

(Address of principal executive offices) (zip code)

(716) 655-5990

(Registrant's telephone number, including area code)

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 No

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (§232.405) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes No

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer, a smaller reporting company, or an emerging growth company. See the definitions of "large accelerated filer," "accelerated filer", "smaller reporting company" and "emerging growth company" in Rule 12b-2 of the Securities Exchange Act.

Large accelerated filer Accelerated filer Non-accelerated filer Smaller reporting company Emerging growth company

If an emerging growth company, indicate by check mark if the registrant has elected not to use the extended transition period for complying with any new or revised financial accounting standards provided pursuant to Section 13(a) of the Exchange Act.

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act).

Yes No

Edgar Filing: SERVOTRONICS INC /DE/ - Form 10-Q

Indicate the number of shares outstanding of each of the issuer's classes of common stock, as of the latest practicable date.

Class	Outstanding at October 31, 2017
Common Stock, \$.20 par value	2,511,076

INDEX

	Page No.
 PART I. FINANCIAL INFORMATION	
Item 1. Financial Statements (Unaudited):	
a) <u>Consolidated Balance Sheets, September 30, 2017 and December 31, 2016 (Audited)</u>	<u>3</u>
b) <u>Consolidated Statements of Income for the three and nine months ended September 30, 2017 and 2016</u>	<u>4</u>
c) <u>Consolidated Statements of Cash Flows for the nine months ended September 30, 2017 and 2016</u>	<u>5</u>
d) <u>Notes to Consolidated Financial Statements</u>	<u>6</u>
Item 2. <u>Management’s Discussion and Analysis of Financial Condition and Results of Operations</u>	<u>16</u>
Item 3. <u>Quantitative and Qualitative Disclosures About Market Risk</u>	<u>20</u>
Item 4. <u>Controls and Procedures</u>	<u>20</u>
 PART II. OTHER INFORMATION	
Item 1. <u>Legal Proceedings</u>	<u>21</u>
Item 1A. <u>Risk Factors</u>	<u>21</u>
Item 2. <u>Unregistered Sales of Equity Securities and Use of Proceeds</u>	<u>21</u>
Item 3. <u>Defaults Upon Senior Securities</u>	<u>21</u>
Item 4. <u>Mine Safety Disclosures</u>	<u>21</u>
Item 5. <u>Other Information</u>	<u>21</u>
Item 6. <u>Exhibits</u>	<u>22</u>
<u>Forward-Looking Statement</u>	<u>22</u>
<u>Signatures</u>	<u>23</u>

SERVOTRONICS, INC. AND SUBSIDIARIES**CONSOLIDATED BALANCE SHEETS**

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

	September 30, 2017 (Unaudited)	December 31, 2016
Current assets:		
Cash and cash equivalents	\$ 2,045	\$ 3,515
Accounts receivable, net	9,100	7,439
Inventories, net	12,993	13,293
Prepaid income taxes	363	182
Other current assets	363	387
Total current assets	24,864	24,816
Property, plant and equipment, net	11,021	9,937
Deferred income taxes	491	491
Other non-current assets	385	376
Total Assets	\$ 36,761	\$ 35,620
Liabilities and Shareholders' Equity		
Current liabilities:		
Current portion of long-term debt	\$ 548	\$ 548
Accounts payable	2,500	2,080
Accrued employee compensation and benefits costs	2,414	1,945
Other accrued liabilities	680	426
Total current liabilities	6,142	4,999
Long-term debt	2,567	2,976
Post retirement obligation	528	528
Shareholders' equity:		
Common stock, par value \$0.20; authorized 4,000,000 shares; issued 2,614,506 shares; outstanding 2,290,527 (2,310,148 - 2016) shares	523	523
Capital in excess of par value	14,168	14,160
Retained earnings	15,194	14,768
Accumulated other comprehensive loss	(20)	(20)

Edgar Filing: SERVOTRONICS INC /DE/ - Form 10-Q

Employee stock ownership trust commitment	(763)	(763)
Treasury stock, at cost 183,983 (164,066 - 2016) shares	(1,578)	(1,551)
Total shareholders' equity	27,524		27,117	
Total Liabilities and Shareholders' Equity	\$ 36,761		\$ 35,620	

See notes to consolidated financial statements

- 3 -

SERVOTRONICS, INC. AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF INCOME**

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

(Unaudited)

	Three Months Ended September 30,		Nine Months Ended September 30,	
	2017	2016	2017	2016
Revenue	\$ 11,325	\$ 9,465	\$ 30,044	\$ 28,708
Cost, expenses and other (income):				
Cost of goods sold, exclusive of depreciation and amortization	8,036	7,043	22,706	20,888
Selling, general and administrative	2,080	1,658	5,523	4,815
Depreciation and amortization	209	198	637	610
Interest expense	18	18	56	54
Other income, net	(6)	(9)	(11)	(19)
Total expenses	10,337	8,908	28,911	26,348
Income before income tax provision	988	557	1,133	2,360
Income tax provision	317	191	331	732
Net income	\$ 671	\$ 366	\$ 802	\$ 1,628
Income per share:				
Basic				
Net Income per share	\$ 0.30	\$ 0.17	\$ 0.35	\$ 0.74
Diluted				
Net income per share	\$ 0.29	\$ 0.16	\$ 0.35	\$ 0.71

See notes to consolidated financial statements

SERVOTRONICS, INC. AND SUBSIDIARIES**CONSOLIDATED STATEMENTS OF CASH FLOWS**

(\$000's omitted)

(Unaudited)

	Nine Months Ended September 30, 2017	2016
Cash flows related to operating activities:		
Net Income	\$ 802	\$ 1,628
Adjustments to reconcile net income to net cash provided (used) by operating activities:		
Depreciation and amortization	637	610
Loss on disposal of property	16	-
Stock based compensation	176	386
Increase in inventory reserve	43	14
Increase (decrease) in allowance for doubtful accounts	72	(8)
Change in assets and liabilities:		
Accounts receivable	(1,733)	(501)
Inventories	257	(1,466)
Prepaid income taxes	(181)	63
Other current assets	24	(75)
Other non-current assets	(9)	(6)
Accounts payable	(88)	598
Accrued employee compensation and benefit costs	469	(16)
Other accrued liabilities	254	145

Net cash provided by operating activities	739		1,372	
Cash flows related to investing activities:				
Capital expenditures - property, plant and equipment	(1,401)	(786)
Proceeds from sale of assets	180		-	
Net cash used in investing activities	(1,221)	(786)
Cash flows related to financing activities:				
Principal payments on long-term debt	(409)	(410)
Purchase of treasury shares	(203)	(197)
Cash dividend	(376)	(380)
Net cash used in financing activities	(988)	(987)
Net decrease in cash and cash equivalents	(1,470)	(401)
Cash and cash equivalents at beginning of period	3,515		3,268	
Cash and cash equivalents at end of period	\$ 2,045		\$ 2,867	

See notes to consolidated financial statements

SERVOTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Basis of Presentation

The accompanying unaudited consolidated financial statements have been prepared in accordance with United States generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 8 of Regulation S-X. Accordingly, they do not include all of the information and footnotes required by United States generally accepted accounting principles for complete financial statements.

The accompanying consolidated financial statements reflect all adjustments which are, in the opinion of management, necessary for a fair statement of the results for the interim periods presented. All such adjustments are of a normal recurring nature. Operating results for the three and nine months ended September 30, 2017 are not necessarily indicative of the results that may be expected for the year ending December 31, 2017. The consolidated financial statements should be read in conjunction with the 2016 annual report and the notes thereto.

2. Business Description and Summary of Significant Accounting Policies

Business Description

Servotronics, Inc. and its subsidiaries design, manufacture and market advanced technology products consisting primarily of control components, and consumer products consisting of knives and various types of cutlery and other edged products.

Principles of Consolidation

The consolidated financial statements include the accounts of Servotronics, Inc. and its wholly-owned subsidiaries (the "Company"). All intercompany balances and transactions have been eliminated upon consolidation.

Cash and Cash Equivalents

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

Accounts Receivable

The Company grants credit to substantially all of its customers and carries its accounts receivable at original invoice amount less an allowance for doubtful accounts. On a periodic basis, the Company evaluates its accounts receivable and establishes an allowance for doubtful accounts based on history of past write-offs, collections, and current credit conditions. The allowance for doubtful accounts amounted to approximately \$149,000 at September 30, 2017 and \$77,000 at December 31, 2016. The Company does not accrue interest on past due receivables.

Revenue Recognition

Revenues are recognized as services are rendered or as units are shipped and at the designated FOB point consistent with the transfer of title, risks and rewards of ownership. Such purchase orders generally include specific terms relative to quantity, item description, specifications, price, customer responsibility for in-process costs, delivery schedule, shipping point, payment and other standard terms and conditions of purchase.

Inventories

Inventories are stated at the lower of cost or net realizable value. Cost includes all costs incurred to bring each product to its present location and condition. Market provisions in respect of lower of cost or market adjustments and inventory expected to be used in greater than one year are applied to the gross value of the inventory through a reserve of approximately \$1,556,000 and \$1,513,000 at September 30, 2017 and December 31, 2016, respectively. Pre-production and start-up costs are expensed as incurred.

SERVOTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The purchase of suppliers' minimum economic quantities of material such as steel, etc. may result in a purchase of quantities exceeding one year of customer requirements. Also, in order to maintain a reasonable and/or agreed to lead time, certain larger quantities of other product support items may have to be purchased and may result in over one year's supply. These amounts are not included in the inventory reserve discussed above.

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 expensed as incurred. Upon 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 income 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	5-40 years
Machinery and equipment	5-20 years
Tooling	3-5 years

Income Taxes

The Company recognizes deferred tax assets and liabilities for the expected future tax consequences of temporary differences between the carrying amounts and the tax basis of assets and liabilities, as well as operating loss and credit carryforwards. The Company and its subsidiaries file a consolidated federal income tax return, combined New York and Texas state income tax returns and separate Pennsylvania and Arkansas income tax returns.

The Company's practice is to recognize interest and/or penalties related to income tax matters in income tax expense. The Company did not have any accrued interest or penalties included in its consolidated balance sheets at September 30, 2017 or December 31, 2016, and did not recognize any interest and/or penalties in its consolidated statements of income during the nine months ended September 30, 2017 and 2016. The Company did not have any material uncertain tax positions or unrecognized tax benefits or obligations as of September 30, 2017 and December 31, 2016. The 2014 through 2016 federal and state tax returns remain subject to examination.

Supplemental Cash Flow Information

Income taxes paid during the nine months ended September 30, 2017 and 2016 amounted to approximately \$165,000 and \$644,000, respectively. Interest paid amounted to approximately \$56,000 and \$54,000, respectively, during the nine months ended September 30, 2017 and 2016. Equipment received but not placed in service and included in accounts payable at September 30, 2017 amounted to approximately \$508,000.

SERVOTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Employee Stock Ownership Plan

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

Impairment of Long-Lived Assets

The Company reviews long-lived assets for impairment annually or whenever events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable based on undiscounted future operating cash flow analyses. If an impairment is determined to exist, any related impairment loss is calculated based on fair value. Impairment losses on assets to be disposed of, if any, are based on the estimated proceeds to be received, less costs of disposal. The Company has determined that no impairment of long-lived assets existed at September 30, 2017 and December 31, 2016.

Use of Estimates

The preparation of the consolidated financial statements in conformity with U.S. generally accepted accounting principles (GAAP) 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 consolidated financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

Reclassifications

Certain balances, as previously reported, were reclassified to conform with classifications adopted in the current period.

Research and Development Costs

Research and development costs are expensed as incurred.

Concentration of Credit Risks

Financial instruments that potentially subject the Company to concentration of credit risks principally consist of cash accounts in financial institutions. Although the accounts exceed the federally insured deposit amount, management does not anticipate nonperformance by the financial institutions.

Fair Value of Financial Instruments

The carrying amount of cash and cash equivalents, accounts receivable, accounts payable and accrued expenses are reasonable estimates of their fair value due to their short maturity. Based on variable interest rates and the borrowing rates currently available to the Company for loans similar to its long-term debt, the fair value approximates its carrying amount.

Recent Accounting Pronouncements

Effective January 1, 2017, the Company adopted new guidance issued by the Financial Accounting Standards Board (“FASB”) ASU 2015-11, “Inventory (Topic 330): Simplifying the Measurement of Inventory”. The ASU changes the measurement principle for certain inventory methods from the lower of cost or market to the lower of cost and net realizable value. Adoption of this new guidance had no impact on the Company’s consolidated results of operations and financial position.

SERVOTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Effective January 1, 2017, the Company adopted new guidance issued by the FASB ASU 2015-17, "Balance Sheet Classification of Deferred Taxes". The guidance requires that all deferred tax assets and deferred tax liabilities, along with any related valuation allowance, be classified as noncurrent on the balance sheet. Adoption of this new guidance during the reporting period resulted in the reclassification of a deferred tax liability, of \$661,000 from current to noncurrent at September 30, 2017 and December 31, 2016. The deferred tax liability, for both reporting periods offsets the deferred tax asset, as presented on the balance sheet at September 30, 2017 and December 31, 2016.

Effective January 1, 2017, the Company adopted new guidance issued by the FASB ASU 2016-09, "Compensation – Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting," which amends the current stock compensation guidance. The amendments simplify the accounting for the taxes related to stock based compensation, including adjustments to how excess tax benefits and a Company's payments for tax withholdings should be classified. Adoption of this new guidance has not had a material impact on the Company's consolidated results of operations and financial position.

Effective January 1, 2017, the Company selected early adoption of the new guidance issued by the FASB ASU 2017-04, "Intangibles – Goodwill and Other (Topic 350): Simplifying the Test for Goodwill Impairment," which removes the requirement to compare the implied fair value of goodwill with its carrying amount as part of step 2 of the goodwill impairment test. Adoption of this new guidance has not had a material impact on the Company's consolidated results of operations and financial position.

In March 2017, the FASB issued ASU 2017-07, "Compensation-Retirement Benefits (Topic 715): Improving the Presentation of Net Periodic Pension Cost and Net Periodic Postretirement Benefit Cost," which requires employers to present the service cost component of net periodic benefit cost in the same income statement line item(s) as other employee compensation costs arising from services rendered during the period. Only the service cost component will be eligible for capitalization in assets. The other components of net periodic benefit cost will be presented separately from the line item(s) that includes the service cost and outside of any subtotal of operating income, if one is presented. This update is effective for annual periods beginning after December 15, 2017.

In May 2014, the FASB issued ASU 2014-09, "Revenue from Contracts with Customers (Topic 606)." The new revenue recognition standard outlines a comprehensive model for companies to use in accounting for revenue arising from contracts with customers and supersedes most current revenue recognition guidance, including industry-specific guidance. In August 2015, the FASB affirmed its proposal to defer the effective date of the standard to annual reporting periods (and interim reporting periods within those years) beginning after December 15, 2017. Entities are

permitted to apply the new revenue standard early, but not before the original effective date of annual periods beginning after December 15, 2016. The Company's revenues are recognized as services are rendered or as units are shipped and at the designated FOB point. The Company does not believe the adoption will have a material impact on our consolidated financial statements.

In February 2016, the FASB issued ASU 2016-02, "Leases (Topic 842)." There are elements of the new standard that could impact almost all entities to some extent, although the lessees will likely see the most significant changes. Lessee will need to recognize virtually all of their leases on the balance sheet, by recording the right-of-use asset and a lease liability. Public business entities are required to adopt the new leasing standard for fiscal years, and interim period within those fiscal years, beginning December 15, 2018. For calendar year-end public companies, this means an adoption date of January 1, 2019. Early adoption is permitted. The Company does not believe the adoption will have a material impact on the financial statements and disclosures.

SERVOTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

3. Inventories

	September 30, 2017	December 31, 2016
	(\$000's omitted)	
Raw material and common parts, net of reserve	\$7,930	\$ 7,618
Work-in-process	3,123	2,062
Finished goods, net of reserve	1,940	3,613
Total inventories	\$12,993	\$ 13,293

4. Property, Plant and Equipment

	September 30, 2017	December 31, 2016
	(\$000's omitted)	
Land	\$7	\$ 21
Buildings	10,144	10,422
Machinery, equipment and tooling	16,285	15,826
Construction in progress	1,544	77
	27,980	26,346
Less accumulated depreciation	(16,959)	(16,409)
	\$11,021	\$ 9,937

As previously disclosed, the Company through a wholly-owned subsidiary, entered into a contract to sell unused commercial real property in Franklinville, New York for approximately \$180,000. The sale transaction closed on March 9, 2017 and the wholly-owned subsidiary recognized a de minimis loss on the sale.

The Company has purchased and received two pieces of equipment in the amount of approximately \$688,000. Both pieces of equipment will be paid using the Company's new lease line of credit for equipment financing dated August 17, 2017. As of September 30, 2017 neither piece of equipment has been put into service.

Depreciation and amortization expense amounted to approximately \$637,000 and \$610,000 for the nine months ended September 30, 2017 and 2016, respectively. Depreciation and amortization expense amounted to approximately \$209,000 and \$198,000 for the three months ended September 30, 2017 and 2016, respectively. 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.

- 10 -

SERVOTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

As of September 30, 2017, there is approximately \$1,544,000 (\$77,000 – 2016) of construction in progress included in property, plant and equipment primarily related to capital projects at the Advanced Technology Group (“ATG”), including the equipment covered under the equipment financing agreement. See Note 7, Commitments and Contingencies, for more information on anticipated capital expenditures.

5. Long-Term Debt

	September 30, 2017	December 31, 2016
	(\$000's omitted)	
Term loan payable to a financial institution; Interest rate option of bank prime or Libor plus 1.4% (2.64% as of September 30, 2017), monthly principal payments of \$21,833 through 2021 with a balloon payment of \$786,000 due December 1, 2021	\$ 1,901	\$ 2,096
Term loan payable to a financial institution; Interest rate option of bank prime or Libor plus 1.4% (2.64% as of September 30, 2017), monthly principal payments of \$23,810 through December 1, 2021	1,214	1,428
	3,115	3,524
Less current portion	(548)	(548)
	\$2,567	\$ 2,976

The Company renewed a \$2,000,000 line of credit available until June 20, 2018. There was no balance outstanding at September 30, 2017 and December 31, 2016.

The term loans are secured by all personal property of the Company with the exception of certain equipment that was purchased from proceeds of government grants.

Certain lenders require the Company to comply with debt covenants as described in the specific loan documents, including a debt service ratio. At September 30, 2017 and December 31, 2016 the Company was in compliance with these covenants.

The Company established a lease line of credit for equipment financing in the amount of \$1,000,000 available until June 28, 2018. This line is non-revolving and non-renewable. The lease term for equipment covered by the lease line of credit is sixty months. Monthly payments will be fixed for the term of each funding based upon the Lender's lease pricing in effect at the time of such funding. There was no balance outstanding at September 30, 2017.

- 11 -

SERVOTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

6. Shareholders' Equity

	Common Stock		(\$000's omitted except for share data)				Accumulated	
	Number of shares issued	Amount	Capital in excess of par value	Retained earnings	ESOT	Treasury stock	Other Comprehensive Loss	Total Shareholders' equity
Balance at December 31, 2016	2,614,506	\$ 523	\$ 14,160	\$ 14,768	\$(763)	\$(1,551)	\$ (20)	\$ 27,117
Net income				802				802
Purchase of treasury shares			-			(203)		(203)
Cash dividend				(376)				(376)
Stock based compensation, net of tax benefit	-	-	8	-	-	176	-	184
Balance at September 30, 2017	2,614,506	\$ 523	\$ 14,168	\$ 15,194	\$(763)	\$(1,578)	\$ (20)	\$ 27,524

The Company's Board of Directors authorized the purchase of up to 450,000 shares of its common stock in the open market or in privately negotiated transactions. As of September 30, 2017, the Company has purchased 349,330 shares and there remains 100,670 shares available to purchase under this program. There were 19,917 shares purchased by the Company during the nine month period ended September 30, 2017.

On April 11, 2016, the Company issued 51,000 shares of restricted stock to Executive Officers and certain key management of the Company under the Company's 2012 Long-Term Incentive Plan. The restricted share awards have varying vesting periods between January 2017 and January 2018; however, these shares have voting rights and accrue dividends prior to vesting. The aggregate amount of expense to the Company, measured based on grant date fair value is expected to be approximately \$370,000 and will be recognized over the requisite service period.

Included in the nine months ended September 30, 2017 and 2016 is approximately \$176,000 and \$386,000, respectively, of stock-based compensation expense related to the restrictive share awards.

On January 1, 2017, 39,750 shares of restricted stock vested of which 15,991 shares were withheld and repurchased by the Company for approximately \$160,000 to satisfy statutory minimum withholding tax requirements for those participants who elected this option as permitted under the Company's 2012 Long-Term Incentive Plan. Additionally, upon the death of Servotronics' Chairman of the Board and Chief Executive Officer (CEO), 15,000 restricted shares awarded to the Chairman and CEO vested.

On May 16, 2017 the Company announced that its Board of Directors declared a \$0.15 per share cash dividend. The dividend was subsequently paid on July 14, 2017 to shareholders of record on June 30, 2017 and was approximately \$376,000 in the aggregate. These dividends do not represent that the Company will pay dividends on a regular or scheduled basis. The amount is a reduction to retained earnings on the accompanying consolidated balance sheet.

Earnings Per Share

Basic earnings per share is computed by dividing net earnings by the weighted average number of shares outstanding during the period. The weighted average number of common shares outstanding does not include any potentially dilutive securities or any unvested restricted shares of common stock. These unvested restricted shares, although classified as issued and outstanding, are considered forfeitable until the restrictions lapse and will not be included in the basic EPS calculation until the shares are vested. 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 the earnings per share that were outstanding for the period. Incremental shares from assumed conversions are calculated as the number of shares that would be issued, net of the number of shares that could be purchased in the marketplace with the cash received upon stock option exercise. The dilutive effect of unvested restrictive stock is determined using the treasury stock method.

SERVOTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

	Three Months Ended		Nine Months Ended	
	September 30,		September 30,	
	2017	2016	2017	2016
	(\$000's omitted except per share data)			
Net Income	\$ 671	\$ 366	\$ 802	\$ 1,628
Weighted average common shares outstanding (basic)	2,262	2,219	2,264	2,203
Unvested restricted stock	29	92	29	92
Weighted average common shares outstanding (diluted)	2,291	2,311	2,293	2,295
Basic				
Net income per share	\$ 0.30	\$ 0.17	\$ 0.35	\$ 0.74
Diluted				
Net income per share	\$ 0.29	\$ 0.16	\$ 0.35	\$ 0.71

7. Commitments and Contingencies

Post retirement obligation. As previously disclosed in filings with the Securities and Exchange Commission (“SEC”), the Company, under an employment agreement, is expected to pay post employment health related benefits to the former Executive Officer of the Company. Approximately \$528,000 has been accrued as of September 30, 2017 and is reflected as Post Retirement Obligation in the accompanying balance sheet.

Facility Expansion. As previously disclosed, the Company has commenced a multi-year investment plan designed to consolidate the operations of the Consumer Products Group (“CPG”). The five year plan included the construction of an approximate 28,000 square foot addition, capital improvements to the existing plant, the reconfiguration of its production process within the expanded facility, and the addition of new state of the art knife-making equipment. The Company broke ground in the second quarter of 2014 and began manufacturing in the newly constructed facility in the fourth quarter of 2015. The cost of the project was approximately \$4,000,000 over a five year period of which \$3,432,000 was completed as of September 30, 2017 and is included in property, plant and equipment.

The CPG was awarded certain incentives from the County of Cattaraugus Industrial Development Agency (CCIDA) in connection with the expansion of the Company’s facility in Franklinville, New York and other proposed capital expenditures. The incentives include certain real property tax and sales tax abatements in connection with the proposed project. The Company’s CPG entered into customary lease and leaseback arrangements with the CCIDA to facilitate the various tax incentives.

SERVOTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

The Company's CPG was awarded a \$300,000 grant from Cattaraugus County, New York. The grant was used towards new manufacturing equipment in connection with the proposed expansion project. As part of the terms of the Grant Contract with Cattaraugus County, the Company's CPG has agreed to maintain certain employment levels for a period of five years from the date of the agreement, March 13, 2014. If the employment levels are not maintained, the Company will be required to repay the grant proceeds on a prorated basis. The Company has maintained the required employment levels as of September 30, 2017.

8. Litigation

Litigation. The Company has pending litigation relative to leases of certain equipment and real property with a former related party, Aero, Inc. Aero, Inc. is suing Servotronics, Inc. and its wholly owned subsidiary and has alleged damages in the amount of \$3,000,000. The Company has filed a response to the Aero, Inc. lawsuit and has also filed a counter-claim in the amount of \$3,191,000. The Company considers the risk of loss remote, and is unable to reasonably or accurately estimate the likelihood and amount of any liability or benefit that may be realized as a result of this litigation. Accordingly, no gain or loss has been recognized in the accompanying financials statements related to this litigation.

There are no other legal proceedings currently pending by or against the Company other than litigation incidental to the business, which is not expected to have a material adverse effect on the business or earnings of the Company.

9. Related Party Transactions

The Company paid legal fees and disbursements of approximately \$188,000 and \$65,000 in the nine month period ended September 30, 2017 and 2016, respectively, for services provided by a law firm that is owned by a member of the Company's Board of Directors. Legal fees paid for the three month period ended September 30, 2017 and 2016 amounted to approximately \$44,000 and \$41,000, respectively. As of September 30, 2017, the Company had accrued additional legal fees of approximately \$39,000 with this firm.

10. Business Segments

The Company operates in two business segments, ATG and CPG. 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 ATG primarily involve the design, manufacture, and marketing of servo-control components (i.e., torque motors, control valves, actuators, etc.) for government, commercial and industrial applications. CPG'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 portion of finished products are for foreign end use.

As of September 30, 2017, the Company had identifiable assets of approximately \$36,761,000 (\$35,620,000 – December 31, 2016) of which approximately \$25,477,000 (\$24,037,000 – December 31, 2016) was for ATG and approximately \$11,284,000 (\$11,583,000 – December 31, 2016) was for CPG.

SERVOTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

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

	(\$000's omitted)					
	ATG		CPG		Consolidated	
	Nine Months Ended		Nine Months Ended		Nine Months Ended	
	September 30,		September 30,		September 30,	
	2017	2016	2017	2016	2017	2016
Revenues from unaffiliated customers	\$23,968	\$23,023	\$ 6,076	\$ 5,685	\$30,044	\$28,708
Cost of goods sold, exclusive of depreciation and amortization	(17,407)	(16,060)	(5,299)	(4,828)	(22,706)	(20,888)
Selling, general and administrative	(4,133)	(3,477)	(1,390)	(1,338)	(5,523)	(4,815)
Depreciation and amortization	(443)	(412)	(194)	(198)	(637)	(610)
Interest expense	(32)	(32)	(24)	(22)	(56)	(54)
Other income, net	9	19	2	-	11	19
Income (loss) before income tax provision (benefits)	1,962	3,061	(829)	(701)	1,133	2,360
Income tax provision (benefits)	580	949	(249)	(217)	331	732
Net income (loss)	\$1,382	\$2,112	\$ (580)	\$ (484)	\$802	\$1,628
Capital expenditures	\$1,777	\$613	\$ 124	\$ 173	\$1,901	\$786

	(\$000's omitted)					
	ATG		CPG		Consolidated	
	Three Months Ended		Three Months Ended		Three Months Ended	
	September 30,		September 30,		September 30,	
	2017	2016	2017	2016	2017	2016
Revenues from unaffiliated customers	\$8,918	\$7,658	\$ 2,407	\$ 1,807	\$ 11,325	\$ 9,465
Cost of goods sold, exclusive of depreciation and amortization	(6,062)	(5,418)	(1,974)	(1,625)	(8,036)	(7,043)
Selling, general and administrative	(1,640)	(1,240)	(440)	(418)	(2,080)	(1,658)
Depreciation and amortization	(143)	(137)	(66)	(61)	(209)	(198)
Interest expense	(9)	(11)	(9)	(7)	(18)	(18)
Other income, net	5	9	1	-	6	9
Income (loss) before income tax provision (benefits)	1,069	861	(81)	(304)	988	557
Income tax provision (benefits)	341	289	(24)	(98)	317	191
Net income (loss)	\$728	\$572	\$ (57)	\$ (206)	\$ 671	\$ 366
Capital expenditures	\$1,282	\$70	\$ 48	\$ 15	\$ 1,330	\$ 85

11. Other Income

Components of other income include interest income on cash and cash equivalents, and other amounts not directly related to the sale of the Company's products. Other income is immaterial in relationship to the consolidated financial statements.

12. Subsequent Events

None.

- 15 -

Item 2. Management's Discussion and Analysis of Financial Condition and Results of Operations Overview

During the three months ended September 30, 2017, approximately 13% of the Company's revenues were derived from contracts with agencies of the U.S. Government or their prime contractors and their subcontractors. This compares to the approximately 10% for the same three months ended 2016. During the nine months ended September 30, 2017, approximately 11% of the Company's revenues were derived from contracts with agencies of the U.S. Government or their prime contractors and their subcontractors. This compares to the approximately 9% for the same nine months ended 2016. The Company believes that government involvement in military operations overseas will continue to have an impact on the financial results in both the Advanced Technology and Consumer Products markets. While the Company is optimistic in relation to these potential opportunities, it recognizes that sales to the government are affected by defense budgets, the foreign policies of the U.S. and other nations, the level of military operations and other factors, and as such, it is difficult to predict the impact on future financial results.

The Company's commercial business is affected by such factors as uncertainties in today's global economy, global competition, the vitality and ability of the commercial aviation industry to purchase new aircraft, the effects and threats of terrorism, market demand and acceptance both for the Company's products and its customers' products which incorporate Company made components.

The ATG engages in business development efforts in its primary markets and is broadening its activities to include new domestic and foreign markets that are consistent with its core competencies. We believe our business remains particularly well positioned in the strong commercial aircraft market driven by the replacement of older aircraft with more fuel efficient alternatives and the increasing demand for air travel in emerging markets. Although the ATG backlog continues to be strong, actual scheduled shipments may be delayed/changed as a function of the Company's customers' final delivery determinations based on changes in the global economy and other factors.

In response to ongoing reductions in military spending, the CPG continues to diversify its revenue streams with a broader government focus and new commercial channels, including the addition of national retailers, international accounts, and a direct-to-consumer business line. The CPG is also actively growing its custom manufacturing business to provide a wide range of metal and plastic fabrication services to a variety of consumer and industrial companies. New product development is focused on the commercialization of products with applications that span government and civilian requirements to maximize demand or that open up new lines of business entirely.

See also Note 10, Business Segments, for information concerning business segment operating results.

Results of Operations

The following table compares the Company's consolidated statements of income data for the nine and three months ended September 30, 2017 and 2016 (\$000's omitted):

	(\$000's omitted except per share data) Nine Months Ended September 30,						2017 vs 2016	
	2017		2016		Dollar	%		
	Dollars	% of Sales	Dollars	% of Sales	Change	(Decrease)		
Revenues:								
Advanced Technology	\$23,968	79.8	% \$23,023	80.2	% \$945	4.1	%	
Consumer Products	6,076	20.2	% 5,685	19.8	% 391	6.9	%	
	30,044	100.0	% 28,708	100.0	% 1,336	4.7	%	
Cost of goods sold, exclusive of depreciation and amortization	22,706	75.6	% 20,888	72.8	% 1,818	8.7	%	
Selling, general and administrative	5,523	18.4	% 4,815	16.8	% 708	14.7	%	
Depreciation and amortization	637	2.1	% 610	2.1	% 27	4.4	%	
Total costs and expenses	28,866	96.1	% 26,313	91.7	% 2,553	9.7	%	
Operating income, net	1,178	3.9	% 2,395	8.3	% (1,217)	-50.8	%	
Interest expense	56	0.2	% 54	0.2	% 2	3.7	%	
Other income, net	(11)	-0.1	% (19)	-0.1	% 8	-42.1	%	