SERVOTRONICS INC /DE/
Form 10KSB
March 31, 2003

U.S. SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549
FORM 10-KSB

X ANNUAL REPORT UNDER SECTION 13 OR 15(d)OF THE SECURITIES EXCHANGE ACT OF 1934
-- For the fiscal year ended December 31, 2002

TRANSITION REPORT UNDER SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF
-- 1934

For the transition period from ________________ to ________________ .

Commission File No. 1-7109

SERVOTRONICS, INC.
(Name of small business issuer as specified in its charter)

Delaware
(State or other jurisdiction of incorporation or organization)

1110 Maple Street, Elma, New York
(Address of principal executive offices)
Issuer's telephone number: 716-655-5990 Securities registered pursuant to Section 12(b) of the Act:

Title of each class

Common Stock, $.20 par value

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

Check whether the issuer (1) filed all reports required to be filed by Section 13 or 15(d) of the Exchange Act during the past 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

Check if disclosure of delinquent filers in response to Item 405 of Regulation S-B is not contained in this form, and no disclosure will 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-KSB or any amendment to this Form 10-KSB. X

Issuer's revenues for its most recent fiscal year: $15,607,000

As of March 15, 2003 the aggregate market value of the voting common stock held by non-affiliates of the registrant was $4,194,310.57 based on the average of sales prices reported by the American Stock Exchange on that day.

As of March 15, 2003 the number of $.20 par value common shares outstanding was 2,392,141.

DOCUMENTS INCORPORATED BY REFERENCE

Document

2003 Proxy Statement

Transitional Small Business Disclosure Format. Yes ___ No X

## PART I

### Item 1. Description of Business

#### General

Servotronics, Inc. and its subsidiaries (collectively the "Registrant" or the "Company") design, manufacture and market advanced technology products consisting primarily of control components and consumer products consisting of knives and various types of cutlery.

The Registrant was incorporated in New York in 1959. In 1972, the Registrant was merged into a wholly-owned subsidiary organized under the laws of the State of Delaware, thereby changing the Registrant's state of incorporation from New York to Delaware.

#### Products

##### Advanced Technology Products

The Registrant designs, manufactures and markets a variety of servo-control components which convert an electrical current into a mechanical force or movement and other related products. The principal servo-control components produced include torque motors, electromagnetic actuators, proportional solenoids, hydraulic valves, pneumatic valves and similar devices, all of which perform the same general function. These are sold principally to the commercial aerospace, missile, aircraft and government related industries.

To fill most of its orders for components, the Registrant must either modify a standard model or design a new item in order to satisfy the customer's particular requirements. The Registrant also produces unique products based on specifications provided by its customers. The Registrant produces under long-term contracts and other types or orders.

The Registrant also produces metallic seals of various cross-sectional configurations. These seals fit between two surfaces, usually metal, to produce a more secure and leak-proof joint. The Registrant manufactures these seals to close tolerances from standard and special alloy steels. Ductile coatings are often applied to the seals in order to increase their effectiveness.



From time to time, the Registrant has also produced other products of its own and/or of a given design to meet customers' requirements.

Consumer Products

The Registrant designs, manufactures and sells a variety of cutlery products. These products include a wide range of knives such as steak, carving, bread, butcher and paring knives for household use and for use in restaurants, government installations, institutions and private industry, and pocket and other types of knives for hunting, fishing, camping and military use. The Registrant also produces and markets other cutlery items such as carving forks, sharpeners and various specialty tools such as putty knives, linoleum sheet cutters and field knives. The Registrant manufactures its cutlery products from stainless or high carbon steel in numerous styles, designs, models and sizes. Substantially all of the Registrant's cutlery and cutlery related products are intended for the medium to premium priced markets.

The Registrant sells many of its cutlery products under its own brand names including "Old Hickory" and "Queen."

Sales, Marketing and Distribution

Advanced Technology Products

The Registrant's advanced technology products are marketed throughout the United States and are essentially non-seasonal in nature. These products are sold to the United States Government, government prime contractors, government subcontractors, commercial manufacturers and end users. Sales are made primarily by the Registrant's professional staff and commissioned field engineering representatives.

During the Registrant's last fiscal year, sales of advanced technology products pursuant to subcontracts with prime or subcontractors for various branches of the United States Government or pursuant to prime contracts directly with the government accounted for approximately 22% of the Registrant's total revenues. In 2002 and 2001, sales of advanced technology products to each of Honeywell and United Technologies (including their respective subsidiaries and/or divisions) exceeded 10% of Registrant's total revenues. No other single customer represented more than 10% of the Company's revenues in any of these years.

The Registrant's prime contracts and subcontracts with the United States Government are subject to termination for the convenience of the Government. In the event of such termination, the Registrant is ordinarily entitled to receive



payment for its costs and profits on work done prior to termination. Since the inception of the Registrant's business, less than 1% of its Government contracts have been terminated for convenience.

Consumer Products

The Registrant's consumer products are marketed throughout the United States. Consumer sales are moderately seasonal. Sales are to hardware, supermarket, variety, department, discount, gift and drug stores. The Registrant's Consumer Products Group also sells its cutlery products (principally machetes, bayonets, survival knives and kitchen knives) to various branches of the United States Government which accounted for approximately 1% of the Registrant's total sales in 2002. The Registrant sells its products through its own sales personnel and through independent manufacturers' representatives.

Business Segments

Business segment information is presented in Note 10 of the accompanying consolidated financial statements.

Intellectual Properties

The Company has rights under certain copyrights and registered domain names. In the view of management, the Registrant's competitive position is not dependent on patent protection.

Research Activities

The amount spent by the Registrant in research and development activities during its 2002 and 2001 fiscal years was not significant.

Environmental Compliance

The Registrant does not anticipate that the cost of compliance with current environmental laws will be material.

Manufacturing

The Registrant manufactures its consumer products in Franklinville, New York and Titusville, Pennsylvania and its advanced technology products in Elma, New York.



Raw Materials and Other Supplies

The Registrant purchases raw materials and certain components for its products from outside vendors. The Registrant is not generally dependent upon a single source of supply for any raw material or component used in its operations.

Competition

Although no reliable industry statistics are available to enable the Registrant to determine accurately its relative competitive position with respect to any of its products, the Registrant believes that it is a significant factor with respect to certain of its servo-control components. The Registrant's share of the overall cutlery market is not significant.

The Registrant encounters active competition with respect to its products from numerous companies, many of which are larger than it in terms of manufacturing capacity, financial resources and marketing organization. Its principal competitors vary depending upon the customer and/or the products involved. The Registrant believes that it competes primarily with more than 20 companies with respect to its consumer products, in addition to foreign imports. To the Registrant's knowledge, its principal competitors with regard to cutlery include ECKO Housewares, Inc., Russell Harrington Cutlery, Inc., W. R. Case & Sons Cutlery Company, Imperial Schrade Corporation and Camillus Cutlery Company.

The Registrant has many different competitors with respect to servo-control components because of the nature of that business and the fact that these products also face competition from other types of control components which, at times, can accomplish the desired result.

The Registrant markets most of its products throughout the United States. The Registrant believes that it competes in marketing its consumer products primarily on the basis of price, quality and delivery, and its control products primarily on the basis of operating performance, adherence to rigid specifications, quality, price and delivery.

## Employees

The Registrant, at December 31, 2002, had approximately 216 employees of which approximately 201 are full time. In excess of 82% of its employees are engaged in production, inspection, packaging or shipping activities. The balance are engaged in executive, engineering, administrative, clerical or sales capacities.

-5-

## Item 2. Description of Properties

The Registrant's executive offices are located on premises leased by the Registrant at 1110 Maple Street, Elma, a suburb of Buffalo, New York. The Registrant owns and/or leases real property as set forth in the following table:

| Location | Approx. acreage | Principal product manufactured | Number of buildings and type of construction |
|---|---|---|---|
| Elma, New York | 38.4 | Advanced technology products | 1-concrete block/ steel |
| Franklinville, New York | 11.7 | Cutlery products | 1-tile/wood and 1 concrete/metal |
| Titusville, Pennsylvania | .4 | Cutlery products | 2-brick |

In Elma, New York, the Registrant leases approximately 38.4 acres of land and a facility from a local industrial development agency. The lease is accounted for as a capital lease and entitles the Registrant to purchase the property for a nominal amount.

See the consolidated financial statements, including Note 8 thereto, for further information with respect to the Registrant's lease commitments.

The Registrant possesses modern precision manufacturing and testing equipment suitable for the development, manufacture, assembly and testing of its advanced technology products. The Registrant designs and makes substantially all of the tools, dies, jigs and specialized testing equipment necessary for the production of the advanced technology products. The Registrant also possesses automatic and semi-automatic grinders, tumblers, presses and miscellaneous metal finishing machinery and equipment for use in the manufacture of consumer products.

Item 3. Legal Proceedings

There are no legal proceedings which are material to the Company currently pending by or against the Company other than ordinary routine litigation incidental to the business which is not expected to materially adversely affect the business or earnings of the Company.

-6-

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

Not applicable.

-7-

PART II

Item 5. Market for Common Equity and Related Stockholder Matters

(a) Price range of common stock

The following table shows the range of high and low prices for the Registrant's common stock as reported by the American Stock Exchange for 2002 and 2001.

| | High | Low |
|---|---|---|
| 2002 | | |
| Fourth Quarter | $ 4.00 | $ 3.30 |
| Third Quarter | 4.40 | 3.60 |
| Second Quarter | 5.20 | 4.40 |

| | | |
|---|---|---|
| First Quarter | 5.22 | 4.70 |
| 2001 | | |
| Fourth Quarter | $ 6.20 | $ 3.70 |
| Third Quarter | 8.90 | 3.40 |
| Second Quarter | 3.65 | 2.30 |
| First Quarter | 2.69 | 1.65 |

(b) Approximate number of holders of common stock

| Title of class | Approximate number of record holders (as of December 31, 2002) |
|---|---|
| Common Stock, $.20 par value per share | 607 |

(c) Dividends on common stock

No cash dividends were paid in 2002 or 2001.



## Item 6. Management's Discussion and Analysis or Plan of Operation

### Summary

The following table sets forth for the periods indicated the percentage relationship of certain items in the consolidated statement of operations to net revenues and the percentage increase or decrease of such items as compared to the indicated prior period:

| | Relationship to net revenues year ended December 31, 2002 | 2001 |
|---|---|---|
| Net revenues: | | |
| Advanced technology products | 65.4% | 67.9 % |
| Consumer products | 34.6 | 32.1 |
| | 100.0 | 100.0 |
| Cost of goods sold | 77.5 | 72.1 |
| Gross profit | 22.5 | 27.9 |
| Selling, general and administrative costs | 19.1 | 16.9 |
| Interest | 1.3 | 1.5 |
| Depreciation | 4.2 | 3.3 |
| | 24.6 | 21.7 |

| | | |
|---|---|---|
| Income (loss) before income taxes | (2.1) | 6.2 |
| Income tax provision (benefit) | (0.6) | 2.3 |
| Net income (loss) | (1.5)% | 3.9% |



## Management Discussion

During the year ended December 31, 2002 and for the comparable period ended December 31, 2001, approximately 23% and 19% respectively of the Company's revenues were derived from contracts with agencies of the U.S. Government or their prime contractors. The Company's business is performed under fixed price contracts. Sales to the government are affected by defense budgets, U.S. & foreign policy and the level of military flight operations. As major international events are currently unfolding, it is difficult to predict the impact on future financial results. In addition, the aftermath of the September 11th terrorist's attacks and the perceived continued threat to the airline industry has significantly lowered commercial passenger traffic and has had a direct effect on revenues in the commercial aerospace markets.

See also Note 10 to the consolidated financial statements for information concerning business segment operating results.

## Results of Operations - Year 2002 as Compared to 2001

The Company's consolidated results of operations for the year ended December 31, 2002 showed an approximate 13% decrease in net revenues with a decrease in net income of approximately 132.8%. The decrease in net revenues is primarily attributable to a decrease in revenue at the Advanced Technology Group of $1,973,000 and a decrease in revenue of $355,000 at the Consumer Products Group. The decrease in revenues for the twelve month period ended December 31, 2002 can be attributed to the overall continued economic softness in the aerospace industry and previously reported reductions and stretch-outs in the commercial markets for the advanced technology products combined with a loss of revenues at the Consumer Products Group due both to a regionalization of markets by a significant customer, certain reprioritizations of government procurements and the general decline in retail markets for edged products.

Gross profit decreased for the twelve month period ended December 31, 2002 primarily due to a decrease in net revenues along with increased expenses to expand the capabilities of our current product lines and resources expended to modify and adapt existing and new products for additional applications in both the aerospace industry as well as other markets. As previously reported, recent changes in accounting rules do not allow for the deferment of pre-production and/or start-up costs and, as such, they are reflected in cost of goods sold for the year ended December 31, 2002 with no, or minimal, benefit to revenue in the current period. Although the current year's gross margin was negatively impacted



by the cyclical and costly nature of pre-production and/or prototype expenses, these long-term investments are necessary and have the potential to provide substantial positive effects on the funded and unfunded backlogs.

Selling, general and administrative costs increased for the year ended December 31, 2002 as a percentage of sales when compared to the same period in 2001. This can be attributed to a smaller percentage of expenses that are dependent upon sales levels and a greater percentage reflecting fixed general and administrative costs. Further, the Company has incurred expenses for costs dedicated to merger/acquisition evaluations, expanded sales and marketing activities, and additional procedures and professional expenses to assure the integrity of financial reporting and corporate disclosure following passage of the Sarbanes-Oxley Act in 2002.

Interest expense as a percentage of long-term debt decreased for the year ended December 31, 2002 when compared to the same period in 2001 due to market driven interest rate fluctuations and the decrease of institutional debt.

Depreciation expense increased due to variable estimated useful lives of depreciable property as identified in Note 1 to the consolidated financial statements.

The Company's effective tax rate (benefit) was (29%) in 2002 compared to 37% in 2001. The variance in the effective tax rate is primarily attributable to state income taxes.

## Results of Operations - Year 2001 as Compared to 2000

The Company's consolidated results of operations for the year ended December 31, 2001 showed an approximate 5.7% increase in net revenues with an increase in net income of approximately 67.5%. The increase in net revenues is primarily attributable to increased revenue at the Advanced Technology Group of $2,699,000 partially offset by a decrease in revenue of $1,733,000 at the Consumer Products Group. The resultant increase in net income is attributable to both product mix at the Advanced Technology Group and the Consumer Products Group, and previously reported cost controls as reflected in the accompanying financial statements.

Selling, general and administrative costs remained consistent for the year ended December 31, 2001 when compared to the same period in 2000 despite the increase in net revenues. This can be attributed to a smaller percentage of expenses that are dependent upon sales levels and a greater percentage reflecting fixed general and administrative costs.

Interest expense as a percentage of long-term debt decreased by approximately 2% for the year ended December 31, 2001 when compared to the same



period in 2000 due to market driven interest rate fluctuations, favorable interest rate renewal agreements and the continued decrease of institutional debt.

Depreciation expense decreased due to variable estimated useful lives of depreciable property as identified in Note 1 to the consolidated financial statements.

The Company's effective tax rate was 37% in 2001 compared to 43% in 2000. The decrease resulted from higher U.S. tax incentives on export sales in 2001.

## Liquidity and Capital Resources

The Company's primary liquidity and capital requirements relate to the working capital needs; primarily inventory, accounts receivable, capital investments in facilities, machinery, tools/dies and equipment and principal/interest payments on indebtedness. The Company's primary sources of liquidity have been from positive cash flows and from bank financing.

During the year ended December 31, 2002, the Company expended $717,000 on capital expenditures of which approximately $260,000 was for the previously reported planned capability expansion at the Consumer Products Group. During the year ended December 31, 2001, the Company capital expenditures were $273,000.

There are no other material commitments for capital expenditures at December 31, 2002.

The Company also has a $1,000,000 line of credit on which there is no balance outstanding at December 31, 2002.

Principal maturities of long-term debt are as follows: 2003 - $378,000; 2004 - $463,000; 2005 - $418,000; 2006 - $312,000; 2007 and thereafter - $4,481,000.

## Critical Accounting Policies

See Note 1 to the consolidated financial statements.

## Item 7. Financial Statements

The financial statements of the Registrant which are included in this Form 10-KSB Annual Report are described in the accompanying Index to Consolidated Financial Statements on Page F1.

## Item 8. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.



# PART III

## Item 9. Directors, Executive Officers, Promoters and Control Persons; Compliance with Section 16(a) of the Exchange Act

Information regarding directors and executive officers of the Registrant is incorporated herein by reference to the information included in the Registrant's definitive proxy statement if it is filed with the Commission within 120 days after the end of the Registrant's 2002 fiscal year or such information will be included by amendment.

## Item 10. Executive Compensation

Information regarding executive compensation is incorporated herein by reference to the information included in the Registrant's definitive proxy statement if it is filed with the Commission within 120 days after the end of the Registrant's 2002 fiscal year or such information will be included by amendment.

## Item 11. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Information regarding security ownership of certain beneficial owners and management is incorporated herein by reference to the information included in the Registrant's definitive proxy statement if it is filed with the Commission within 120 days after the end of the Registrant's 2002 fiscal year or such information will be included by amendment.

Item 12. Certain Relationships and Related Transactions

Information regarding certain relationships and related transactions is incorporated herein by reference to the information included in the Registrant's definitive proxy statement if it is filed with the Commission within 120 days after the end of the Registrant's 2002 fiscal year or such information will be included by amendment.

-13-

Item 13. Exhibits and Reports on Form 8-K

(a) Exhibits

| Exhibit number | Presentation | Referenc |
|---|---|---|
| 3(A)(1) | Certificate of Incorporation | Exhibit 3(A)( Form 10-KS |
| 3(A)(2) | Amendments to Certificate of Incorporation dated August 27, 1984 | Exhibit 3(A)( Form 10-KS |
| 3(A)(3) | Certificate of designation regarding Series I preferred stock | Exhibit 4(A) Form 10-K* |
| 3(A)(4) | Amendments to Certificate of Incorporation dated June 30, 1998 | Exhibit 3(A)( Form 10-KS |
| 3(B) | By-laws | Exhibit 3(B) Form 10-K* |
| 4.1(A) | First amended and restated term loan agreement with Fleet Bank of New York dated October 4, 1993 | Exhibit 4(A) Form 10-KS |
| 4.1(B) | Second amended and restated term loan agreement with Fleet Bank of New York dated February 26, 1999 | Exhibit 4.1(B Form 10-KS |
| 4.1(C) | First amendment to second amended and restated term loan agreement with Fleet Bank of New York dated December 17, 1999 | Exhibit 4.1(C Form 10-KS |

| | | |
|---|---|---|
| 4.2(A)(1) | Letter of Credit Reimbursement Agreement with Fleet Bank dated December 1, 1994 | Exhibit 4(B)( 1994 10-KS |

---

*Incorporated herein by reference (File No. 1-7109)
**Indicates management contract or compensatory plan or arrangement



| Exhibit number | Presentation | Referenc |
|---|---|---|
| 4.2(B) | First Amendment and Extension to Letter of Credit and Reimbursement Agreement with Fleet Bank of New York dated as of December 17, 1999 | Exhibit 4.2(B Form 10-KS |
| 4.2(B)(2) | Agency Mortgage and Security Agreement dated as of December 1, 1994 from the Registrant and its subsidiaries | Exhibit 4(B)( 1994 10-KS |
| 4.2(B)(3) | Guaranty Agreement dated as of December 1, 1994 from the Registrant and its subsidiaries to the Erie County Industrial Development Agency ("ECIDA"), Norwest Bank Minnesota, N.A., as Trustee, and Fleet Bank | Exhibit 4(B)( 1994 10-KS |
| 4.3 | Shareholder Rights Plan dated as of August 27, 2002 | Exhibit 4 to 8-K filed 2002* |
| 10(A)(1) | Employment contract** | Exhibit 10(A) Form 10-K* |
| 10(A)(2) | Amendment to employment contract** | Filed herewit |
| 10(A)(3) | Amendment to employment contract** | Filed herewit |
| 10(B) | Form of Indemnification Agreement between the Registrant and each of its Directors and Officers** | Exhibit 10(E) Form 10-K* |

---

*Incorporated herein by reference (File No. 1-7109)
**Indicates management contract or compensatory plan or arrangement



| Exhibit number | Presentation | Referenc |
|---|---|---|
| 10(C)(1) | Loan agreement between the Company and its employee stock ownership trust, as amended | Exhibit 10(C) to 1991 Fo |
| 10(C)(2) | Stock purchase agreement between the Company and its employee stock ownership trust | Exhibit 10(D) 1988 Form |
| 10(D)(1)(a) | 2000 Employees Stock Option Plan** | Exhibit 10(D) Form 10-KS |
| 10(D)(2) | Stock Option Agreement for Donald W. Hedges dated March 24, 1998** | Exhibit 10(D) Form 10-KS |
| 10(D)(2)(a) | Stock Option Agreement for Donald W. Hedges dated July 7, 2000** | Exhibit 10(D) Form 10-KS |
| 10(D)(3)(b) | Stock Option Agreement for Nicholas D. Trbovich dated March 24, 1998** | Exhibit 10(D) Form 10-KS |
| 10(D)(3)(c) | Stock Option Agreement for Nicholas D. Trbovich dated July 7, 2000** | Exhibit 10(D) Form 10-KS |
| 10(D)(4) | Stock Option Agreement for William H. Duerig dated March 24, 1998** | Exhibit 10(D) Form 10-KS |
| 10(D)(4)(a) | Stock Option Agreement for William H. Duerig dated July 7, 2000** | Exhibit 10(D) Form 10-KS |
| 10(D)(5)(b) | Stock Option Agreement for Nicholas D. Trbovich, Jr. dated March 24, 1998** | Exhibit 10(D) Form 10-KS |

---

*Incorporated herein by reference (File No. 1-7109)
**Indicates management contract or compensatory plan or arrangement

| Exhibit number | Presentation | Referenc |
|---|---|---|
| 10(D)(6)(b) | Stock Option Agreement for Nicholas D. Trbovich, Jr. dated March 24, 1998** | Exhibit 10(D) Form 10-KS |
| 10(D)(6)(c) | Stock Option Agreement for Nicholas D. Trbovich, Jr. dated July 7, 2000** | Exhibit 10(D) Form 10-KS |
| 10(D)(7)(b) | Stock Option Agreement for Lee D. Burns dated March 24, 1998** | Exhibit 10(D) Form 10-KS |
| 10(D)(7)(c) | Stock Option Agreement for Lee D. Burns dated July 7, 2000** | Exhibit 10(D) Form 10-KS |
| 10(D)(8)(b) | Stock Option Agreement for Raymond C. Zielinski dated March 24, 1998** | Exhibit 10(D) Form 10-KS |
| 10(D)(8)(c) | Stock Option Agreement for Raymond C. Zielinski dated July 7, 2000** | Exhibit 10(D) Form 10-KS |
| 10(D)(9) | Land Lease Agreement between TSV, Inc. (wholly-owned subsidiary of the Registrant) and the ECIDA dated as of May 1, 1992, and Corporate Guaranty of the Registrant dated as of May 1, 1992 | Exhibit 10(D) Form 10-KS |
| 10(D)(10) | Amendment to Land Lease Agreement and Interim Lease Agreement dated November 19, 1992 | Exhibit 10(D) Form 10-KS |

---

*Incorporated herein by reference (File No. 1-7109)

**Indicates management contract or compensatory plan or arrangement



| Exhibit number | Presentation | Referenc |
|---|---|---|

| | | |
|---|---|---|
| 10(D)(11) | Lease Agreement dated as of December 1, 1994 between the Erie County Industrial Development Agency ("ECIDA") and TSV, Inc. | Exhibit 10(D) 1994 10-KS |
| 10(D)(12) | Sublease Agreement dated as of December 1, 1994 between TSV, Inc. and the Registrant | Exhibit 10(D) 1994 10-KS |
| 10(D)(13) | 2001 Long-Term Stock Incentive Plan | Appendix A to Proxy** |
| 21 | Subsidiaries of the Registrant | Exhibit 21 to 10-KSB* |
| 99.1 | Section 906 Certification of Chief Executive Officer | Filed herewit |
| 99.2 | Section 906 Certification of Chief Financial Officer | Filed herewit |

The Registrant hereby agrees that it will furnish to the Securities and Exchange Commission upon request a copy of any instrument defining the rights of holders of long-term debt not filed herewith.

(b) Reports on Form 8-K

(1) Form 8-K Filed November 14, 2002

Regulation FD Disclosure. Certifications by the Chief Executive Officer and Chief Financial Officer pursuant to 18 U.S.C. Section 1350 as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 to accompany the Quarterly Report on Form 10-QSB for the quarterly period ended September 30, 2002.

---

*Incorporated herein by reference (File No. 1-7109)
**Indicates management contract or compensatory plan or arrangement

-18-

Item 14. Controls and Procedures

Our management has reviewed our disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) as of a date within 90 days prior to this report. Our management believes that such disclosure controls and procedures are adequate to ensure that material information relating to the Company is made known to management by others within the Company.

In addition, our management reviewed our internal controls and, to management's knowledge, there have been no significant changes in the Company's internal controls or in other factors that could significantly affect internal controls subsequent to the date of their last evaluation.

FORWARD-LOOKING STATEMENTS

In addition to historical information, certain sections of this Form 10-KSB contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, such as those pertaining to the Company's capital resources and profitability. Forward-looking statements involve numerous risks and uncertainties. The Company derives a material portion of its revenues from contracts with agencies of the U.S. Government or their prime contractors. The Company's business is performed under fixed price contracts and the following factors, among others discussed herein, could cause actual results and future events to differ materially from those set forth or contemplated in the forward-looking statements: uncertainties in today's global economy, global competition, difficulty in predicting defense appropriations, the vitality of the commercial aviation industry and its ability to purchase new aircraft, the willingness and ability of the Company's customers to fund long-term purchase programs and market demand and acceptance both for the Company's products and its customers' products which incorporate Company-made components. The success of the Company also depends upon the trends of the economy, including interest rates, income tax laws, governmental regulation, legislation, population changes and those risk factors discussed elsewhere in this Form 10-KSB. Readers are cautioned not to place undue reliance on forward-looking statements, which reflect management's analysis only as the date hereof. The Company assumes no obligation to update forward-looking statements.

-19-

SIGNATURES

In accordance with 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.

SERVOTRONICS, INC.

March 18, 2003 By /s/ Nicholas D. Trbovich, President

Nicholas D. Trbovich
President, Chief Executive Officer
and Chairman of the Board

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

| | | |
|---|---|---|
| /s/ Nicholas D. Trbovich<br>Nicholas D. Trbovich | President, Chief Executive Officer, Chairman of the Board and Director | March 18, |

| | | |
|---|---|---|
| /s/ Lee D. Burns<br>----------------<br>Lee D. Burns | Treasurer and Secretary<br>(Chief Financial Officer) | March 18, |
| /s/ Donald W. Hedges<br>--------------------<br>Donald W. Hedges | Director | March 18, |
| /s/ William H. Duerig<br>---------------------<br>William H. Duerig | Director | March 18, |
| /s/ Nicholas D. Trbovich Jr.<br>----------------------------<br>Nicholas D. Trbovich Jr. | Director | March 18, |

-20-

CERTIFICATION

I, Lee D. Burns, certify that:

1. I have reviewed this annual report on Form 10-KSB of Servotronics, Inc.;

2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;

3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

    a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;

    b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and

    c) presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

   a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

   b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: March 18, 2003

/s/ Lee D. Burns, Chief Financial Officer

Lee D. Burns
Chief Financial Officer



CERTIFICATION

I, Nicholas D. Trbovich, certify that:

1. I have reviewed this annual report on Form 10-KSB of Servotronics, Inc.;

2. Based on my knowledge, this annual report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this annual report;

3. Based on my knowledge, the financial statements, and other financial information included in this annual report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this annual report;

4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-14 and 15d-14) for the registrant and we have:

   a) designed such disclosure controls and procedures to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this annual report is being prepared;

b) evaluated the effectiveness of the registrant's disclosure controls and procedures as of a date within 90 days prior to the filing date of this annual report (the "Evaluation Date"); and

c) presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures based on our evaluation as of the Evaluation Date;

5. The registrant's other certifying officers and I have disclosed, based on our most recent evaluation, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

a) all significant deficiencies in the design or operation of internal controls which could adversely affect the registrant's ability to record, process, summarize and report financial data and have identified for the registrant's auditors any material weaknesses in internal controls; and

b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls; and

6. The registrant's other certifying officers and I have indicated in this annual report whether or not there were significant changes in internal controls or in other factors that could significantly affect internal controls subsequent to the date of our most recent evaluation, including any corrective actions with regard to significant deficiencies and material weaknesses.

Date: March 18, 2003

/s/ Nicholas D. Trbovich, Chief Executive Officer

Nicholas D. Trbovich
Chief Executive Officer

-22-

SERVOTRONICS, INC. AND SUBSIDIARIES

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

Consolidated statement of operations for the years ended
December 31, 2002 and 2001

Consolidated statement of cash flows for the years ended
December 31, 2002 and 2001

Notes to consolidated financial statements

Financial statement schedules are omitted because they are not applicable or the required information is shown in the financial statements or the notes thereto.



## Report of Independent Accountants

To the Board of Directors and Shareholders of
Servotronics, Inc.

In our opinion, the accompanying consolidated balance sheet and the related consolidated statements of operations and cash flows present fairly, in all material respects, the financial position of Servotronics, Inc. (the "Company") and its subsidiaries at December 31, 2002 and December 31, 2001, and the results of their operations and their cash flows for the years then ended in conformity with accounting principles generally accepted in the United States of America. 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 of these statements in accordance with auditing standards generally accepted in the United States of America, which 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, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

PricewaterhouseCoopers LLP

Buffalo, New York
March 18, 2003



## SERVOTRONICS, INC. AND SUBSIDIARIES

### CONSOLIDATED BALANCE SHEET

December 31, 2002

($000's omitted except share and per share data)

Assets
Current assets:

Cash
Accounts receivable
Inventories
Prepaid income taxes
Deferred income taxes
Other (See Note 1 to consolidated financial statements)

Total current assets

Property, plant and equipment, net

Other assets

Liabilities and Shareholders' Equity
Current liabilities:
Current portion of long-term debt
Accounts payable
Accrued employee compensation and benefit costs
Other accrued liabilities

Total current liabilities

Long-term debt
Deferred income taxes
Other non-current liabilities
Shareholders' equity:
Common stock, par value $.20; authorized 4,000,000 shares; issued 2,614,506 shares
Capital in excess of par value
Retained earnings
Accumulated other comprehensive income (loss)

Employee stock ownership trust commitment
Treasury stock, at cost 222,365 shares

Total shareholders' equity

See notes to consolidated financial statements



SERVOTRONICS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF OPERATIONS

($000's omitted except per share data)

| | Ye Dec 2002 |
|---|---|
| Net revenues | $ 15,607 |
| Costs and expenses: | |
| Cost of goods sold | 12,096 |
| Selling, general and administrative | 2,977 |
| Interest | 196 |
| Depreciation | 660 |
| | 15,929 |
| Income (loss) before income taxes | (322) |
| Income tax provision (benefit) | (93) |
| Net income (loss) | $ (229) |
| Income (Loss) Per Share: | |
| Basic | |
| Net income (loss) per share | $ (0.12) |
| Diluted | |
| Net income (loss) per share | $ (0.12) |

See notes to consolidated financial statements

-F4-

SERVOTRONICS, INC. AND SUBSIDIARIES

CONSOLIDATED STATEMENT OF CASH FLOWS

($000's omitted)

| | Ye Dec 2002 |
|---|---|
| Cash flows related to operating activities: | |
| Net income (loss) | $ (229) |
| Adjustments to reconcile net income (loss) to net cash provided by operating activities - | |
| Depreciation | 660 |
| Deferred income taxes | (97) |
| Change in assets and liabilities - | |

| | |
|---|---|
| Accounts receivable | 66 |
| Inventories | 276 |
| Prepaid income taxes | (48) |
| Other current assets | 628 |
| Other assets | (9) |
| Accounts payable | (442) |
| Accrued employee compensation & benefit costs | 103 |
| Other accrued liabilities | (77) |
| Other non-current liabilities | (8) |
| Employee stock ownership trust payment | 101 |
| Net cash provided by operating activities | 924 |
| Cash flows related to investing activities: | |
| Capital expenditures - property, plant & equipment | (717) |
| Purchase of treasury shares | - |
| Net cash used in investing activities | (717) |
| Cash flows related to financing activities: | |
| Increase in demand loan | 400 |
| Acquisition of long-term debt | 500 |
| Payments on demand loan | (600) |
| Principal payments on long-term debt | (548) |
| Net cash used in financing activities | (248) |
| Net (decrease) increase in cash | (41) |
| Cash at beginning of period | 720 |
| Cash at end of period | $ 679 |

Supplemental disclosures:

| | |
|---|---|
| Income taxes paid | $ 132 |
| Interest paid | $ 226 |

See notes to consolidated financial statements



SERVOTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Summary of significant accounting policies

The principal accounting policies of Servotronics, Inc. (the "Company") and subsidiaries are as follows:

Principles of consolidation

The consolidated financial statements include the accounts of Servotronics, Inc. and its wholly-owned subsidiaries.

Cash and cash equivalents

The Company considers cash and cash equivalents to include all cash accounts and short-term investments purchased with a maturity of three months or less.

Revenue recognition

The Company's revenues are principally recognized as units are shipped and as terms and conditions of purchase orders are met. The Company also incurred costs for certain contracts which are long-term. These contracts are accounted for under the percentage of completion method (cost-to-cost) which recognizes revenue as the work progresses towards completion.

Included in other current assets is $829,000 of unbilled revenues which represents revenue earned under the percentage of completion method (cost-to-cost) not yet billable under the terms of the contracts.

Inventories

Inventories are stated generally at the lower of standard cost, which approximates actual cost (first-in, first-out), or market. Pre-production and start-up costs are expensed as incurred.

Shipping and handling costs

Shipping and handling costs are classified as a component of cost of goods sold.



Property, plant and equipment

Property, plant and equipment is carried at cost; expenditures for new facilities and equipment and expenditures which substantially increase the useful lives of existing plant and equipment are capitalized; expenditures for maintenance and repairs are charged directly to cost or expenses as incurred. Upon retirement or disposal of properties, the related cost and accumulated depreciation are removed from the respective accounts and any profit or loss on disposition is included in income.

Depreciation is provided on the basis of estimated useful lives of depreciable properties, primarily by the straight-line method for financial statement purposes and by accelerated methods for tax purposes. Depreciation expense includes the amortization of capital lease assets. The estimated useful lives of depreciable properties are generally as follows:

| | |
|---|---|
| Buildings and improvements | 5-39 years |
| Machinery and equipment | 5-15 years |
| Tooling | 3-5 years |

Income taxes

The Company and its subsidiaries file a consolidated federal income tax return and separate state income tax returns.

The Company follows the asset and liability approach to account for income taxes. This approach requires the recognition of deferred tax liabilities and assets for the expected future tax consequences of operating loss carryforwards and temporary differences between the carrying amounts and the tax bases of assets and liabilities.

Employee stock ownership plan

Contributions to the employee stock ownership plan are determined annually by the Company according to plan formula.

Use of estimates

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

-F7-

New accounting pronouncements

In 2001, the Company adopted Statement of Financial Accounting Standards ("SFAS") No. 144 Accounting for the Impairment or Disposal of Long-Lived Assets. SFAS No. 144 contains accounting and reporting requirements for the impairment and disposal of long-lived assets and discontinued operations. Adoption of SFAS No. 144 had no effect on the Company's financial statements.

2. Inventories

| | December 3 |
|---|---|
| | ($000's om |
| Raw materials and common parts | $ 97 |
| Work-in-process | 5,10 |
| Finished goods | 91 |
| | 6,99 |
| Less common parts expected to be used after one year | (23 |
| | $ 6,76 |

3. Property, plant and equipment

| | December 3 |
|---|---|
| | ($000's om |
| Land | $ 2 |
| Buildings and improvements | 6,45 |

| | |
|---|---|
| Machinery, equipment and tooling | 9,61 |
| | 16,08 |
| Less accumulated depreciation | (9,00 |
| | $ 7,08 |

Property, plant and equipment includes land and building under a $5,000,000 capital lease which can be purchased for a nominal amount at the end of the lease term. The Company believes that it maintains property and casualty insurance in amounts adequate for the risk and nature of its assets and operations and which are generally customary in its industry.



4. Long-term debt

| | December 3 |
|---|---|
| | ($000's om |
| Industrial Development Revenue Bonds; secured by a letter of credit from a bank with interest payable monthly at a floating rate (1.85% at December 31, 2002) | $ 4,49 |
| Term loans; payable to a financial institution $500,000 at LIBOR plus 2% (3.38% at December 31, 2002); quarterly principal payments of $17,500 commencing January 1, 2005; payable in full October 1, 2009; and $464,000 at a rate of 5.82% at December 31, 2002; quarterly principal payments of $35,714 through February 1, 2006 | 96 |
| Various other secured term notes payable to government agencies | 59 |
| | 6,05 |
| Less current portion | (37 |
| | $ 5,67 |

Industrial Development Revenue Bonds were issued by a government agency to finance the construction of the Company's headquarters/Advanced Technology facility. Annual sinking fund payments of $170,000 commenced December 1, 2000 and continue through 2013, with a final payment of $2,620,000 due December 1, 2014. The Company has agreed to reimburse the issuer of the letter of credit if there are draws on that letter of credit. The Company pays the letter of credit bank an annual fee of 1% of the amount secured thereby and pays the remarketing agent for the bonds an annual fee of .25% of the principal amount outstanding. The Company's interest under the facility capital lease has been pledged to secure its obligations to the government agency, the bank and the bondholders.

Principal maturities of long-term debt are as follows: 2003 - $378,000;

2004 - $463,000; 2005 - $418,000; 2006 - $312,000; 2007 and thereafter $4,481,000.

The Company also has a $1,000,000 line of credit on which there was no outstanding balance at December 31, 2002.

5. Employee benefit plans

Employee stock ownership plan (ESOP)

Under the Company's ESOP adopted in 1985, participating employees are awarded shares of the Company's common stock based upon eligible compensation and minimum service requirements. Upon inception of the



ESOP, the Company borrowed $2,000,000 from a bank and lent the proceeds to the trust established under the ESOP to purchase shares of the Company's common stock. The Company's loan to the trust is at an interest rate approximating the prime rate and is repayable to the Company over a 40-year term ending in December 2024. During 1987 and 1988, the Company loaned an additional $1,942,000 to the trust under terms similar to the Company's original loan. Each year the Company makes contributions to the trust which the plan's trustees use to repay the principal and interest due the Company under the trust loan agreement. Shares held by the trust are allocated in the aggregate to participating employees in proportion to the amount of the loan repayment made by the trust to the Company. Since inception of the ESOP, approximately 379,000 shares have been allocated, exclusive of shares distributed to ESOP participants. At December 31, 2002 and 2001, approximately 470,000 and 497,000 shares, respectively, purchased by the ESOP remain unallocated.

Related compensation expense associated with the Company's ESOP, which is equal to the principal reduction on the loans receivable from the trust, amounted to $101,000 in 2002 and 2001. Included as a reduction to shareholders' equity is the employee stock ownership trust commitment which represents the remaining indebtedness of the trust to the Company. Employees are entitled to vote allocated shares and the ESOP trustees are entitled to vote unallocated shares and those allocated shares not voted by the employees.

Defined benefit plan

The Company has noncontributory defined benefit pension plans. Plan benefits are based on stated amounts for each year of service; funding is in accordance with statutory requirements. Pension cost of $29,000 and $20,000 was recognized in 2002 and 2001, respectively, and was calculated using a weighted-average discount rate of 6.5% in 2002 and 7.0% in 2001, and weighted-average expected rate of return on plan assets of 8.0% for both years. The projected benefit obligation under the plan at December 31, 2002 was $90,000, net of $314,000 of plan assets at fair value.

Deferred compensation program

The Company maintains a deferred compensation program designed to achieve, among other things, benefit parity for an officer of the Company. During 2002, no amount was accrued under this program and

$24,000 was accrued during 2001. The current balance of $249,000 is reflected on the December 31, 2002 Consolidated Balance Sheet.



6. Income taxes

The provision (benefit) for income taxes included in the consolidated statement of operations consists of the following:

| | |
|---|---|
| | 2 |
| | --- |
| | ($0 |
| Current: | |
| Federal income tax (benefit) | ($ |
| State income tax | |
| | --- |
| | --- |
| Deferred: | |
| Federal income tax (benefit) | |
| State income tax | |
| | --- |
| | --- |
| | ($ |
| | == |

The reconciliation of the difference between the Company's effective tax rate based upon the total income tax provision (benefit) and the federal statutory income tax rate is as follows:

| | |
|---|---|
| | 2 |
| | --- |
| Statutory rate | ( |
| Increase resulting from: | |
| State income taxes (less federal effect) | |
| Extraterritorial income exclusion | |
| Nondeductible expenses | |
| Other | |
| | -- |
| | ( |
| | == |



At December 31, 2002, the deferred tax assets (liabilities) were comprised of the following:

($000's

| | |
|---|---|
| Inventory | $ |
| Accrued vacation | |
| Federal and state net operating losses and credits | |
| Deferred compensation | |
| Other | |
| Total deferred tax assets | |
| Property, plant and equipment | |
| Other liabilities | |
| Total deferred tax liabilities | |
| Net deferred tax asset | $ |

Realization of the net deferred tax asset is dependent upon generating sufficient taxable income over the periods in which the temporary differences are anticipated to reverse. Although realization is not assured, management believes it is more likely than not that the net deferred tax asset will be realized. However, the amount of net deferred tax asset considered realizable could be reduced in the near term if estimates of future taxable income are reduced.

At December 31, 2002, the Company has a Federal consolidated net operating loss carryforward of approximately $524,000 (approximately a $178,000 tax benefit) which begins to expire in 2022.

At December 31, 2002, the Company also has New York State net operating loss carryforwards of approximately $1,558,000 (approximately a $62,000 tax benefit) that begin to expire in 2019. The Company also has a State of Pennsylvania net operating loss carryforward of approximately $1,450,000 (approximately a $58,000 tax benefit) that begins to expire in 2008.



7. Common shareholders' equity

| | Common stock | | | | | | |
|---|---|---|---|---|---|---|---|
| | Number of shares issued | Amount | Capital in excess of par value | Retained earnings | ESOP | Treasury stock | Compreh inco |
| | ($000's omitted) | | | | | | |
| Balance December 31, 2000 | 2,614,506 | $523 | $13,361 | $ 794 | ($ 2,539) | ($ 955) | |
| Comprehensive income: | | | | | | | |
| Net income | - | - | - | $ 700 | - | - | $ |
| Other comprehensive income (loss), net of tax: | | | | | | | |
| Minimum pension liability adjustment | - | - | - | - | - | - | |

| | | | | | | | |
|---|---|---|---|---|---|---|---|
| Other comprehensive income (loss) | - | - | - | - | - | - | --- |
| Comprehensive income | - | - | - | - | - | - | $ |
| Compensation expense | - | - | - | - | 101 | | |
| Treasury stock | - | - | - | (3) | - | (99) | |
| Balance December 31, 2001 | 2,614,506 | $523 | $13,361 | $1,491 | ($ 2,438) | ($ 1,054) | |
| Comprehensive income (loss): | | | | | | | |
| Net income (loss) | - | - | - | $ (229) | - | - | $ |
| Other comprehensive income (loss), net of tax: | | | | | | | |
| Minimum pension liability adjustment | | - | - | - | - | - | |
| Other comprehensive income (loss) | - | - | - | - | - | - | --- |
| Comprehensive income (loss) | | - | - | - | - | - | $ |
| Compensation expense | - | - | - | - | 101 | - | |
| Balance December 31, 2002 | 2,614,506 | $523 | $13,361 | $1,262 | ($ 2,337) | ($ 1,054) | |



Earnings per share

Basic earnings per share is computed by dividing net earnings by the weighted average number of shares outstanding during the period. Diluted earnings per share is computed by dividing net earnings by the weighted average number of shares outstanding during the period plus the number of shares of common stock that would be issued assuming all contingently issuable shares having a dilutive effect on earnings per share were outstanding for the period.

| | Yea Dece 2002 ($000 except pe |
|---|---|
| Net income (loss) | $ (229) |
| Weighted average common shares outstanding (basic) | 1,898 |
| Incremental shares from assumed conversions of stock options | 0 |
| Weighted average common shares outstanding (diluted) | 1,898 |

| | |
|---|---|
| Basic | |
| Net income (loss) per share | $ (0.12) |
| Diluted | |
| Net income (loss) per share | $ (0.12) |

Comprehensive income (loss)

The minimum pension liability adjustment of $82,000, which is net of taxes amounting to $48,000, is the only component of other comprehensive income (loss) for 2002.



Stock options

Under the Servotronics, Inc. 2000 Employee Stock Option Plan authorized by the Board of Directors and the 2001 Long-Term Stock Incentive Plan authorized by the Board of Directors and the Shareholders, and other separate agreements authorized by the Board of Directors, the Company has granted non-qualified options to its Directors and Officers. The Company applies APB Opinion No. 25 and related interpretations in accounting for these Plans and the separate option agreements. Accordingly, no compensation expense has been charged to earnings in 2002 or prior years as stock options granted have an exercise price equal to the market price on the date of grant. At December 31, 2002, 301,600 shares of common stock were available under these plans. Options granted under these Plans have durations of ten years and vesting periods ranging from six months to three years.

A summary of the status of options granted under all employee plans is presented below:

| | Options Outstanding | Weighted Average Exercise Price ($) |
|---|---|---|
| Outstanding as of December 31, 2000 | 211,372 | 6.06 |
| Granted in 2001 | 125,000 | 4.38 |
| Exercised in 2001 | (17,172) | 5.787 |
| Forfeited in 2001 | - | - |
| Outstanding as of December 31, 2001 | 319,200 | 5.37 |
| Granted in 2002 | - | - |
| Exercised in 2002 | - | - |
| Forfeited in 2002 | - | - |
| Outstanding as of December 31, 2002 | 319,200 | 5.37 |

The following tables summarize information about options outstanding at

December 31, 2002:

| | Exercise Prices ($) | Number Outstanding | Remaining contractual Life | Options Exercisable |
|---|---|---|---|---|
| | 8.50 | 93,000 | 5 years | 93,000 |
| | 3.8125 | 101,200 | 8 years | 93,700 |
| | 4.38 | 125,000 | 9 years | 109,000 |
| Total | | 319,200 | | 295,700 |



The Company has adopted the disclosure-only provisions of SFAS No. 123, "Accounting for Stock-Based Compensation". If the compensation cost for these plans had been determined based on the Black-Scholes calculated values at the grant dates for awards consistent with the method prescribed by SFAS No. 123, the pro forma effects on the years ended December 31, 2002 and 2001 are as follows:

| | 2002 | 2001 |
|---|---|---|
| Net income (loss): | | |
| As reported | $(229,000) | $700,000 |
| Pro forma | $(406,000) | $521,000 |
| Earnings (loss) per common share: | | |
| As reported - basic | $(0.12) | $0.37 |
| As reported - diluted | $(0.12) | $0.37 |
| Pro forma - basic | $(0.21) | $0.28 |
| Pro forma - diluted | $(0.21) | $0.28 |

There were 125,000 options granted in 2001. The Black-Scholes calculated estimated value of the options granted in 2001 was $2.96. The assumptions used to calculate this value include a risk-free interest rate of 4.85%, an expected term of 10 years, and an annual standard deviation (volatility) factor of 50.9%. The Black-Scholes option pricing model was developed for use in estimating values of traded options that have no vesting restrictions and are fully transferable. In addition, option pricing models require the use of highly subjective assumptions, including the expected stock price volatility. Because the Company's stock options are restricted and have characteristics significantly different from those of traded options, and because changes in the subjective assumptions can materially affect the calculated estimated values, in the Company's opinion the existing models do not necessarily provide a reliable measure of the value of the Company's stock options. The estimated value calculated by the Black-Scholes methodology is hypothetical and does not represent an actual tangible Company expense or an actual tangible monetary transfer to the optionee. Further, for the reasons stated above (among others) and especially because of the volatility factor used in the Black-Scholes calculations for the Company's 2001 options, the derived estimated value may be, in the Company's opinion, substantially higher than the value which may be realized in an arms-length transaction under the above stated and existing conditions.

Shareholders' rights plan

During 2002, the Company's Board of Directors adopted a shareholders' rights plan (the "Rights Plan") and simultaneously declared a dividend distribution of one Right for each outstanding share of the Company's common stock outstanding at August 28, 2002. The Rights Plan replaced a previous shareholder right plan that was adopted in 1992 and expired on August 28, 2002. The Rights do not become exercisable until the earlier of (i) the date of the Company's public announcement that a person or affiliated group other than Dr. Nicholas D. Trbovich or the ESOP trust (an "Acquiring Person") has acquired, or obtained the right to acquire, beneficial ownership of 25% or more of the Company's common stock (excluding shares held by the ESOP trust) or (ii) ten business days following the commencement of a tender offer that would result in a person or affiliated group becoming an Acquiring Person.

The exercise price of a Right has been established at $32.00. Once exercisable, each Right would entitle the holder to purchase one one-hundredth of a share of Series A Junior Participating Preferred Stock. In the event that any person becomes an Acquiring Person, each Right would entitle any holder other than the Acquiring Person to purchase common stock or other securities of the Company having a value equal to three times the exercise price. The Board of Directors has the discretion in such event to exchange two shares of common stock or two one-hundredths of a share of preferred stock for each Right held by any holder other than the Acquiring Person.

8. Commitments

The Company leases certain equipment pursuant to operating lease arrangements. Total rental expense in 2002 and 2001 and future minimum payments under such leases are not significant.

9. Litigation

There are no legal proceedings which are material to the Company currently pending by or against the Company other than ordinary routine litigation incidental to the business which is not expected to materially adversely affect the business or earnings of the Company.

10. Business segments

The Company operates in two business segments, the Advanced Technology Group and the Consumer Products Group. The Company's reportable segments are strategic business units that offer different products and services. The segments are composed of separate corporations and are managed separately. Operations in the Advanced Technology Group involve the design, manufacture, and marketing of servo-control components for government and commercial applications. The Consumer Products Group's operations involve the design, manufacture and marketing of a variety of cutlery products for use by consumers and government agencies. The Company derives its primary sales revenue from domestic customers, although a significant portion of finished products are for foreign end use.

Information regarding the Company's operations in these segments is summarized as follows:

| Year ended December 31, 2002 | Advanced Technology Group | Consumer Products Group |
|---|---|---|
| | | ($000's omitted) |
| Revenues from unaffiliated customers | $ 10,213 | $ 5,394 |
| Profit (loss) | $ 1,080 | $ (41) |
| Depreciation expense | $ (506) | $ (154) |
| Interest expense | | |
| General corporate expense | | |
| Income (loss) before income taxes | | |
| Identifiable assets | $ 14,521 | $ 5,208 |
| Capital expenditures | $ 326 | $ 391 |

| Year ended December 31, 2001 | Advanced Technology Group | Consumer Products Group |
|---|---|---|
| | | ($000's omitted) |
| Revenues from unaffiliated customers | $ 12,186 | $ 5,749 |
| Profit | $ 2,259 | $ 167 |
| Depreciation expense | $ (434) | $ (154) |
| Interest expense | | |
| General corporate expense | | |
| Income before income taxes | | |
| Identifiable assets | $ 15,759 | $ 4,937 |
| Capital expenditures | $ 200 | $ 73 |



The Company engages in a significant amount of business with the United States

Government through sales to its prime contractors and otherwise. Such contracts by the Advanced Technology Group accounted for revenues of approximately \$3,400,000 in 2002 and \$3,082,000 in 2001. Similar contracts by the Consumer Products Group accounted for revenues of approximately \$192,000 in 2002 and \$299,000 in 2001. Sales of advanced technology products to one prime contractor, including various divisions and subsidiaries of a common parent company, amounted to approximately 18% and 23% of total revenues in 2002 and 2001, respectively. Sales to another customer amounted to approximately 21% and 22% of total revenues in 2002 and 2001, respectively. No other single customer represented more than 10% of the Company's revenues in any of these years.