AEROSONIC CORP /DE/
Form 10-K
April 06, 2004

SECURITIES AND EXCHANGE COMMISSION

Washington, D.C. 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d) of

The Securities Exchange Act of 1934

For the Fiscal Year Ended January 31, 2004

Commission File Number 1-11750

AEROSONIC CORPORATION

(Exact name of registrant as specified in its charter)

Delaware

74-1668471

(State or other jurisdiction of incorporation or organization)

(I.R.S. Employer Identification No.)

1212 North Hercules Avenue

Clearwater, Florida 33765

(Address of principal executive offices and Zip Code)

Registrant s telephone number, including area code: (727) 461-3000

Securities registered pursuant to Section 12(b) of the Act:

Title of Each Class

Name of Each Exchange on Which Registered

Common Stock, $.40 par value

American Stock Exchange

Securities registered pursuant to Section 12(g) of the Act:

None.

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 S   No £

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act).

Yes £   No S

The aggregate market value of the voting stock held by non-affiliates of the registrant was approximately $24,845,000 as of July 31, 2003 based upon the closing price of the Common Stock on the American Stock Exchange (**Amex**) on that date, and approximately $20,791,000 as of March 31, 2004, based upon the closing price of the Common Stock on the Amex on that more recent date.

As of March 31, 2004, the issuer had 3,921,019 shares of Common Stock outstanding.

Documents Incorporated by Reference: None.

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TABLE OF CONTENTS

AEROSONIC CORPORATION

FORM 10K

YEAR ENDING JANUARY 31, 2004

Table of Contents

PART I

THIS REPORT CONTAINS CERTAIN FORWARD-LOOKING STATEMENTS WITHIN THE MEANING OF SECTION 27A OF THE SECURITIES ACT OF 1933, AS AMENDED, AND SECTION 21E OF THE SECURITIES EXCHANGE ACT OF 1934, AS AMENDED, WHICH ARE INTENDED TO BE COVERED BY THE SAFE HARBORS CREATED THEREUNDER. FORWARD-LOOKING STATEMENTS CAN BE IDENTIFIED BY THE USE OF FORWARD-LOOKING TERMINOLOGY SUCH AS MAY, WILL, SHOULD, EXPECT, ANTICIPATE, ESTIMATE, CONTINUE, PLANS, INTENDS AND WORDS SIMILAR IMPORT. ALTHOUGH THE COMPANY BELIEVES THAT THE ASSUMPTIONS UNDERLYING THE FORWARD-LOOKING STATEMENTS CONTAINED HEREIN ARE REASONABLE, ANY OF THE ASSUMPTIONS COULD BE INACCURATE. THEREFORE, THE COMPANY S ACTUAL RESULTS COULD DIFFER MATERIALLY FROM THE RESULTS ANTICIPATED IN THESE FORWARD-LOOKING STATEMENTS. ADDITIONALLY, ACTUAL RESULTS MIGHT BE AFFECTED BY CERTAIN FACTORS SET FORTH HEREIN IN MANAGEMENT S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS. THE COMPANY UNDERTAKES NO OBLIGATION TO UPDATE PUBLICLY ANY FORWARD-LOOKING STATEMENTS, WHETHER AS A RESULT OF NEW INFORMATION, FUTURE EVENTS OR OTHERWISE.

Significant Events. On March 17, 2003, Aerosonic Corporation (the **Company**) issued a press release stating that it had initiated an investigation into financial and accounting irregularities involving revenue and inventory reported during prior periods. On May 19, 2003, J. Mervyn Nabors resigned as the Company s Chairman and ceased all day-to-day involvement in management activity. Prior to this event, David A. Baldini was appointed President of the Company (on November 14, 2002) to replace Mr. Nabors in that capacity, and Gary E. Colbert was appointed Chief Financial Officer (on January 14, 2003), to replace Eric J. McCracken in that capacity, who had resigned in October 2002. Item 3 and Item 7 of this report include discussions of both an investigation by the U.S. Securities and Exchange Commission regarding the above referenced financial and accounting issues and a halt of trading in the Company s Common Stock imposed by the American Stock Exchange on September 25, 2003 that continued until November 25, 2003. Such investigation and trading halt also are discussed in several other portions of this report.

On October 31, 2003, the Company filed its Annual Report on Form 10-K for the fiscal year ended January 31, 2003 (the **2003 Form 10-K**). As discussed in the Company s 2003 Form 10-K, as a result of the Company s investigation into financial and accounting irregularities, the Company restated its financial statements for the fiscal years ended January 31, 1999, 2000, 2001 and 2002, and restated its previously reported unaudited financial information for the first three quarters of the fiscal year ended January 31, 2003. The Company s 2003 Form 10-K contains important information regarding such restatements, the contributing causes (including misstatements, falsification of inventory records, improper adjustments for obsolete and slow moving inventory, improper revenue recognition, improper fixed asset capitalization and errors in the application of Staff Accounting Bulletin No. 101 and generally accepted accounting principles) and the impact thereof on the Company and its operations and affairs.

Item l. Business.

The Company is a Delaware corporation formerly known as Instrument Technology Corporation (**ITC**). ITC, which was incorporated in 1968, was the surviving corporation of a merger, in 1970, with Aerosonic Corp., a Florida corporation (**Aerosonic Florida**). Aerosonic Florida, which was incorporated in 1957, ceased to exist as a separate corporation as a result of the merger. Following the merger, ITC changed its name to Aerosonic Corporation.

In January 1993, the Company acquired Avionics Specialties, Inc., a Virginia corporation (**Avionics**), from Teledyne Industries, Inc. (**Teledyne**). Prior to the acquisition, Avionics had been a division of Teledyne. Since the acquisition, Avionics has been maintained as an operating and wholly owned subsidiary of the Company.

As used herein, unless the context requires otherwise, references to Aerosonic, the Company, we or our include Aerosonic Corporation and its operating subsidiary, Avionics.

Table of Contents

The Company is principally engaged in one business segment, which is the manufacture and sale of aircraft instruments. The Company consists of four operating divisions in three locations. The divisions are: the Clearwater, Florida Instrument Division (**Clearwater Instruments**), the Wichita, Kansas Division (**Kansas Instruments**), Avionics in Earlysville, Virginia, and the Clearwater, Florida Precision Component Division (**Precision Components**).

Clearwater Instruments primarily manufactures altimeters, airspeed indicators, rate of climb indicators, microprocessor controlled air data test sets, and a variety of other flight instrumentation. Kansas Instruments is the source inspection location for our Wichita customers and is the primary location for Clearwater Instruments repair business. Avionics maintains three major product lines in the aircraft instrument segment: (1) angle of attack stall warning systems; (2) integrated multifunction probes, which are integrated air data sensors; and (3) other aircraft sensors and monitoring systems. In August 1998, the Company formed Precision Components as a new division to perform high volume precision machining of mechanical components, which was not significant to operations in the fiscal years ended January 31, 2004, 2003 or 2002.

The Company has a January 31 fiscal year end. Accordingly, all references in this Annual Report on Form 10-K to a fiscal year mean the fiscal year ended on January 31 of the referenced year; for example, references to fiscal year 2004 mean the fiscal year ended January 31, 2004.

Industry

The current market niche for Aerosonic has been and will continue to be the design, development and supply of primary flight control systems components and instruments. These include altimeters, airspeed indicators, angle of attack, stall prevention systems, and air data measurement systems. All of these aircraft products are critical to aircraft operations, performance and safety.

With the cost of both commercial and military aircraft rising, the number of new aircraft programs continues to decrease in both the number of programs and quantity of aircraft being built. Increasing value to the customer has become extremely important to sustaining Aerosonic s market position as well as the Company s market share.

The military original equipment manufacturers (**OEM**), such as BAE Systems LTD, Bell Helicopter Textron Inc., Korea Aerospace Industries, Lockheed Martin Corporation (**Lockheed**), Sikorsky Aircraft Corporation, The Boeing

Company (**Boeing**), and others, have increased their reliance on their subcontractors to carry a greater share of the aircraft responsibility, including system requirements, hardware design, and physical and electrical interfaces. This increased responsibility has allowed Aerosonic to develop a greater technical capability for serving its customer base. The evolution of this role has taken Aerosonic to a dominant position in its business segment within the military aircraft market.

This increased technical capability has also positioned the Company to push further into the commercial aircraft market with our new technologies. New development programs with Gulfstream Aerospace Corporation, Learjet Inc., and Raytheon Aircraft Company will allow us to increase and protect our market share.

The Company continues as an industry leader in the manufacturing of mechanical instruments. These products are used for both primary flight data as well as standby redundant instruments in cockpits that use electronic displays for primary flight data. As cockpit panel space becomes more valuable in the new age of glass displays, the Company has maintained a strong position with OEMs as a premier supplier of quality mechanical instruments in both the military and commercial aircraft marketplace.

Strategy

The Company s goal is to continue to reposition its products for profitable growth and maintain dominance within niche markets. The Company intends to focus on the development of profitable long-term contracts. New aircraft cockpits increasingly are being developed through strategic alliances with market leaders. The Company is well positioned to take advantage of these strategic alliances. An increase in sales volume will depend upon new product introduction and further penetration of existing markets. The Company continues to hold a competitive advantage derived from its philosophy of vertical integration. The Company is substantially vertically integrated in its manufacturing and distributing activities.

Table of Contents

Products and Distribution

The Company s products are sold to manufacturers of commercial and private aircraft, both domestic and foreign, and the U.S. military services. For the fiscal year ended January 31, 2004, approximately 48% of the Company s total sales were to the private sector and 52% to United States military services. For the fiscal year ended January 31, 2003, approximately 60% of the Company s total sales were to the private sector and 40% to United States military services. This shift in volume is due to the increase in development activity for the F-35 development program as well as the ramp-up of production for the 32A contract, both of which are military applications. Domestic sales of the Company s products are made to many different commercial (non-government) customers, and there is an increasing movement toward development contracts for future applications. For the fiscal year ended January 31, 2004, sales related to development programs accounted for approximately 20% of net sales, or $6.3 million, an increase of $2.2 million from the fiscal year ended January 31, 2003, where such sales represented 16% of net sales. During fiscal year 2004, there were two commercial customers, Lockheed and Boeing, who represented 25% and 11%, respectively, of total revenues. A substantial amount of the business related to these customers is related to contracts each customer has with the U.S. Government. If the Company lost either of these customers, such a loss would have a material adverse effect on the Company s results of operations.

In addition, the Company sells its products to customers outside of the U.S. The aggregate percentage of international sales to overall sales was 13%, 17%, and 28% for the fiscal years ended January 31, 2004, 2003 and 2002, respectively.

Most of the Company s instrument sales are made directly through Company employees to OEMs or to the United States military, with the Company s remaining sales being made through other customers (who resell to aircraft operators).

The Company produces a full line of both three-inch and two-inch mechanical and electro-mechanical cockpit instruments. These instruments require no backup power, as they transfer valuable flight data to the pilot using only air pressure (from aircraft probes) as a power source. The Company also manufactures a state of the art air data test set used by aircraft OEMs, repair centers and the U.S. military.

The Company also produces an integrated multifunction probe (**IMFP**), which is a combination of existing technologies, including the angle of attack/air data sensing probe and pressure sensing electronics. This integrated approach to providing aircraft air data reduces the customers system complexity with respect to aircraft troubleshooting and logistics support, increases reliability, and decreases system costs.

The Company has completed a redesign of the basic components of the angle of attack (**AOA**)/stall warning product line. The combined stall warning transmitter merges existing technologies of AOA and stall warning into a single technical standard order C54 stall warning transmitter. This combined instrument has dramatically reduced the system weight and increased the system reliability.

The Company is currently developing a new product line that includes microprocessor-based sensors with an analog pointer display that have been selected by Cessna to be standby units on their new Mustang light jet program. The Microprocessor-based Standby Airspeed indicator and the Microprocessor-based Standby Altimeter indicator have completed their preliminary design review. These indicators combine the accuracy, robustness and the long term mean time before failure of electronic sensing presented with a pilot familiar analog pointer display. Initial deliveries of test instruments will be made during the second quarter of fiscal 2005.

Precision Components operates as a high precision machining operation. Precision Components products include a variety of mechanical parts primarily related to the optics industry. Some of the products include the mechanical components for rifle scopes, printing presses, microscopes and tank gun sights.

Customers

The Company primarily markets its products to OEMs, particularly manufacturers of corporate and private jets, and to contractors of military jets. Customers include, among others, the U.S. Government and a majority of the OEMs throughout the world. The Company also markets its products to private aircraft owners through its network of authorized resellers.

Table of Contents

Contracts

The Company s contracts are normally for production or development. The Company s production contracts are typically fixed-price over a two to five year period, and the industry trend for such contracts is moving away from five year contracts and toward two year contracts. The Company also secures purchase orders from customers for product sales in the normal course of business that are binding contracts upon acceptance of the terms of orders by the Company.

Fixed-price contracts provide for a firm fixed price on a variety of products and quantities of those products. These contracts allow the Company to negotiate better overall prices that fit into customers production programs. These long-term commitments also allow the Company to capitalize on quantity based price reduction for raw materials. Under the firm fixed-price contracts, the Company agrees to perform for an agreed-upon price. Accordingly, the Company derives benefits from cost savings, but bears the risk of cost overruns.

Development contracts provide resources for technology advancement necessary for development of various products. The Company negotiates for and generally receives payments from customers based upon milestones that correlate with the costs incurred. Early in our fiscal year ended January 31, 2003, we were notified that a variation of the IMFP had been selected for use on the Joint Strike Fighter. Development of this system continued through fiscal year 2004 and is expected to conclude in fiscal year 2006. During the fiscal year ended January 31, 2004, the Company was awarded a development contract to provide the stall prevention system for the new G150 business aircraft being developed jointly by Gulfstream and Israeli Aircraft Industries.

As discussed in Note 12 to the Financial Statements, on February 5, 2004 the Company sold its Engine Vibration Monitoring System (**EVMS**) product line inventory to Beran Instruments Limited, a U.K. company. This sale, which also includes the U.S.-registered trademark EVMS , will allow the Company to concentrate on core technology developments in its other product lines.

In accordance with normal practice, most of our contracts with the U.S. Government and its agencies and departments are subject to partial or complete termination at any time at the government s convenience. Our government contracts generally contain provisions providing that in the event of a termination for convenience by the government, the Company shall have the right to recover allowable costs incurred to the date of termination as well as a proportionate share of the profit on the work completed, consistent with U.S. Government contract regulations and procedures.

Sales and Marketing

The Company has generally focused sales efforts on government and military entities, OEMs and resellers. The Company intends to increase sales efforts with respect to retrofit, modifications and repair programs.

Due to the system impact of its components, the Company is involved at a very early stage with the aircraft manufacturers engineers to integrate the components into the aircraft design. All of the Company s component instruments are integrated into the aircraft in order to help maintain the safe operation of the airplane.

At January 31, 2004, the Company s backlog of firm orders was approximately $27,414,000, a decrease of approximately $7,364,000 when compared to backlog as of January 31, 2003. The amount of backlog that is deliverable within twelve months was approximately $22,446,000 at January 31, 2004, a decrease of approximately $1,993,000 when compared to January 31, 2003. The majority of the reduction in the overall backlog is due to work that was completed on the Joint Strike Fighter development program during the 2004 fiscal year. The foregoing backlog amounts represent firm orders only and do not include current contract options. Such orders, however, may be subject to rescheduling and/or cancellation.

In January 2001, the Company moved its repair operations to the Kansas facility. The Company believes this improves its ability to provide prompt and effective repair and upgrade service.

Table of Contents

Government Regulation

The manufacture and installation of the Company s products in aircraft owned and operated in the U.S. are governed by U.S. Federal Aviation Administration (**FAA**) regulations. The regulations that have the most significant impact on the Company are the Technical Standard Order (**TSO**) and Type Certificate (**TC**) or Supplemental Type Certificate (**STC**) certifications. TSO outlines the minimum standards that a certain type of equipment has to satisfy to be TSO certified. Many OEMs and retrofitters prefer TSO-certified aviation equipment because it acts as an industry-wide stamp of approval. The Company also sells its products to European and other non-U.S. OEMs, which typically require approval from the Joint Aviation Authorities (**JAA**).

The Company has received TSO approval on over 400 different instruments, as well as 70 STCs. Most new instruments qualify for approval based on similarity. This provides a significant advantage to the Company and its customers by reducing the time required obtaining TSO approval on new instruments. The Company also has many instruments with JAA approval.

Quality Assurance

Product quality is critical in the aviation industry. The Company strives to maintain the highest standards within each of its divisions.

The Company is ISO 9001 certified. ISO 9001 standards are an international consensus on effective management practices for ensuring that a company can consistently deliver its products and related services in a manner that meets or exceeds customer quality requirements. ISO 9001 standards outline the minimum requirements a quality system must meet to achieve this certification.

As an ISO 9001-certified manufacturer, the Company can represent to its customers that it maintains high quality industry standards in the education of employees and the design and manufacture of its products. In addition, the Company s products undergo extensive quality control testing prior to being delivered to customers. As part of the Company s quality assurance procedures, the Company maintains detailed records of test results and quality control processes.

Patents and Licenses

The Company has patents on certain commercial and military products such as air data probes. The Company also has certain registered trademarks. The patents and intellectual property portfolio, in the aggregate, is valuable to operations, however the Company does not believe the business, as a whole, is materially dependent on any single patent, trademark or copyright.

Research and Development

The Company expended approximately $167,000, $745,000 and $1,083,000 in research and development costs for potential new products and enhancements during the fiscal years ended January 31, 2004, 2003 and 2002, respectively. The reduction in expenditures in 2004 is a result of the redirection of resources toward specific customer contracts where such charges are classified as cost of sales. Approximately 28 engineers working at the Company, on a full-time or part-time basis, are involved in these activities.

The Company continued its various development efforts during fiscal year 2004 for both military and commercial applications, the most notable of which is the F-35 Joint Strike Fighter program. The Company plans to continue its design efforts in the satisfaction of its existing contractual obligations as well as its internal development of products for future customer applications.

Competition

The markets for the Company s products are highly competitive and characterized by several industry niches in which a number of manufacturers specialize. The Company manufactures a larger variety of aircraft instruments than its competitors who, in most instances, compete with the Company on no more than a few types of aircraft instruments.

Table of Contents

The Company believes that the principal competitive factors are price, development cycle time, responsiveness to customer preferences, product quality, technology, reliability and variety of products. Management believes that the Company s significant and long-standing customer relationships reflect its ability to compete favorably with respect to these factors.

Manufacturing, Assembly and Material Acquisition

The Company s manufacturing processes (except for certain electronic products) includes the manufacture of all principal components and subassemblies for the instruments, the assembly of those components, and the testing of products at various stages in the manufacture and assembly process.

The Company manufactures, or has the capability to manufacture, principally all components and subassemblies for its instruments. Raw materials, such as glass lenses, raw metals and castings, generally are available from a number of sources and in sufficient quantities to meet current requirements, subject to normal lead times. The Company believes that retaining the ability to completely manufacture the instruments allows the Company the flexibility to respond to customers quickly and control the quality of its products.

When appropriate, less critical component parts are purchased under short and long term supply agreements. These purchased parts are normally standard parts that can be easily obtained from a variety of suppliers. This allows the company to lower overhead expenses and maintain control required to meet the exacting tolerances demanded in the industry.

Employees

As of the fiscal year ended January 31, 2004, the Company employed 269 employees in its business operations. This consisted of 122 Clearwater Instrument employees, 15 Kansas Instrument employees, 125 Avionics employees and 7 Precision Component employees. The Company s future success depends on the ability to attract, train and retain quality personnel. The Company s employees are not represented by labor unions and management considers its relations with its employees to be good.

Available Information

The Company s Annual Reports on Form 10-K, its Quarterly Reports on Form 10-Q, any Current Reports on Form 8-K, and any amendments to these reports are available on the Company s Internet website address www.aerosonic.com as soon as reasonably practicable after such materials are filed with or furnished to the SEC. The website address is intended to be an inactive textual reference only and none of the information contained on the Company s website is part of this report nor is incorporated by reference herein.

The Company s reports filed with the SEC also are available from the SEC, and can be obtained by accessing the SEC website at www.sec.gov/edgar.shtml or writing to the following address:

U.S. Securities and Exchange Commission

450 5th Street N.W.

Washington D.C. 20222

No charge is assessed for any access, viewing, printing or downloading reports from the Company s Internet website. Alternatively, if a paper copy of any such report (without exhibits) is desired, please write to Gary E. Colbert, Chief Financial Officer, Aerosonic Corporation, 1212 North Hercules Avenue, Clearwater, Florida 33765, and a copy of such requested report will be provided, free of charge.

Table of Contents

Item 2. Properties.

The following table sets forth the locations and general characteristics of the Company s principal properties:

Location		**Approximate Number of Square Feet of Factory and Office Area**
Clearwater, Florida	...	90,000
Wichita, Kansas	...	7,500
Charlottesville, Virginia	...	53,000

All of the Company s properties are well maintained, fully occupied by the Company and suitable for the Company s present level of production and usage. All locations operate one shift, five days a week. As of January 31, 2004, the Clearwater, Florida property, which is used by both Clearwater Instruments and Precision Components, was mortgaged in accordance with an Industrial Revenue Bond executed in 1987. Subsequent to January 31, 2004, this mortgage was refinanced with Wachovia Bank N.A. (See Notes 7 and 12, **Financial Statements**)

The Earlysville, Virginia property was purchased from Teledyne Industries in April 1994. The property consists of a 53,000 square foot manufacturing facility on approximately 12 acres of land. As of January 31, 2004, the Virginia property was mortgaged by a long term note with SunTrust Bank N. A. Subsequent to January 31, 2004, this mortgage was repaid when the Company refinanced its debt with Wachovia Bank N.A. (See Notes 7 and 12, **Financial Statements**)

Item 3. Legal Proceedings.

SEC Formal Investigation

The Company is the subject of a Formal Order of Investigation issued by the U.S. Securities and Exchange Commission (the **SEC**) on May 13, 2003 with respect to potential violations of the federal securities laws in connection with the accounting misstatements and contributing causes disclosed by the Company in press releases dated March 17 and May 22, 2003 and further discussed in the Company s annual report for the fiscal year ended January 31, 2003 and the subsequent quarterly reports on Form 10-Q, which the Company brought to the attention of the SEC in conjunction with management s internal investigation, and other potential issues. The Company continues to cooperate fully with the SEC.

Matters Relating to the American Stock Exchange

On July 30, 2003, the Company received a deficiency letter from the American Stock Exchange (**Amex**) informing the Company that it was not in compliance with the Amex continued listing standards. The deficiency letter cited, among other things, the Company s disclosures regarding underlying causes of its financial misstatements and the late filing of the Company s 2003 Form 10-K and the Form 10-Q for the quarter ended April 30, 2003. On August 20, 2003, the Company provided a response, which included a plan to achieve compliance with applicable Amex rules. On September 24, 2003, the Company submitted an amended compliance plan to the Amex, which included an undertaking by the Company to file its 2003 Form 10-K no later than October 31, 2003 and to file both its April 30 and July 31, 2003 Forms 10-Q no later than November 15, 2003. On October 8, 2003, the Amex accepted the Company s compliance plan, as amended, and informed the Company that its listing on the Amex would be continued with the understanding that the Company would implement its compliance plan within the timeframe specified in the plan.

On September 25, 2003 (prior to the October 8, 2003 Amex acceptance of the Company s compliance plan), the Amex halted trading in the Company s Common Stock due to the lack of current financial information concerning the Company. Trading in the Company s Common Stock was resumed by the Amex on November 25, 2003, after the October 31, 2003 filing of the Company s 2003 Form 10-K and the November 20, 2003 filing of its Forms 10-Q for April 30 and July 31, 2003.

Table of Contents

Additional Proceedings and Matters

A claim has been asserted by Miriam Frank, on behalf of the estate of the Company s former President and Chairman Herbert J. Frank, for indemnification with respect to fines paid and legal expenses incurred by Mr. Frank in connection with an investigation by the United States government of the unauthorized use of foreign-manufactured components in aircraft clocks manufactured and sold by the Company (the **Government Action**) and for which Mrs. Frank claims the Company was obligated to indemnify Mr. Frank. As of the date of this report, Ms. Frank has not clarified the amount of her claim to the Company and has not provided the Company with information sufficient to determine the amount of the alleged loss. However, Mrs. Frank has submitted a November 1996 letter addressed to the Company from counsel to the Estate of Herbert J. Frank asserting an indemnification claim of approximately $350,000 plus interest, consisting of costs and expenses resulting from the Government Action. In view of the available information, the Company believes that any obligation to pay the claim is remote.

Securities Class Action Litigation

On November 12, 2003, a class action lawsuit was filed in the United States District Court for the Middle District of Florida by Sebastian P. Gaeta, individually and on behalf of all other similarly situated (the **Gaeta Suit**), against the Company, PricewaterhouseCoopers LLP, the Company s former independent accountant, J. Mervyn Nabors, a former director and former President and CEO of the Company, Eric J. McCracken, a former Chief Financial Officer of the Company, and Michael T. Reed, a former Controller of the Company. The action alleges violations of Sections 10(b) and 20(a) of the Securities Exchange Act of 1934 and Rule 10b-5 promulgated under that act, including, among other things, that the Company made materially false statements concerning the Company s financial condition and its future prospects. The plaintiff alleges that he suffered damages as the result of his purchase and sale of the Company s Common Stock during the asserted Class Period from November 13, 1998 through March 17, 2003. Subsequently Mr. Gaeta was joined by other named plaintiffs in this action to form what is referred to as the **Miville Group** . The action seeks compensatory and other damages, and costs and expenses associated with the litigation.

Shortly after the Gaeta Suit was filed, two other putative class actions (the **"Pratsch Suit"** and **"Suarez Suit"**) were filed against the same defendants as in the Gaeta Suit and predicated upon alleged violations of the same securities laws, asserting that plaintiffs purchased the Company s stock at artificially inflated prices during the Class Period and have been damaged thereby. The Pratsch Suit and Suarez Suit assert a Class Period from May 3, 1999 through March 17, 2003. At a February 27, 2004 hearing, plaintiffs in the Suarez Suit voluntarily withdrew their complaint. On February 27, 2004, the Court entered an order consolidating the Gaeta Suit and Pratsch Suit into one case entitled "In re Aerosonic Corporation Securities Litigation," appointing Lead Plaintiffs (the "Miville Group"), approving the selection of Lead Plaintiffs Counsel (Berger & Montague P.C.), and giving Lead Plaintiffs until April 27, 2004 to file an amended and consolidated class action complaint. The outcome of the consolidated class action lawsuit cannot be adequately determined, and the impact upon the Company cannot be assessed, at this time. Any resolution of such litigation could have a material adverse effect upon the Company s financial position, results of operations, and cash flow.

In addition to the foregoing, from time to time, the Company is involved in certain claims and legal actions arising in the ordinary course of business. In the opinion of management, at this time, there are no claims or legal actions that will have a material adverse effect on the Company s financial position, results of operations, or liquidity.

Item 4. Submission of Matters to a Vote of Security Holders.

The Company held its annual meeting of shareholders for fiscal year 2003 on December 18, 2003, at which time shareholders elected six directors to serve on the six member board, until the next annual meeting. The six elected directors, each of whom had been serving as a director prior to the meeting, include: David A. Baldini, Charles M. Foster, Robert J. McGill, William C. Parker, P. Mark Perkins and David M. Vosen.

Table of Contents

The election of directors was the only matter voted upon at the annual meeting and 3,715,532 shares were voted at the meeting. Mr. Baldini received a vote of 3,600,443 shares with 115,089 shares withheld, Mr. Foster received a vote of 3,626,859 shares with 88,673 shares withheld, Mr. McGill received a vote of 3,626,859 shares with 88,673 shares withheld, Mr. Parker received a vote of 3,224,257 shares with 491,275 shares withheld, Mr. Perkins received a vote of 3,626,859 shares with 88,673 shares withheld and Mr. Vosen received a vote of 3,626,871 shares with 88,661 shares withheld. There were 0 abstentions.

Item 5. Market for Registrant s Common Stock and Related Security Holder Matters.

The Company s Common Stock is listed on the American Stock Exchange under the symbol AIM . As discussed above in Item 3. Legal Proceedings Matters Relating to the American Stock Exchange, on September 25, 2003, the Amex halted trading in the Company s Common Stock due to the lack of current financial information concerning the Company. The Amex permitted trading to resume on November 25, 2003, after the Company brought its reporting obligations up to date by filing its 2003 Form 10-K on October 31, 2003 and its Forms 10-Q for the quarters ended April 30 and July 31, 2003 on November 20, 2003.

The range of high and low sales prices as reported by the Amex for each of the quarters of the fiscal years ended January 31, 2004 and January 31, 2003 is as follows:

Fiscal Year Ended January 31, 2004

Quarter				**Price**			**Price**
1		High	$	15.45	Low	$	9.40
2	..	High	$	10.48	Low	$	8.00
3	..	High	$	10.80	Low	$	9.65
4	..	High	$	12.30	Low	$	7.00

Fiscal Year Ended January 31, 2004

Quarter				**Price**			**Price**
1		High	$	28.00	Low	$	18.85
2	..	High	$	29.50	Low	$	22.50

3	..	High	$	24.75	Low	$	21.30
4	..	High	$	21.50	Low	$	13.51

During those same periods, no cash dividends were paid. The Company does not anticipate or intend on paying a dividend in the foreseeable future. Rather, the Company intends to retain its earnings to finance the development and expansion of its business. Additionally, covenants in our long-term debt documents impose significant restrictions on our ability to pay dividends. Any future payment of any dividends on the Company s Common Stock and the amount thereof will depend on the Company s earnings, financial requirements, compliance with the above described covenants, and other factors deemed relevant by the Company s Board of Directors.

As of March 12, 2004, the Company s outstanding shares of Common Stock were owned by approximately 1,440 shareholders of record.

The following table sets forth information with respect to the Company s equity compensation plans.

Plan Category	**Number of securities to be issued upon exercise of outstanding options, warrants and rights**	**Weighted-average exercise price of outstanding options, warrants and rights**	**Number of securities remaining available for future issuance under equity compensation plans (excluding those reflected in column (a))**
	(a)	**(b)**	**(c)**
Equity compensation plans approved -by security holders	**-----**	**N/A**	**N/A**
Equity compensation plans not approved by security holders	**-----**	**N/A**	**N/A**
Total	**-----**	**N/A**	**N/A**

Table of Contents

In 1993, the Company s Board of Directors and stockholders approved the Aerosonic Corporation 1993 Incentive Stock Option Plan, pursuant to which the Company was authorized to issue options for up to 300,000 shares of Common Stock to its employees (including officers), directors and consultants. Following the adoption of the plan by the Company s Board of Directors, options were granted to a limited number of employees, all of which have been exercised or have expired pursuant to their terms. As of March 2003, no additional options may be granted pursuant to the terms of the plan. The Company does not have any other equity compensation plans or arrangements.

Item 6. Selected Financial Data.

The following selected financial data as of January 31, 2004 and 2003 and for each of the three years in the period ended January 31, 2004 have been derived from the Company s audited Consolidated Financial Statements included elsewhere herein. The selected financial data as of January 31, 2002 and 2001 have been derived from audited financial information not separately presented herein. The selected financial data as of January 31, 2000 has been derived from unaudited financial information.

	Years Ended January 31,				
	2004	2003	2002	2001	2000(1)
	$	$	$	$	$
Revenue	.31,113,000	25,672,000	26,686,000	23,528,000	23,271,000
Cost of sales	(22,494,000)	(16,783,000)	(17,441,000)	(15,381,000)	(18,812,000)
Gross Margin	8,619,000	8,889,000	9,245,000	8,147,000	4,459,000
Selling, general and administrative expenses	(8,421,000)	(7,776,000)	(8,082,000)	(8,130,000)	(7,538,000)
Operating income (loss)	198,000	1,113,000	1,163,000	17,000	(3,079,000)
Other income (expense) ..	(121,000)	(129,000)	(431,000)	(349,000)	(418,000)
Income (loss) from before income taxes	.. 77,000	984,000	732,000	(332,000)	(3,497,000)
Income tax benefit	465,000	22,000	(21,000)	(10,000)	366,000

(expense)					
Net income (loss)	$ 542,000	$ 1,006,000	$ 711,000	$ (342,000)	$ (3,131,000)
Basic and diluted earnings per share	$ .. 0.14	$ 0.26	$ 0.18	$ (0.09)	$ (0.80)
Total Assets	$ 18,985,000	$ 17,269,000	$ 16,093,000	$ 15,522,000	$ 17,509,000
Long term debt (2)	$ 2,416,000	$ 3,411,000	$ 4,374,000	$ 5,404,000	$ 4,293,000

(1)

During the preparation of the Company s Annual Report on Form 10-K for the fiscal year ended January 31, 2003, the Company was unable to determine the full extent of adjustments that would be necessary to a fair presentation of the restated financial information included herein for the fiscal year ended January 31, 2000 due to unavailability of certain accounting records for periods predating the fiscal year ended January 31, 2001. See Note 2 to Consolidated Financial Statements in the Company s Annual Report on Form 10-K for the fiscal year ended January 31, 2003 for a discussion of the restatement of the Company s results for the fiscal years ended January 31, 1999, 2000, 2001, 2002.

(2)

Long term debt is defined as all outstanding long term debt and capital leases, including current maturities.

Item 7. Management s Discussion and Analysis of Financial Condition and Results of Operations.

Management s Discussion and Analysis of Results of Operations and Financial Condition (**MD&A**) is provided as a supplement to the accompanying consolidated financial statements and footnotes to help provide an understanding of our business, financial condition, changes in financial condition and results of operations. The MD&A is organized as follows:

Table of Contents

Overview. This section provides a discussion of recent events which we believe are important to understanding the Company s financial condition and the information set forth in the MD&A.

Results of Operations. This section provides an analysis of results of operations for the three fiscal years presented in the accompanying consolidated statements of operations.

Liquidity and Capital Resources. This section provides an analysis of cash flows, a discussion of outstanding debt and commitments, both firm and contingent, that existed as of January 31, 2004, and trends, demands, commitments, events and uncertainties with respect to the Company s ability to finance its continuing operations.

Critical Accounting Policies. This section discusses the accounting policies (i) that require the Company to make estimates that are highly uncertain at the time the estimate is made, (ii) for which a different estimate which could have been made would have a material impact on the Company s financial statements, (iii) that are the most important and pervasive policies utilized, and (iv) that are the most sensitive to material change from external factors. In addition, our significant accounting policies, including the critical accounting policies, are summarized in Note 1 to the accompanying consolidated financial statements.

Cautionary Statement and Additional Trends and Uncertainties. This section cautions on the basis of certain forward looking statements which are susceptible to uncertainty and changes in circumstances and discusses important trends and uncertainties that may impact the Company s financial condition and results of operations.

Overview

In March 2003, the Company announced that it had discovered apparent accounting discrepancies in previously reported financial information. As announced in March 2003 and on subsequent dates, upon discovery of such misstatements, the Company took immediate steps to quantify the extent of any incorrect financial reporting, discover the cause thereof, correct any problems and prevent future misstatements, including commencing a comprehensive internal review and notifying the U.S. Securities and Exchange Commission, the Company s auditor, the American Stock Exchange, and the public of the existence of the apparent misstatements. The nature and extent of the misstatements are fully disclosed in the Company s Annual Report on Form 10-K for the fiscal year ended January 31, 2003.

Results of Operations

Revenues

Revenues increased $5,441,000, or 21%, to $31,113,000 for fiscal year 2004, from $25,672,000 for fiscal year 2003. This growth was driven by an increase in revenue of $2,900,000 for the Joint Strike Fighter program, as well as an increase in core instrument sales of approximately $3,028,000. These increases were partially offset by a decrease in Precision Component revenue of approximately $703,000.

Revenues for the fiscal year ended January 31, 2003 decreased $1,014,000, or 4% to $25,672,000 when compared to the results for fiscal year 2002. The decrease in revenue resulted primarily from a decrease in demand for commercial products that was partially offset by an increase in demand for government products. For fiscal year 2003, the overall decrease in product sales was $3,320,000, or 16%, to $17,900,000 when compared to fiscal year 2002. However, such decrease in product sales was largely offset by the initiation of the Joint Strike Fighter development program, which was the primary reason for an increase in sales related to development projects of $2,193,000. The Company also experienced an increase in sales related to spare parts and repairs in fiscal year 2003 of approximately $113,000 when compared to fiscal year 2002.

Table of Contents

Cost of Sales

Cost of sales increased $5,711,000 or 34%, to $22,494,000, or 72% of revenues, for fiscal year 2004 from $16,783,000, or 65% of revenues, for fiscal year 2003. This increase in cost was primarily due to lower margins on the Joint Strike Fighter (**JSF**) development program, as approximately $260,000 of costs were incurred for what the Company believes were changes on scope and for which no additional revenue has yet been recognized. In addition, the rate of growth in JSF program costs incurred exceeded the rate of growth in revenues recognized as additional testing was required during certain aspects of the development cycle. Also, a shift in product mix where instrumentation revenues increased and represented a larger percentage of volume than in fiscal year 2003 (while revenues for repairs and spare parts remained relatively the same) put downward pressure on gross margins.

Cost of sales decreased $658,000 or 4%, to $16,783,000, or 65% of revenues, for fiscal year 2003 from $17,441,000 or 65% of revenues, for fiscal year 2002. This decrease in cost is primarily due to a reduction in revenue, as the change in sales mix that resulted in lower product sales was offset by higher sales of spare parts, repairs and development projects.

Selling, General and Administrative Expenses

Selling, general and administrative (**SG&A**) expense increased $645,000, or 8%, to $8,421,000, or 27% of revenue, for fiscal year 2004 from $7,776,000, or 30% of revenues for fiscal year 2003. The increase in SG&A expense was attributable to one-time charges for auditing and legal fees related to the Company s restatement of results of approximately $1,679,000, a retirement contract of approximately $134,000 and a consulting arrangement with the Company s former Chairman and Chief Executive Officer of approximately $134,000. These one-time charges were partially offset by reductions in engineering costs of approximately $652,000 that are largely due to the redeployment of engineering staff to the F-35 program where the engineering costs are absorbed in cost of sales, a reduction in compensation and benefits in general and administrative expense of approximately $275,000 and a reduction in consulting fees of approximately $100,000.

SG&A expense decreased $306,000, or 4%, to $7,776,000, or 30% of revenue, for fiscal year 2003 from $8,082,000, or 30% of revenue for fiscal year 2002. SG&A expense was 30% of revenues in fiscal year 2003 as well as in fiscal year 2002. The decrease was attributable to decreased commission expenses for sales in Europe and Japan as well as the redirection of engineering resources from internally-funded research and development efforts to customer-funded design work for the Joint Strike Fighter program.

Interest Expense

Net interest expense decreased $38,000, or 18% to $169,000 in fiscal year 2004 from net interest expense of $207,000 in fiscal year 2003. The net interest expense decrease was primarily due to lower average outstanding debt during the year and lower interest rates.

Net interest expense decreased $218,000, or 51%, to $207,000 in fiscal year 2003 from net interest expense of $425,000 in fiscal year 2002. The net interest expense decrease was primarily due to lower average outstanding debt during the year and lower interest rates.

Other Income (Expense)

Other income, net decreased $30,000 to $48,000 in fiscal year 2004 from other income, net $78,000 in fiscal year 2003. The decrease was primarily related to the one-time litigation settlement in fiscal year 2003 and was partially offset by foreign exchange gains on British Pound transactions.

Other income, net increased $84,000 to $78,000 in fiscal year 2003 from other income, net of ($6,000) in fiscal year 2002. The increase was primarily related to the settlement of litigation.

Table of Contents

Income Tax Expense

Income tax expense was a benefit of $465,000 for fiscal year 2004 as compared to an income tax benefit of $22,000 for fiscal year 2003. The income tax obligations that arise from pretax income for fiscal year 2004 are offset by the reversal of a deferred tax valuation allowance that had been previously recognized; as it is more likely than not that the deferred tax asset benefits will be realized in future periods.

The effective rate decreased 601.7% to (603.9%) in fiscal year 2004 from (2.2%) in fiscal year 2003. The decrease in the effective tax rate is primarily due to the reversal of a deferred tax valuation allowance that had been previously recognized.

Income tax expense was a benefit of $22,000 for fiscal year 2003 as compared to an expense of $21,000 for fiscal year 2002. The income tax obligations that arise from pretax income for fiscal year 2003 are offset by tax credits for research and development expenditures obtained through the filing of amended tax returns in the third quarter of fiscal year 2003 plus the change in the deferred tax allowance recognized in fiscal year 2003.

The effective tax rate decreased to (2.2%) in fiscal year 2003 from 2.9% in fiscal year 2002. The decrease in the effective tax rate is primarily due to the impact of the research and development credits that were recognized during fiscal year 2003 as well as the smaller change in the deferred tax valuation allowance recognized in fiscal year 2003 versus the large change in the deferred tax valuation allowance recognized in fiscal year 2002.

Income

Net income decreased $464,000 to $542,000, or 1.7% of revenue, for fiscal year 2004 from net income of $1,006,000, or 3.9% of revenue, for fiscal year 2003. Earnings per share decreased $0.12 to $0.14 for fiscal year 2004 from earnings per share of $0.26 in fiscal year 2003.

Net income increased $295,000 or 41% to $1,006,000, or 3.9% of revenue, for fiscal year 2003 from $711,000, or 2.7% of revenue, for fiscal year 2002. Earnings per share increased $0.08 to $0.26 for fiscal year 2003 from $0.18 in fiscal year 2002.

Inflation

The Company does not believe that inflation has had a material effect on the Company s financial position or results of operations. However, the Company cannot predict the future effects of inflation.

Liquidity and Capital Resources

Cash provided by operating activities was $2,214,000 for fiscal year 2004, compared to $93,000 for fiscal year 2003. The Company incurred substantial costs for professional services in fiscal year 2004, and a significant portion remained in accounts payable at January 31, 2004, resulting in a provision of cash of approximately $673,000. In addition, a large payment that was accrued as an account payable but was paid subsequent to January 31, 2004 resulted in a provision of cash of approximately $650,000. The ramp-up of production for the 32A government contract as well as the shipment of finished goods that were held at January 31, 2003 contributed to the cash provided by the decline in inventory of approximately $1,317,000. Also, a reduction in accrued liabilities due to the payment of professional fees that were accrued at January 31, 2003 contributed to cash used due to a decline in accrued expenses and other liabilities of approximately $534,000.

Cash provided by operating activities was $93,000 for fiscal year 2003 as compared to cash provided by operating activities of $1,775,000 for fiscal year 2002. The decrease was primarily attributable to an increase in inventory balances in anticipation of fulfillment of orders for the 32A government contract that was awarded in May 2002 and the commencement of a product development contract for a government product application.

Cash used in investing activities was $403,000 for fiscal year 2004 as compared to $681,000 for fiscal year 2003. The decrease was primarily attributable to the deferral of capital investment activity.

Cash used in investing activities was $681,000 for fiscal year 2003 as compared to $617,000 for fiscal year 2002. The decrease was primarily attributable to a slight decrease in investment in Machinery and Equipment.

Table of Contents

Cash used in financing activities was $795,000 for fiscal year 2004 as compared to cash used of $857,000 in fiscal year 2003. This decrease in cash usage was primarily due to lower debt repayment obligations as well as the absence of treasury stock purchases.

Cash used in financing activities was $857,000 for fiscal year 2003 as compared to cash used of $530,000 in fiscal year 2002. This increase in cash usage was primarily due to repayments of a portion of the Company s long-term debt.

To accommodate fluctuation in cash flow, the Company had a $1,000,000 revolving credit facility, which was set to expire in May 2003. As discussed below, the Company recently was in default under this facility with respect to, among other things, representations and warranties it made regarding encumbrances on the collateral, and covenants to provide annual and quarterly financial statements and maintain certain financial ratios, although waivers of such defaults were obtained. The Company requested and was granted subsequent extensions of this credit facility until September 5, 2003, December 5, 2003 and, most recently, until April 30, 2004. The credit facility originally bore interest at the trailing 90-day treasury index plus 2.75%. As a result of the extensions of the credit line, the interest rate for this facility has been changed to the prime rate, which was 4.00% as of September 5, 2003. At January 31, 2004, this facility was fully utilized.

As described in Note 12 to the Financial Statements, the Company completed a refinancing of its existing debt with Wachovia Bank, N.A. on February 25, 2004 (the **Wachovia Refinancing**). The new debt facilities consist of a $3,000,000 term loan, a $2,500,000 revolving credit facility and a $211,000 term loan. The proceeds from the refinancing were used to repay all of the Company s debt obligations to First Commercial Bank and SunTrust Bank N.A.

The Company had been in breach of certain covenants and other provisions of the documents related to its Industrial Development Revenue Bond (**IDRB**), the Mortgage on its Earlysville, Virginia property, and the Term Notes and Line of Credit with First Commercial Bank.

The Company had previously obtained written waivers for breaches of covenant violations that had occurred during fiscal year 2004. As of January 31, 2004, the Company was still in violation of certain financial covenants, but the underlying debt obligations were subsequently repaid out of the Wachovia Refinancing in February 2004. The Company also had negotiated an extension of its Term Notes and Line of Credit with First Commercial Bank to April 30, 2004. Consequently, the Company had no covenant violations with respect to its obligations to First Commercial Bank as of January 31, 2004. All loan obligations to First Commercial Bank were paid out of the proceeds of the Wachovia Refinancing in February 2004.

Future capital requirements depend on numerous factors, including research and development, expansion of products lines, and other factors. Management believes that cash and cash equivalents, together with the Company s cash flow from operations and current borrowing arrangements will provide for these necessary capital expenditures. Furthermore, the Company may develop and introduce new or enhanced products, respond to competitive pressures, invest or acquire businesses or technologies or respond to unanticipated requirements or developments, which would require additional resources.

Table of Contents

As shown in the table below, as of January 31, 2004, there are liquidation payments that were due with respect to long-term debt and other contractual obligations in fiscal year 2005 and beyond:

Contractual Obligations	Payments Due by Period				
	Total	Less than One Year	1 - 3 Years	4 - 5 Years	After 5 Years
Purchase Commitments	$7,680,000				