
Loss on sale of short-term investments classified as available-for-sale	(6,063)	405,789	169,766
Deferred income taxes	(313,867)	104,561	(31,910)
Change in operating assets:			
Accounts receivable	(7,081,327)	(4,590,757)	(11,212,334)
Inventory	1,423,543	4,204,549	(17,472,844)
Other current assets	932,165	(1,083,019)	(270,724)
Change in operating liabilities:			
Accounts payable	(228,996)	(390,321)	3,245,924
Other liabilities	1,284,106	(50,491)	1,584,749
Net cash provided by operating activities	44,986,726	45,461,704	9,308,902
Cash flows from investing activities:			
Expenditures for property, plant and equipment	(18,220,850)	(29,661,438)	(12,790,517)
Proceeds from the disposition of property, plant, and equipment	58,297	4,602	14,250
Purchase of restricted investments	(50,000,000)		
Purchase of short-term investments classified as available-for-sale	(5,271,247)	(8,309,030)	(16,322,455)
Net cash used in investing activities	(73,433,800)	(37,965,866)	(29,098,722)
Cash flows from financing activities:			
Redemption of bonds payable	(20,000,000)		
Proceeds from bond issuance	50,000,000		20,000,000
Proceeds from public offering, net of expenditures			15,705,362
Proceeds from issuance of common stock	415,870	781,758	346,889
Income tax benefit from exercise of non-qualified stock options	733,034	1,533,926	
Purchase of treasury stock	(2,200,000)		
Net cash provided by financing activities	28,948,904	2,315,684	36,052,251
Net increase in cash and cash equivalents	501,830	9,811,522	16,262,431
Cash and cash equivalents, beginning of year	44,839,131	35,027,609	18,765,178
Cash and cash equivalents, end of year	\$45,340,961	\$44,839,131	\$35,027,609
Supplemental disclosure of cash flow information:			
Cash paid during the year for interest, net of capitalized interest of \$204,153, \$393,096 and \$235,928 in 1997, 1996 and 1995, respectively	\$ 1,844,741	\$ 909,368	\$1,030,851
Cash paid during the year for income taxes	\$20,042,644	\$22,151,925	\$13,033,140

The accompanying notes are an integral part of these financial statements.

Notes to Financial Statements

1. Summary of Significant Accounting Policies

ADTRAN, Inc. (the "Company") designs, develops, manufactures, markets, and services a broad range of high-speed digital transmission products utilized by telephone companies ("Telcos") and corporate end-users to implement advanced digital data services over existing telephone networks. The Company also customizes many of its products for private label distribution and for original equipment manufacturers to incorporate into their own products. Most of the Company's Telco and customer premises equipment products are connected to the local loop, which is the large existing infrastructure of the telephone network, predominantly consisting of copper wireline, which connects end-users to a Telco's Central Office. The Central Office is the Telco facility that provides local switching and distribution functions. The balance of the Company's products are used in the Telcos' Central Offices.

Cash and Cash Equivalents:

Cash and cash equivalents represent demand deposits, money market accounts, and short-term investments classified as held-to-maturity (see Note 2) with original maturities of three months or less.

Financial Instruments:

The carrying amount reported in the balance sheets for cash and cash equivalents, accounts receivable, and accounts payable approximates fair value because of the immediate or short-term maturity of these financial instruments. The carrying amount reported for the bonds payable approximates fair value because the underlying instruments are at variable rates that re-price frequently.

Short-term investments represent re-marketed preferred stocks and municipal bonds classified as available-for-sale securities. Re-marketed preferred stocks are designed to be marketed as money market instruments. These instruments' interest rates reset on a short-term basis to maintain the price of the instruments at par. These instruments may be redeemed on the date the interest rate resets. The fair value of short-term investments is estimated based on quoted market prices (see Note 2). Realized gains or losses are computed under the specific identification method.

Inventory:

Inventory is carried at the lower of cost or market, with cost being determined using the first-in, first-out method.

Property, Plant, and Equipment:

Property, plant, and equipment, which is stated at cost, is depreciated using methods which approximate straight-line depreciation over the estimated useful lives of the assets. Expenditures for repairs and maintenance are charged to expense as incurred; betterments which materially prolong the lives of the assets are capitalized. The cost of assets retired or otherwise disposed of and the related accumulated depreciation are removed from the accounts and the gain or loss on such disposition is included in income.

Long-Lived Assets:

The Company recognizes impairment losses on long-lived assets used in operations when indicators of impairment are present and the undiscounted cash flows estimated to be generated by those assets are less than the assets' carrying values. There were no such losses recognized during 1997, 1996, and 1995.

Research and Development Costs:

Research and development costs are expensed as incurred.

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 revenue and expenses during the reporting period. Actual results could differ from those estimates.

Income Taxes:

The Company utilizes the asset and liability method of accounting for income taxes which requires the establishment of deferred tax liabilities and assets, as measured by enacted tax rates, for all temporary differences caused when the tax bases of assets and liabilities differ from those reported in the financial statements.

Earnings Per Share:

Earnings per common share and earnings per common share assuming dilution are computed in compliance with SFAS No. 128, which the Company adopted December 31, 1997. This statement simplifies the standards for computing earnings per share previously found in APB Opinion No. 15, Earnings per Share, and makes them comparable to international EPS standards. It replaces the presentation of primary EPS with a presentation of basic EPS. The statement requires a computation for earnings per common share and earnings per common share assuming dilution (see Note 13).

Reclassifications:

Certain reclassifications have been made to the 1995 and 1996 financial statements and related footnotes to conform with the 1997

presentation. These reclassifications had no impact on retained earnings or net income.

Recently Issued Accounting Standards:

In June 1997, the Financial Accounting Standards Board (FASB) issued Statement of Financial Accounting Standards (SFAS) No. 130, Reporting Comprehensive Income, which requires the reporting and display of comprehensive income and its components in an entity's financial statements, and SFAS No. 131, Disclosures about Segments of an Enterprise and Related Information, which specifies revised guidelines for determining an entity's operating segments and the type and level of financial information to be required. The Company is required to adopt these standards in 1998. The Company does not expect the impact of these pronouncements to be material.

2. Investments

At December 31, 1997 and 1996, the Company held the following securities as available-for-sale or held-to-maturity recorded at amortized cost which approximates fair value:

1997	
Short-term investments, available-for-sale:	
Municipal Bonds	\$10,333,240
Re-marketed preferred stocks:	
GE Capital preferred asset corporation A series A	5,000,000
Muniyield Fund Auction market preferred series A	5,000,000
VKM Investment Grade Municipal Trust preferred	5,000,000
Nuveen Premium Income Fund preferred series M	2,500,000
Duff & Phelps RP series C	5,000,000
Van Kampen Merritt Municipal Income	5,000,000
Total short-term investments 1997	\$37,833,240
1996	
Short-term investments, available-for-sale:	
Municipal Bonds	\$10,055,930
Re-marketed preferred stocks:	
GE Capital preferred asset corporation A series A	5,000,000
Merrill Lynch preferred series G	5,000,000
Muniyield Fund Auction preferred series A	5,000,000
VKM Investment Grade Municipal Trust preferred	5,000,000
Nuveen Premium Income Fund preferred series A	2,500,000
Total short-term investments in 1996	\$32,555,930

Cash equivalents, held-to-maturity:

Triple A One Plus, zero coupon bonds, matured January 10, 1997	\$ 4,992,889
Receivables Capital, zero coupon bonds, matured January 10, 1997	4,992,889
Barton Corporation, zero coupon bonds, matured January 15, 1997	4,989,248
Three Rivers Funding, zero coupon bonds, matured January 16, 1997	4,988,533
Total cash equivalents in 1996	\$19,963,559

3. Inventory

At December 31, 1997 and 1996 inventory consisted of the following:

	1997	1996
Raw materials	\$24,199,720	\$24,454,251
Work in process	2,565,179	2,963,220
Finished goods	12,604,204	13,375,175
	\$39,369,103	\$40,792,646

4. Property, Plant, and Equipment

Property, plant, and equipment comprised the following at December 31, 1997 and 1996:

Land	\$ 4,263,104	\$ 4,263,104
Building	28,673,642	26,230,470
Construction in progress	3,081,702	2,021,525
Land improvements	7,963,770	7,177,261
Office machinery and equipment	17,184,334	8,338,789
Engineering machinery and equipment	24,534,852	19,577,071
	85,701,404	67,608,220
Less accumulated depreciation	(20,900,272)	(13,637,007)
	\$64,801,132	\$53,971,213

5. Line of Credit

The Company has a \$10,000,000 line of credit at a bank, which bears interest at the rate of 87.5 basis points over the 30 day London inter-bank offered rate. At December 31, 1997 and 1996, the Company had no borrowings against this line. The line of credit expires on May 1, 1998.

6. Alabama State Industrial Development Authority Financing

In conjunction with an expansion of its Huntsville, Alabama facility, the Company was approved for participation in an incentive program offered by the State of Alabama Industrial Development Authority (the "Authority"). Pursuant to such program, on January 13, 1995, the Authority issued \$20,000,000 of its taxable revenue bonds pursuant to such program and loaned the proceeds from the sale of the bonds to the Company. The bonds were originally purchased by AmSouth Bank of Alabama, Birmingham, Alabama (the "Bank"). First Union National Bank of Tennessee, Nashville, Tennessee (the "Bondholder") purchased the original bond from the Bank and made further advances to the Authority in the total amount of \$50,000,000. An Amended and Restated Taxable Revenue Bond (ADTRAN, Inc. Project) Series 1995 was issued and the original financing agreement was amended. The Amended and Restated Bond bears interest, payable monthly, at the rate of 45 basis points over the money market rate of the Bondholder and will mature on January 1, 2020. The Company has agreed to make payments to the Authority in amounts necessary to pay the principal of and interest on the Amended and Restated Bond. Construction on the project began in March 1995 and certain phases were completed by December 31, 1997.

7. Income Taxes

A summary of the components of the provision (benefit) for income taxes as of December 31 is as follows:

	1997	1996	1995
Current:			
Federal	\$21,251,520	\$21,329,522	\$13,896,982
State	1,679,903	2,247,809	968,492
Total Current	22,931,423	23,577,331	14,865,474
Deferred tax provision (benefit)	(313,867)	104,561	(31,910)
Total historical provision for income taxes	22,617,556	\$23,681,892	\$14,833,564

The provision for income taxes differs from the amounts computed by applying the federal statutory rate due to the following:

	1997	1996	1995
Tax provision computed at the federal statutory rate (35% in 1997, 1996 and 1995)	\$21,989,390	\$22,225,629	\$15,501,952
State income tax provision, net of federal benefit	1,091,936	1,461,076	629,520
Federal research credits	(1,248,925)	(151,500)	(815,408)
Permanent differences and other	785,155	146,687	(482,500)
	\$22,617,566	\$23,681,892	\$14,833,564

Temporary differences which create deferred tax assets and liabilities at December 31, 1997 and 1996 are detailed below.

	1997		1996	
	Current	Non-current	Current	Non-current
Property, plant and equipment		(\$2,147,635)		(\$1,602,116)
Accounts receivable	\$ 381,022		\$ 341,584	
Inventory	1,130,083		584,204	
Accruals	947,031		672,962	
Deferred tax asset (liability)	\$2,458,136	(\$2,147,635)	\$1,598,750	(\$1,602,116)

No valuation allowance is deemed necessary by management as the realization of recorded deferred tax assets is considered more likely than not.

8. Stock Split

On April 20, 1995, the stockholders approved the board of directors' recommendation to increase authorized common stock from 30 million shares to 60 million shares, par value \$.01. Following approval by the board of directors, the Company declared a 2-for-1 stock split, payable on May 12, 1995, to stockholders of record on April 27, 1995. All common stock information included in the financial statements, except in the statements of changes in stockholders' equity, gives retroactive effect to this stock split.

9. Operating Leases

The Company leases office space and equipment under operating leases. As of December 31, 1997, future minimum rental payments under the non-cancellable operating leases are approximately as follows:

1998	\$ 529,000
1999	329,000
2000	125,000
2001	45,000
	\$1,028,000

Rental expense was approximately \$657,000, \$851,000, \$447,000 in 1997, 1996 and 1995, respectively.

10. Employee Incentive Stock Option Plan and Director's Stock Option Plan

The Board of Directors of the Company adopted the 1996 Employees Incentive Stock Option Plan (the "1996 Plan") effective February 14, 1996, under which 2,488,100 shares of common stock have been reserved as of December 31, 1997 for issuance to certain employees and officers through incentive stock options and non-qualified stock options. In addition, the Company currently has options outstanding under its 1986 Employee Incentive Stock Option Plan (the "1986 Plan"), which plan expired on February 14, 1996. Options granted under the 1996 Plan or the 1986 Plan become exercisable after one year of continued employment after the date of grant or pursuant to a five year vesting schedule beginning on the first anniversary of the grant date. Expiration dates of options outstanding under the 1996 Plan and the 1986 Plan at December 31, 1997 range from 1998 to 2007.

The Board of Directors of the Company adopted a Director's Stock Option Plan effective October 31, 1995 under which 70,000 shares of common stock have been reserved. The Plan is a formula plan to provide options to non-employee directors of the Company. At December 31, 1997, 36,000 options have been granted under the plan. Expiration dates of options outstanding under the Director's Stock Option Plan at December 31, 1997 range from 2005 to 2007.

Pertinent information regarding the Plans is as follows:

	Number of Options	Range of Exercise Prices	Weighted Average Exercise Price	Vesting Provisions
Options outstanding, December 31, 1994	2,902,574	\$.06 - \$12.53	\$0.49	100% /year
Options granted	84,350	\$22.50 - \$46.25	\$34.86	100% /year
Options cancelled	(1,450)	\$31.75	\$31.75	100% /year
Options exercised	(815,079)	\$.06 - \$3.33	\$0.43	100% /year
Options outstanding, December 31, 1995	2,170,395	\$.06 - \$46.25	\$1.83	100% /year
Options granted	342,000	\$39.75 - \$65.75	\$63.99	20% /year
Options granted	7,950	\$30.50 - \$65.75	\$44.43	100% /year
Options cancelled	(9,050)	\$3.33 - \$65.75	\$61.78	various
Options exercised	(1,307,239)	\$.06 - \$31.75	\$0.60	100% /year
Options outstanding, December 31, 1996	1,204,056	\$.11 - \$65.75	\$20.38	various
Options granted	697,750	\$22.00 - \$42.38	\$25.62	various
Options granted	3,000	\$42.72 - \$42.72	\$42.72	various
Options granted	21,700	\$25.37 - \$45.78	\$32.26	various
Options cancelled	(38,300)	\$22.00 - \$65.75	\$50.89	various
Options exercised	(611,750)	\$.11 - \$31.75	\$.68	various
Options outstanding, December 31, 1997	1,276,456	\$.17 - \$65.75	\$32.24	various

The following table summarizes information about stock options outstanding at December 31, 1997:

Range of Exercise Prices	Number Outstanding 12/31/97	Weighted Average Remaining Contractual Life	Weighted Average Exercise Price	Number Exercisable 12/31/97	Weighted Average Exercise Price
\$0.17-\$2.50	135,831	2.80	\$1.64	135,831	\$1.64
\$3.00-\$22.50	54,225	5.91	\$5.46	52,925	\$5.06
\$25.38-\$25.38	676,450	9.54	\$25.38	0	\$0.00
\$27.50-\$42.38	109,050	7.98	\$36.10	69,850	\$35.76
\$42.72-\$42.72	3,000	9.11	\$42.72	0	\$0.00
\$46.25-\$46.25	3,500	8.03	\$46.25	3,100	\$46.25
\$56.25-\$56.25	5,000	8.54	\$56.25	5,000	\$56.25
\$59.50-\$59.50	3,500	8.56	\$59.50	700	\$59.50
\$63.75-\$63.75	22,500	8.65	\$63.75	4,500	\$63.75
\$65.75-\$65.75	263,400	8.53	\$65.75	53,000	\$65.75
	1,276,456			324,906	

The options above were issued at exercise prices which approximate fair market value at the date of grant. At December 31, 1997, 1,513,250 shares are available for grant under the plans. The Company applies APB Opinion 25 and related Interpretations in accounting for its stock plans. Accordingly, no compensation cost has been recognized related to stock options. Had compensation cost for the Company's stock-based compensation plans been determined based on the fair value at the grant dates for awards under those plans consistent with the method prescribed in SFAS No. 123, the Company's net income and earnings per share would have been reduced to the pro forma amounts indicated below:

	1997	1996	1995
Net income - as reported	\$40,209,272	\$39,819,904	\$29,457,727
Net income - pro forma	\$37,634,225	\$38,018,766	\$28,852,035
Earnings per share - as reported assuming dilution	\$1.02	\$1.01	\$0.75
Earnings per share - pro forma assuming dilution	\$.96	\$.96	\$0.73

The pro forma amounts reflected above are not representative of the effects on reported net income in future years because, in general, the options granted typically do not vest for several years and additional awards are made each year. The fair value of each option grant is estimated on the grant date using the Black-Scholes option-pricing model with the following weighted-average assumptions:

	1997	1996	1995
Dividend yield	0%	0%	0%
Expected life (years)	5	5	5
Expected volatility (range)	47.07% - 49.19%	48.59% - 49.25%	49.40% - 52.37%
Risk-free interest rate (range)	6.01% - 6.69%	5.86% - 7.12%	6.23% - 8.29%

11. Employee Benefit Plan

In March 1990, the Company adopted an incentive savings plan (the "Savings Plan") for all of its employees. The Savings Plan provides certain employment benefits to all eligible employees and qualifies as a deferred arrangement under Section 401(k) of the Internal Revenue Code of 1986, as amended. The Company matches one-third of a participant's contribution, limited to 5% of a participant's income. An employee's interest in the Company's contributions becomes 100% vested at the date participation in the Savings Plan commenced. Charges to operations for the plan amounted to \$717,196, \$547,072, \$415,791 in 1997, 1996 and 1995, respectively.

12. Major Customers

Sales of the Company's transmission and test equipment to the Regional Bell Operating Companies (RBOCs) amounted to approximately 33%, 36% and 40% of total sales during the years ended December 31, 1997, 1996 and 1995, respectively. At December 31, 1997, 1996 and 1995 respectively, 26%, 23% and 36% of the accounts receivable balance consisted of amounts due from RBOCs.

13. Earnings Per Share

A summary of the calculation of basic and diluted earnings per share for the years ended December 31, 1997, 1996 and 1995 is as follows:

For the Year Ended 1997

Income (Numerator)	Shares (Denominator)	Per-Share Amount
--------------------	----------------------	------------------

Basic EPS			
Income available to common stockholders	\$40,209,272	39,201,871	\$1.03
Effect of Dilutive Securities			
Stock Options	0	363,626	
Diluted EPS			
Income available to common stockholders + assumed conversions	\$40,209,272	39,565,497	\$1.02
			For the Year Ended 1996
	Income	Shares	Per-Share
	(Numerator)	(Denominator)	Amount
Basic EPS			
Income available to common stockholders	\$39,819,904	38,603,289	\$1.03
Effect of Dilutive Securities			
Stock Options	0	945,365	
Diluted EPS			
Income available to common stockholders + assumed conversions	\$39,819,904	39,548,654	\$1.01
			For the Year Ended 1995
	Income	Shares	Per-Share
	(Numerator)	(Denominator)	Amount
Basic EPS			
Income available to common stockholders	\$29,457,727	36,984,156	\$0.80
Effect of Dilutive Securities			
Stock Options	0	2,264,945	
Diluted EPS			
Income available to common stockholders + assumed conversions	\$29,457,727	39,249,101	\$0.75

The following options were outstanding during the respective year granted, but were not included in the computation of that year's diluted EPS because the options' exercise price was greater than the average market price of the common shares in the respective year. All options were still outstanding at year end 1997 except for 23,100 options granted in 1996 with an exercise price of \$65.75 which were cancelled during 1997 and 2,500 options granted in 1995 with an exercise price of \$46.25 which were cancelled during 1997.

1997			1996			1995		
Options Granted	Exercise Price	Expiration	Options Granted	Exercise Price	Expiration	Options Granted	Exercise Price	Expiration
1,000	\$37.63	2007	5,000	\$56.25	2005-2006	6,000	\$46.25	2005
7,700	\$37.88	1999-2007	3,500	\$59.50	2005-2006			
6,000	\$42.38	2007	22,500	\$63.75	2005-2006			
3,000	\$42.72	2007	286,500	\$65.75	2005-2006			

14. Summarized Quarterly Financial Data (Unaudited)

The following table presents unaudited quarterly operating results for each of the Company's last eight fiscal quarters. This information has been prepared by the Company on a basis consistent with the Company's audited financial statements and includes all adjustments, consisting only of normal recurring adjustments, that the Company considers necessary for a fair presentation of the data.

Three Months Ended (In thousands, except for per share amounts)

	March 31, 1997	June 30, 1997	September 30, 1997	December 31, 1997
Net sales	\$61,231	\$59,125	\$70,579	\$74,400
Gross profit	31,791	28,632	36,092	38,566
Income from operations	14,258	10,291	16,778	18,726
Net income	9,522	6,980	11,141	12,566
Earnings per common share assuming dilution	0.24	0.18	0.28	0.32
Earnings per common				

share-basic	0.25	0.18	0.28	0.32
	March 31, 1996	June 30, 1996	September 30, 1996	December 31, 1996
Net sales	\$54,544	\$63,305	\$62,635	\$69,637
Gross profit	25,734	29,960	29,419	35,054
Income from operations	12,975	15,802	14,963	17,472
Net Income	8,623	10,340	9,406	11,451
Earnings per common share assuming dilution	0.22	0.26	0.24	0.29
Earnings per common share - basic	0.22	0.27	0.24	0.30

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

No independent certified public accountant of the Company has resigned, indicated any intent to resign or been dismissed as the independent certified public accountant of the Company during the two fiscal years ended December 31, 1997 or subsequent thereto.

PART III

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

Information relating to nominees for director of the Company is set forth under the caption "Election of Directors-Information Regarding Nominees for Director" in the Proxy Statement for the Annual Meeting of Stockholders to be held on April 27, 1998. Such information is incorporated herein by reference. The definitive Proxy Statement will be filed with the Securities and Exchange Commission within 120 days after the Company's fiscal year end. Information relating to the executive officers of the Company, pursuant to Instruction 3 of Item 401(b) or Regulation S-K and General Instruction G(3) of Form 10-K, is set forth at Part I, Item 4(A) of this report under the caption (Executive Officers of the Registrant." Such information is incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION

Information relating to executive compensation is set forth under the caption "Executive Compensation" in the Proxy Statement referred to in Item 10 above. Such information is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

Information relating to ownership of Common Stock of the Company by certain persons is set forth under the caption "Share Ownership of Principal Stockholders and Management" in the Proxy Statement referred to in Item 10 above. Such information is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

Information relating to existing or proposed relationships or transactions between the Company and any affiliate of the Company is set forth under the caption "Compensation Committee Interlocks and Insider Participation" in the Proxy Statement referred to in Item 10 above. Such information is incorporated herein by reference.

PART IV

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

(a) Documents Filed as Part of This Report.

1. Financial Statements

The financial statements of the Company and the related report of independent auditors thereon are set forth under Part II, Item 8 of this report.

Balance Sheets as of December 31, 1997 and 1996

Statements of Income for the years ended December 31,
1997, 1996 and 1995

Statements of Changes in Stockholders' Equity for the
years ended December 31, 1997, 1996 and 1995.

Statements of Cash Flows for the years ended December
31, 1997, 1996 and 1995.

Notes to Financial Statements

2. Financial Statement Schedules

Schedule II - Valuation of Qualifying Accounts

3. Exhibits

The following exhibits are filed with or incorporated by reference in this report. Where such filing is made by incorporation by reference to a previously filed registration statement or report, such registration statement or report is identified in parentheses. The Company will furnish any exhibit upon request to: ADTRAN, Inc., Attn: Investor Relations, P. O. Box 140000, 901 Explorer Boulevard, Huntsville, Alabama 35814. There is a charge of \$.50 per page to cover expenses for copying and mailing.

Exhibit
Number Description

3.1 Certificate of Incorporation, as amended (Exhibit 3.1 to the Company's Registration Statement on Form S-1, No. 33-81062 (the "Form S-1 Registration Statement")).

3.2 Bylaws, as amended (Exhibit 3.2 to the Form S-1 Registration Statement).

10.1 Documents relative to the \$50,000,000 Taxable Revenue Bond, Series 1995 (ADTRAN, Inc. Project) issued by the State Industrial Development Authority, consisting of the following (Exhibit 10.3 to the Company's Annual Report on Form 10-K for the year ended December 31, 1994 (the "1994 Form 10-K")):

(a) Financing Agreement dated January 1, 1995, among the State Industrial Development Authority, a public corporation organized under the laws of the State of Alabama (the "Issuer"), the Company and AmSouth Bank of Alabama, a state banking corporation under the laws of the State of Alabama;

(b) Loan Agreement dated January 1, 1995 (the "Loan Agreement"), between the Issuer and the Company;

(c) Resolution of the Issuer authorizing the issuance of the \$50,000,000 Taxable Revenue Bond, Series 1995 (ADTRAN, Inc. Project);

(d) Specimen Taxable Revenue Bond, Series 1995 (ADTRAN, Inc Project);

(e) Resolution of the Company authorizing the Financing Agreement, the Loan Agreement and the Note;

(f) Specimen Note from the Company to AmSouth Bank of Alabama, dated January 13, 1995;

(g) Pledge Agreement dated January 13, 1995 between AmSouth Bank of Alabama and the Company;

(h) Eighth Amended and Restated Closing Agreement between the Company and AmSouth Bank of Alabama dated March 24, 1997 and effective January 13, 1995; and

(i) Preliminary Agreement dated November 16, 1994 between the Issuer and the Company.

10.2 Master Note for Business and Commercial Loans, dated June 1, 1996 and in the original principal amount of \$10,000,000 by and between the Company and AmSouth Bank of Alabama.

10.3 Tax Indemnification Agreement dated July 1, 1994 by and among the Company and the stockholders of the Company prior to the Company's initial public offering of Common Stock (Exhibit 10.5 to the 1994 Form 10-K).

10.4 Management Contracts and Compensation Plans:

(a) 1996 Employees Stock Incentive Plan (Exhibit 10.4 to 1995 Form 10-K).

(b) 1995 Directors Stock Incentive Plan (Exhibit 10.4 to 1995 Form 10-K).

***23 Consent of Coopers & Lybrand L.L.P.**

***24 Powers of Attorney**

*27 Financial Data Schedule for current period and restated Financial Data Schedules for other periods.

(b) Reports on Form 8-K.

None

*Filed herewith

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) of the Securities Exchange Act of 1934, the Registrant has duly caused this report to be signed on its behalf by the undersigned, thereunto duly authorized on March 30, 1998.

ADTRAN, Inc. (Registrant)

By: /s/ John R. Cooper
John R. Cooper
Vice President-Finance
and 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 indicated on March 30, 1998.

<i>Signature</i>	<i>Title</i>
<i>/s/ Mark C. Smith Mark C. Smith</i>	<i>Chairman of the Board, Chief Executive Officer and Director</i>
<i>Howard A. Thrailkill* Howard A. Thrailkill</i>	<i>President, Chief Operating Officer and Director</i>
<i>Lonnie S. McMillian* Lonnie S. McMillian</i>	<i>Sr. Vice President, Secretary, and Director</i>
<i>O. Gene Gabbard* O. Gene Gabbard</i>	<i>Director</i>
<i>William L. Marks* William L. Marks</i>	<i>Director</i>
<i>Roy J. Nichols* Roy J. Nichols</i>	<i>Director</i>
<i>James L. North* James L. North</i>	<i>Director</i>
<i>/s/ John R. Cooper John R. Cooper</i>	<i>Vice President-Finance and Chief Financial Officer</i>
<i>*By: /s/Mark C. Smith Mark C. Smith as Attorney-in-Fact</i>	

ADTRAN, INC.

INDEX OF EXHIBITS

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 - (c) Resolution of the Issuer authorizing the issuance of the \$50,000,000 Taxable Revenue Bond, Series 1995 (ADTRAN, Inc. Project);
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- *23 Consent of Coopers & Lybrand L.L.P.**
- *24 Powers of Attorney**
- *27 Financial Data Schedule for current period and restated Financial Data Schedules for other periods.

*Filed herewith

REPORT OF INDEPENDENT ACCOUNTANTS

**To the Board of Directors
ADTRAN, Inc.**

Our report on the financial statements of ADTRAN, Inc. has been included on page 25 of this Form 10-K. In connection with our audits of such financial statements we have also audited the related financial statement schedule included on page 44 of this Form 10-K.

In our opinion, the financial statement schedules referred to above, when considered in relation to the basic financial statements taken as a whole, presents fairly, in all material respects, the information required to be included therein.

*/s/ Coopers & Lybrand L.L.P.
COOPERS & LYBRAND L.L.P.
Birmingham, Alabama
January 13, 1998*

SCHEDULE II
VALUATION AND QUALIFYING ACCOUNTS

	Balance at Beginning of Period	Additions	Deductions	Balance at end of Period
Year ended December 31, 1997				
Allowance for Doubtful Accounts	\$ 872,724	\$ 254,366	\$233,701	\$ 893,389
Inventory Reserve	\$ 883,032	\$1,366,031		\$2,249,063
Warranty Liability	\$1,026,156	\$ 409,103		\$1,435,259
Year ended December 31, 1996				
Allowance for Doubtful Accounts	\$ 544,526	\$ 430,789	\$102,591	\$ 872,724
Inventory Reserve	\$ 660,151	\$ 222,881		\$ 883,032
Warranty Liability	\$ 523,027	\$ 503,129		\$1,026,156
Year ended December 31, 1995				
Allowance for Doubtful Accounts	\$ 450,000	\$ 178,952	\$ 84,426	\$ 544,526
Inventory Reserve	\$ 497,825	\$ 162,326		\$ 660,151
Warranty Liability	\$ 280,806	\$ 242,221		\$ 523,027

Consent of Independent Accountants

We consent to the incorporation by reference in the registration statement of ADTRAN, Inc. on Form S-8 of our reports dated January 13, 1998, on our audits of the financial statements and financial statement schedule of ADTRAN, Inc. as of December 31, 1997 and 1996, and for the years ended December 31, 1997, 1996 and 1995, which reports are incorporated by reference in this annual report on Form 10-K.

*/s/ Coopers & Lybrand L.L.P.
Coopers & Lybrand L.L.P.
Birmingham, Alabama*

March 30, 1998

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned constitutes and appoints Mark C. Smith, Howard A. Thrailkill and John R. Cooper, and each of them, his true and lawful attorneys-in-fact and agents, with full power of substitution, for him and in his name, place and stead, in any and all capacities, to sign the Annual Report on Form 10-K of ADTRAN, Inc. for the fiscal year ended December 31, 1997, and any and all amendments thereto, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite or necessary to be done, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents or any of them, or their or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

This 14th day of January, 1998.

/s/ Lonnie S. McMillian
Lonnie S. McMillian

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned constitutes and appoints Mark C. Smith, Howard A. Thrailkill and John R. Cooper, and each of them, his true and lawful attorneys-in-fact and agents, with full power of substitution, for him and in his name, place and stead, in any and all capacities, to sign the Annual Report on Form 10-K of ADTRAN, Inc. for the fiscal year ended December 31, 1997, and any and all amendments thereto, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite or necessary to be done, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents or any of them, or their or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

This 26th day of January, 1998.

/s/ Roy J. Nichols
Roy J. Nichols

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned constitutes and appoints Mark C. Smith, Howard A. Thrailkill and John R. Cooper, and each of them, his true and lawful attorneys-in-fact and agents, with full power of substitution, for him and in his name, place and stead, in any and all capacities, to sign the Annual Report on Form 10-K of ADTRAN, Inc. for the fiscal year ended December 31, 1997, and any and all amendments thereto, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite or necessary to be done, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents or any of them, or their or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

This 21th day of January, 1998.

/s/ William L. Marks
William L. Marks

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned constitutes and appoints Mark C. Smith, Howard A. Thrailkill and John R. Cooper, and each of them, his true and lawful attorneys-in-fact and agents, with full power of substitution, for him and in his name, place and stead, in any and all capacities, to sign the Annual Report on Form 10-K of ADTRAN, Inc. for the fiscal year ended December 31, 1997, and any and all amendments thereto, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite or necessary to be done, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents or any of them, or their or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

This 23th day of January, 1998.

/s/ Mark C. Smith
Mark C. Smith

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned constitutes and appoints Mark C. Smith, Howard A. Thrailkill and John R. Cooper, and each of them, his true and lawful attorneys-in-fact and agents, with full power of substitution, for him and in his name, place and stead, in any and all capacities, to sign the Annual Report on Form 10-K of ADTRAN, Inc. for the fiscal year ended December 31, 1997, and any and all amendments thereto, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite or necessary to be done, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents or any of them, or their or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

This 22th day of January, 1998.

/s/ Howard A. Thrailkill
Howard A. Thrailkill

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned constitutes and appoints Mark C. Smith, Howard A. Thrailkill and John R. Cooper, and each of them, his true and lawful attorneys-in-fact and agents, with full power of substitution, for him and in his name, place and stead, in any and all capacities, to sign the Annual Report on Form 10-K of ADTRAN, Inc. for the fiscal year ended December 31, 1997, and any and all amendments thereto, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite or necessary to be done, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents or any of them, or their or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

This 21th day of January, 1998.

/s/ John R. Cooper
John R. Cooper

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned constitutes and appoints Mark C. Smith, Howard A. Thrailkill and John R. Cooper, and each of them, his true and lawful attorneys-in-fact and agents, with full power of substitution, for him and in his name, place and stead, in any and all capacities, to sign the Annual Report on Form 10-K of ADTRAN, Inc. for the fiscal year ended December 31, 1997, and any and all amendments thereto, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite or necessary to be done, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents or any of them, or their or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

This 21th day of January, 1998.

/s/ O. Gene Gabbard
O. Gene Gabbard

POWER OF ATTORNEY

KNOW ALL MEN BY THESE PRESENTS, that the undersigned constitutes and appoints Mark C. Smith, Howard A. Thrailkill and John R. Cooper, and each of them, his true and lawful attorneys-in-fact and agents, with full power of substitution, for him and in his name, place and stead, in any and all capacities, to sign the Annual Report on Form 10-K of ADTRAN, Inc. for the fiscal year ended December 31, 1997, and any and all amendments thereto, and to file the same, with all exhibits thereto and other documents in connection therewith, with the Securities and Exchange Commission, granting unto said attorneys-in-fact and agents, and each of them, full power and authority to do and perform each and every act and thing requisite or necessary to be done, as fully to all intents and purposes as he might or could do in person, hereby ratifying and confirming all that said attorneys-in-fact and agents or any of them, or their or his substitute or substitutes, may lawfully do or cause to be done by virtue hereof.

This 21th day of January, 1998.

/s/ James L. North
James L. North

ARTICLE 5

This schedule contains summary financial information extracted from the condensed statement of income for the year ended December 31, 1997 and the condensed balance sheet as of December 31, 1997 and is qualified in its entirety by reference to such financial statements.

CIK: 0000926282

NAME: ADTRAN, Inc.

MULTIPLIER: 1

CURRENCY: US Dollar

PERIOD TYPE	12 MOS
FISCAL YEAR END	Dec 31 1997
PERIOD START	Jan 01 1997
PERIOD END	Dec 31 1997
EXCHANGE RATE	1
CASH	45,340,961
SECURITIES	37,833,240
RECEIVABLES	1,250,350
ALLOWANCES	(893,389)
INVENTORY	39,369,103
CURRENT ASSETS	167,400,078
PP&E	85,701,404
DEPRECIATION	(20,900,272)
TOTAL ASSETS	282,401,210
CURRENT LIABILITIES	18,216,500
BONDS	50,000,000
PREFERRED MANDATORY	0
PREFERRED	0
COMMON	393,813
OTHER SE	212,037,075
TOTAL LIABILITY AND EQUITY	282,401,210
SALES	265,334,768
TOTAL REVENUES	265,334,768
CGS	130,253,531
TOTAL COSTS	130,253,531
OTHER EXPENSES	44,973,175
LOSS PROVISION	0
INTEREST EXPENSE	1,838,814
INCOME PRETAX	62,826,828
INCOME TAX	22,617,556
INCOME CONTINUING	40,209,272
DISCONTINUED	0
EXTRAORDINARY	0
CHANGES	0
NET INCOME	40,209,272
EPS PRIMARY	1.03
EPS DILUTED	1.02

ARTICLE 5

RESTATED FINANCIAL DATA SCHEDULE This schedule contains summary financial information extracted from the condensed statement of income for the year ended December 31, 1996 and the condensed balance sheet as of December 31, 1996 and is qualified in its entirety by reference to such financial statements.

CIK: 0000926282

NAME: ADTRAN, Inc.

MULTIPLIER: 1

CURRENCY: US DOLLAR

PERIOD TYPE	12 MOS
FISCAL YEAR END	DEC 31 1996
PERIOD START	JAN 01 1996
PERIOD END	DEC 31 1996
EXCHANGE RATE	1
CASH	44,839,131
SECURITIES	32,555,930
RECEIVABLES	34,698,284
ALLOWANCES	(872,724)
INVENTORY	40,792,646
CURRENT ASSETS	156,235,933
PP&E	67,608,220
DEPRECIATION	(13,637,007)
TOTAL ASSETS	210,207,146
CURRENT LIABILITIES	15,726,131
BONDS	20,000,000
PREFERRED MANDATORY	0
PREFERRED	0
COMMON	387,695
OTHER SE	172,491,204
TOTAL LIABILITY AND EQUITY	210,107,146
SALES	250,120,836
TOTAL REVENUES	250,120,836
CGS	129,953,371
TOTAL COSTS	129,953,371
OTHER EXPENSES	34,308,436
LOSS PROVISION	430,637
INTEREST EXPENSE	(894,657)
INCOME PRETAX	63,501,796
INCOME TAX	23,681,892
INCOME CONTINUING	39,819,904
DISCONTINUED	0
EXTRAORDINARY	0
CHANGES	0
NET INCOME	39,819,904
EPS PRIMARY	1.01
EPS DILUTED	1.01

ARTICLE 5

RESTATED FINANCIAL DATA SCHEDULE This schedule contains summary financial information extracted from the condensed statement of income for the year ended December 31, 1995 and the condensed balance sheet as of December 31, 1995 and is qualified in its entirety by reference to such financial statements.

CIK: 0000926282

NAME: ADTRAN, Inc.

MULTIPLIER: 1

CURRENCY: US DOLLAR

PERIOD TYPE	12 MOS
FISCAL YEAR END	DEC 31 1995
PERIOD START	JAN 01 1995
PERIOD END	DEC 31 1995
EXCHANGE RATE	1
CASH	35,027,609
SECURITIES	24,652,689
RECEIVABLES	30,092,106
ALLOWANCES	544,526
INVENTORY	44,997,195
CURRENT ASSETS	136,522,054
PP&E	29,245,252
DEPRECIATION	0
TOTAL ASSETS	165,767,306
CURRENT LIABILITIES	14,056,329
BONDS	20,000,000
PREFERRED MANDATORY	0
PREFERRED	0
COMMON	374,623
OTHER SE	130,368,688
TOTAL LIABILITY AND EQUITY	165,767,306
SALES	181,478,065
TOTAL REVENUES	181,478,065
CGS	93,006,672
TOTAL COSTS	93,006,672
OTHER EXPENSES	27,259,610
LOSS PROVISION	0
INTEREST EXPENSE	1,105,156
INCOME PRETAX	44,291,291
INCOME TAX	14,833,564
INCOME CONTINUING	29,457,727
DISCONTINUED	0
EXTRAORDINARY	0
CHANGES	0
NET INCOME	29,457,727
EPS PRIMARY	0.32
EPS DILUTED	0.32

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