AEROSONIC CORP /DE/
Form 10-K
May 02, 2011

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D.C. 20549

FORM 10-K

Annual Report Pursuant to Section 13 or 15(d) of
The Securities Exchange Act of 1934

For the Fiscal Year Ended January 31, 2011
Commission File Number 1-11750

AEROSONIC CORPORATION
(Exact name of registrant as specified in its charter)

Delaware	74-1668471
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1212 North Hercules Avenue
Clearwater, Florida 33765
(Address of principal executive offices and Zip Code)

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

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

Title of Each Class	Name of Each Exchange on Which Registered
Common Stock, $.40 par value	NYSE Amex

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

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act
Yes ¨ No x

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Securities Act Yes ¨ No x

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 (the "Exchange Act") during the preceding 12 months (or for such shorter period that the registrant was required to file such reports), and (2) has been subject to such filing requirements for the past 90 days. Yes x No ¨

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate website, if any,

every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T 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 if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K ¨.

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See definition of "large accelerated filer", "large accelerated filer", "non-accelerated filer and "small reporting company" in Rule 12b-2 of the Exchange Act. (Check one)

Large accelerated filer ¨ Accelerated filer ¨ Non-accelerated filer (do not check if a smaller reporting company) ¨ Smaller reporting company x

Indicate by check mark whether the registrant is a shell company (as defined in Rule 12b-2 of the Exchange Act). Yes ¨ No x

The aggregate market value of the common stock held by non-affiliates of the registrant as of July 30, 2010, the last business day of the registrant's most recently completed second quarter was approximately $13,821,000, based upon the closing price of the common stock on the NYSE Amex (formerly the "American Stock Exchange" "AMEX") on that date.

As of May 2, 2011, the issuer had 3,753,675 shares of Common Stock outstanding, net of treasury shares.

Documents Incorporated by Reference:

Incorporation by reference: Portions of registrant's definitive proxy statement for the 2011 Annual Meeting of Stockholders to be held July 14, 2011 into Part III of this Form 10-K. The definitive proxy statement is expected to be filed with the Securities and Exchange Commission within 120 days after the close of the fiscal year covered by this Form 10-K.

Forward-Looking Statements

Unless stated to the contrary, or unless the context otherwise requires, references to "Aerosonic," "the Company," "we," "our" or "us" in this report include Aerosonic Corporation and its subsidiaries.

Certain statements made in this Annual Report on Form 10-K that are not statements of historical or current facts are forward-looking statements within the meaning of the Private Securities Litigation Reform Act of 1995. Forward-looking statements may involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from historical results or from any future results expressed or implied by such forward-looking statements.

In addition to statements that explicitly describe such risks and uncertainties, readers are urged to consider statements in future or conditional tenses or, include terms such as "believes," "belief," "expects," "intends," "anticipates" or "plans" to be uncertain and forward-looking. Forward-looking statements may include comments as to our beliefs and expectations as to future events and trends affecting our business. Forward-looking statements are based upon management's current expectations concerning future events and trends and are necessarily subject to uncertainties, many of which are outside of our control. The factors set forth in Item 1A. Risk Factors, as well as other factors, could cause our actual results to differ materially from those reflected or predicted in forward-looking statements.

If one or more of these or other risks or uncertainties materialize, or if the underlying assumptions prove to be incorrect, actual results may vary materially from those reflected in or suggested by forward-looking statements. Any forward-looking statement you read in this Annual Report on Form 10-K reflects our current views with respect to future events and is subject to these and other risks, uncertainties and assumptions relating to our operations, results of operations, growth strategy and liquidity. All subsequent written and oral forward-looking statements attributable to us or individuals acting on our behalf are expressly qualified in their entirety by this paragraph. You should specifically consider the factors identified in this Annual Report on Form 10-K that would cause actual results to differ from those referred to in forward-looking statements.

Any forward-looking statements are based on management's beliefs and assumptions, using information currently available to us. We assume no obligation for updating, and do not intend to update, these forward-looking statements.

We have a January 31 fiscal year end. Accordingly, all references in this Annual Report on Form 10-K to a fiscal year mean the fiscal year ended on January 31 of the referenced year; for example, references to fiscal year 2011 mean the fiscal year ended January 31, 2011.

PART I

ITEM 1. BUSINESS

General

We are a Delaware corporation formerly known as Instrument Technology Corporation ("ITC"). ITC, which was incorporated in 1968, was the surviving corporation of a merger, in 1970, with Aerosonic Corp., a Florida corporation. Aerosonic Corp., which was incorporated in 1957, ceased to exist as a separate corporation as a result of the merger. Following the merger, ITC changed its name to Aerosonic Corporation. In January 1993, we acquired Avionics Specialties, Inc. ("Avionics"), a Virginia corporation located in Earlysville, Virginia, from Teledyne Industries, Inc. ("Teledyne"). Avionics was previously a division of Teledyne. In fiscal year 2008, we commenced the consolidation of the Avionics operations with our Clearwater, Florida location. Avionics remains a wholly-owned subsidiary of the Company.

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Until October 31, 2006, we maintained an operating division in Wichita, Kansas. This division was the source inspection location for our Wichita customers and was the primary location for our repair business. During the fourth quarter of fiscal year 2007, we consolidated activity at the Wichita location with our Clearwater, Florida location.

On August 21, 2007, we purchased 100% of the outstanding stock of OP Technologies, Inc. ("OP Tech"), an Oregon based developer and manufacturer of cockpit glass display solutions. The acquisition of OP Tech is consistent with our strategy of revenue growth into related industry markets. These operations have been integrated into our Clearwater, Florida location. OP Tech remains a wholly-owned subsidiary of Aerosonic. The accompanying consolidated financial statements include the accounts of Aerosonic and our wholly-owned subsidiaries, Avionics and OP Tech.

In fiscal year 2008, we undertook the consolidation of our Avionics manufacturing operation based in Earlysville, Virginia into our Clearwater, Florida facility, where we continue to manufacture Avionics' products. This consolidation is a continuation of our actions to be more responsive to customers' demands while increasing efficiencies. We retained certain engineering and support functions in the Earlysville area at a new facility more appropriately sized for our planned streamlined structure. We are in the process of selling the Earlysville facility.

We are principally engaged in one business segment, which is the manufacture and sale of aircraft instruments and sensors. We design and manufacture both mechanical and digital altimeters, airspeed indicators, rate of climb indicators, microprocessor controlled air data test sets, and a variety of other flight instrumentation. Additionally, we design and manufacture angle of attack stall warning systems; integrated multifunction probes, which are integrated air data sensors; and other aircraft sensors and monitoring systems.

Industry

Military original equipment manufacturers ("OEM"), such as BAE Systems, Bell Helicopter, Korea Aerospace Industries, Lockheed Martin Corporation, Sikorsky Aircraft Corporation and The Boeing Company ("Boeing") increasingly rely on subcontractors to carry a greater share of aircraft design scope, including system requirements, hardware and software design, and physical and electrical interfaces. Supporting this increased need has enabled us to develop a greater technical capability for serving our customer base. Our increased technical capability has also positioned us to push further into the commercial aircraft market with new technologies. Aerosonic has established a presence in the Experimental and General Aviation market with our glass panel Electronic Flight Information Systems. We continue to work with customers to identify new product and product application opportunities.

We are an aerospace industry leader in the design and manufacturing of aircraft instrumentation, air data sensing and air data test equipment. Our instrumentation products are used for both primary flight data and standby redundant instrumentation in cockpits. Our electronic displays are used for primary flight data. As cockpit panel space becomes more valuable in the new age of glass displays, we have maintained a strong position with OEMs as a premier supplier of quality aircraft instrumentation in the military, general aviation and commercial aircraft marketplaces. Our air data sensing product line offers a broad range of air data and aircraft attitude sensing devices ranging from Angle of Attack (AoA) sensors, Stall Warning Transmitters (SWT) and Integrated Multi-Function Probes (IMFP®) to leading-edge Modular Static Flush Port (MSFP) technology. This range of products allows us to offer a fully integrated avionics package from air data to display and backup instrumentation thus reducing the number of suppliers required on the aircraft. Examples of our unique capabilities in air data products include our development of the MSFP implementation on the Dassault Aviation nEUROn Unmanned Combat Air Vehicle (UCAV) (with Alenia Aeronautica, a Finmeccanica Company) and Level A certification for the Stall Warning Transmitter (SWT) for Hawker Beachcraft Corporation's Premier II aircraft.

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Building on our expertise with mechanical instrumentation, we successfully developed and marketed digital instrumentation and displays for both primary flight data systems and standby redundant systems to complement our mechanical line of business. Continued development and enhancement of current technology has yielded an advanced anti-icing design for legacy air data systems as well as a number of technology enhancing implementations for both military and commercial aircraft including entry into the Transport aircraft category and a variety of advanced technology fighter and UAV opportunities.

Our current market focus continues to be design, development and supply of electronic and mechanical primary and standby flight control systems components and instruments. These include altimeters, airspeed indicators, angle of attack indicators, stall warning systems, air data measurement/computation systems and flight display systems. All of these products are critical to aircraft operation, performance and safety.

In conjunction with our development and production activities, Aerosonic has developed expertise in the build, test and validation of critical test equipment including ESS chambers and wind tunnels. Aerosonic is expanding that knowledge to offer customers the ability to order turnkey solutions to their test needs.

Strategy

Our market objectives are to deliver increasing value to our customers in three primary ways. First, because Aerosonic has a large installed base with many existing aircraft, as well as many long-standing relationships with global OEM's, we are working to ensure that our service, repair, and overhaul operations provide effective product support. This is a significant driver of customer satisfaction and financial contribution for our business. Second, we continuously strive to improve our ability to deliver new production on-time to customers' exacting manufacturing schedules and technical specifications. Aircraft manufacturers need our increasingly lean and cost-effective supply chain and we are working to ensure that we support their initiatives. Third, and most important from a growth perspective, we strive to design and deploy new products that enable our customers to deliver upgraded and/or new aircraft models. An important example of this is our work to develop digital instrumentation to replace aging mechanical designs. We have specialized air sensor, information processing, data presentation, design methodology, and manufacturing process knowledge that enables us to develop product solutions that enhance pilot performance and aircraft safety. Continually reinvesting and building on that capability in support of our customers is one of our core commitments.

Our business strategy is underpinned by our Company values, whereby we strive every day to be the best in the world at what we do. Our stated values include open communication, honesty, mutual respect, trust, a bias for action, teamwork, leadership and other values that we believe attract good people and help retain the best. We expect that, over time, a team of people dedicated to serving our stakeholders based on these shared values will lead to the success and growth of our Company.

Products and Distribution

Our products are sold to manufacturers of commercial and private aircraft, both domestic and foreign, and the United States and numerous foreign military services. For the years ended January 31, 2011 and 2010, approximately 66% and 72%, respectively, of our sales were to the private sector. During these same two years, 34% and 28%, respectively, of our sales were either directly or indirectly to United States military services.

We sell our products to customers outside of the U.S. Our aggregate percentages of international sales to overall sales were 25% and 41% for our fiscal years 2011 and 2010, respectively.

Most of our instrument sales are made directly through our sales personnel to OEMs or to the United States military, with our remaining sales being made through distributors and commissioned sales representatives who resell to aircraft operators.

We produce a full line of mechanical and electro-mechanical cockpit instruments. These instruments require no backup input, as they transfer valuable flight data to the pilot using only air pressure from aircraft probes as a power source.

We produce a leading-edge line of angle of attack ("AoA") stall warning products, including a "self-test" AoA sensor. We also produce Integrated Multi-Function Probes ("IMFP®"). This product combines existing technologies, including the angle of attack/air data sensing probe and pressure sensing electronics. We are one of a few developers of flush port air data technologies and are finalizing designs for European UCAV implementations with prospects for further global expansion. Our air data devices also include Stall Warning Transmitter and indicating devices. This integrated approach to providing aircraft air data reduces a customer's system complexity with respect to aircraft troubleshooting and logistics support, increases reliability, reduces supply complexity and decreases system costs.

We also produce digital cockpit instruments. These Technical Service Order ("TSO") certified indicators combine accuracy, robustness and long-term reliability of digital electronic equipment, with a "pilot familiar" analog pointer display.

The acquisition of Op Tech added Integrated Flight Display systems and electronic multi-function backup displays to our product offering. These systems provide us with the opportunity to play an increased role in the cockpit of new and updated aircraft. These display systems transfer critical flight data through highly accurate sensors to a flat panel display that reduces pilot workload and enhances situational awareness. We believe that our development methodology and modular architecture make our product unique in the industry.

Customers

We primarily market our products to OEMs, particularly manufacturers of corporate and private jets, and to contractors of military jets. Customers include, among others, the U.S. Government and a majority of the OEMs throughout the world. We also market our products to general aviation aircraft owners through our network of authorized distributors.

During fiscal year 2011, our largest customer, in terms of revenue, was Korea Aerospace Industries, which represented 14% of total revenues. The loss of this customer would have a material adverse effect on our results of operations.

Contracts

Our contracts are normally for production or development and are generally firm fixed-price contracts. Our production contracts are typically fixed-price for a one year period with options to be exercised over a one to five year period with pricing targets established. The aerospace industry trend for such contracts continues to move away from five year contracts and toward contracts of shorter duration. We also secure purchase orders from customers for product sales in the normal course of our business that are binding contracts upon acceptance of the terms and conditions of the orders by us.

Fixed-price contracts provide for a firm fixed-price on a variety of products and quantities of those products. Long-term contracts allow us to negotiate better overall prices that fit into customers' production programs. These long-term commitments also allow us to capitalize on quantity based price reduction for raw materials.

Under the firm fixed-price contracts, we agree to perform for an agreed-upon price. Accordingly, we derive benefits from cost savings; however, we also bear the risk of cost overruns.

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

The inherent nature of the U.S. Government's contracting and budgeting process may effect our operating results and production backlog. Examples include the limited availability of year-end monies to accomplish important last minute contracts for supplies and services, enactment of continuing resolutions that limit spending to the previous year's level until a budget is signed into law, late approval of new budgets, and the use and timing of supplemental appropriations. These events significantly affect the amount of orders that we have in backlog and the number and size of major contracts for our products.

Sales and Marketing

We focus our sales efforts on government and military entities, OEMs and distributors. We have increased our sales efforts with respect to retrofit, modifications and repair programs.

Due to the integration of components manufactured by us with flight management systems, our sales force is generally involved at a very early stage with the aircraft manufacturers' engineers to integrate the components into the aircraft design. Our component instruments and systems are often integrated into the aircraft design helping to maintain and ensure the safe and effective operation of the aircraft.

At January 31, 2011, our backlog of firm orders was approximately $16.7 million, a decrease of approximately $3.4 million when compared to our backlog as of January 31, 2010. The amount of backlog that is deliverable within twelve months was approximately $14.1 million at January 31, 2011, an increase of approximately $3.1 million when compared to January 31, 2010. The foregoing backlog amounts represent firm production and development orders only and do not include current contract options. Such option orders, however, may be subject to rescheduling and/or cancellation. Backlog amounts include business generated through repair and spare parts orders.

Government Regulation

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

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

Quality Assurance

Product quality is critical in the aerospace industry. We strive to maintain the highest standards within our operations.

We are ISO 9001/AS9100 certified. ISO 9001/AS9100 standards are an international consensus on effective management practices for ensuring that we can consistently deliver our products and related services in a manner that meets or exceeds customer quality requirements. ISO 9001/AS9100 standards outline the minimum requirements a quality system must meet to achieve this certification.

As an ISO 9001/AS9100 certified manufacturer, we can represent to our customers that we maintain high quality industry standards in the education of employees and the design and manufacture of our products. In addition, our products undergo extensive quality control testing prior to being delivered to customers. As part of our quality assurance procedures, we maintain detailed records of test results and quality control processes.

Patents and Licenses

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

Research and Development

We expended approximately $3,092,000 and $1,423,000 in both internally and externally funded research and development costs for potential new products and enhancements during the years ended January 31, 2011 and 2010, respectively. In fiscal year 2011, we continued our efforts on several externally funded research and development projects initiated in fiscal year 2010. During fiscal year 2010, we expended a significant portion of our engineering capacity to recover lost production and test capabilities from the August 2008 fire described below.

We continued various development efforts during fiscal year 2011 for both military and commercial applications. Creating innovative digital, integrated flight management and backup devices has been a primary focus of our R&D efforts, along with additional advancements for our industry unique air data instruments. These efforts will provide for an integrated product line from sensors and information processing through primary and backup displays for the flight crew. Further, we plan to continue our design efforts to satisfy our existing contractual obligations as well as our internal development of products for future customer applications. This includes re-engineering of existing products and processes to improve manufacturability, increase reliability, enhance throughput, and reduce production costs.

Competition

Markets for our products are highly competitive and characterized by several aerospace industry niches in which a number of manufacturers specialize. In our market niche, we believe that we manufacture a broader variety of aircraft instruments than our competitors who, in most instances, compete with us on no more than a few types of aircraft instruments. In addition to mechanical instruments that formed the initial foundation of our business, we offer electronic instruments and components that are integrated into the flight management system of aircraft. This product offering allows us to compete on many levels within the aerospace industry.

Our AoA, stall warning and IMFP® products provide flight critical functions and are typically designed into the aircraft. Our rotating probe design provides a competitive advantage in terms of responsiveness and accuracy. There is limited competition in this product family.

We believe that our principal competitive factors are development cycle time, responsiveness to customer preferences, product quality, delivery reliability, price, technology, product reliability and product variety. We believe that our significant and long-standing customer relationships reflect our ability to compete favorably with respect to these factors.

Manufacturing, Assembly and Material Acquisition

Our manufacturing processes, except for certain electronic components, include the manufacture of all principal components and subassemblies for the instruments, the assembly of those components, and the testing of products at various stages in the manufacture and assembly process.

We manufacture, or have the capability to manufacture, principally all components, except for certain electronic components and subassemblies for our instruments. Raw materials, such as glass lenses, raw metals and castings, generally are available from a number of sources and in sufficient quantities to meet current requirements, subject to normal lead times. We believe that retaining the ability to completely manufacture the instruments allows us the flexibility to respond to customers quickly and control the quality of our products.

When appropriate, less critical component parts are purchased under short and long-term supply agreements. These purchased parts are normally standard parts that can be easily obtained from a variety of suppliers. This allows us to focus our attention on more critical component parts to maintain a level of quality control required to meet the exacting tolerances demanded within the aerospace industry and by our customers. On August 8, 2008, we suffered the destruction of one of our buildings comprising our Clearwater, Florida facility as a result of a fire. The building was primarily used for general storage and product testing, probe and sensor manufacturing, as well as for shipping and receiving. While our main operating facility was not damaged by the fire, our production was affected through loss of staged incoming raw materials inventory and outgoing finished goods. During the third quarter of fiscal year 2009 and the first quarter and second quarter of fiscal year 2010, our insurer extended advances to us totaling $2,600,000, $500,000 and $50,000, respectively. On February 4, 2010, we settled our claims against our insurance carrier and insurance broker in consideration of payment to us of $235,000. We applied portions of the insurance proceeds to replacing raw materials inventory and production assets lost in the fire and also retooled and reengineered production equipment in our unaffected main operating facility to accommodate lost production activities.

Employees

As of January 31, 2011, we employed 218 people, of which, 217 are full time. Our future success depends on the ability to attract, train and retain quality personnel. Our employees are not represented by labor unions and we consider our relations with our employees to be good.

Available Information

Our most recent Annual Report on Form 10-K, Quarterly Reports on Form 10-Q, Current Reports on Form 8-K and amendments to those reports may be viewed or downloaded electronically, free of charge, from our website: http://www.aerosonic.com as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC. In addition, you may read and copy any materials we file with the SEC at the SEC’s Public Reference Room at 100 F Street, NE, Washington, DC 20549. To obtain information on the operation of the Public Reference Room, you may call the SEC at 1-800-SEC-0330. Our recent press releases are also available to be viewed or downloaded electronically at http://www.aerosonic.com. We will also provide electronic copies of our SEC filings free of charge upon request. Any information posted on or linked from our website is not incorporated by reference into this Annual Report on Form 10-K. The SEC also maintains a website at http://www.sec.gov, which contains reports, proxy and information statements and other information regarding issuers that file electronically with the SEC.

ITEM 1A. RISK FACTORS

The following factors are important and should be considered carefully in connection with any evaluation of our business, financial condition, results of operations, prospects, or an investment in our common stock. In particular, our results of operations, revenue, liquidity and capital resources may be materially and unfavorably affected by a number of risk factors, trends and uncertainties. Set forth below are the risk factors, trends and uncertainties which we believe could have a material and unfavorable impact on our results of operations, revenue, liquidity, capital resources and any investment in our stock. Additional risk factors, trends and uncertainties may be discussed elsewhere within this document.

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Our business is dependent on the aerospace industry and defense spending

Our principal business is in the aerospace industry. Our commercial sector business is cyclically affected by the state of the economy. In the military sector, we are affected by overall spending levels in the defense budgets of the U.S. and foreign governments, the priorities reflected in those budgets, and developments affecting the timing of those expenditures. Adverse developments in the economy generally, aerospace industry in particular, or government defense sector could have a material adverse effect on our results of operation.

A portion of our business is dependent on U.S. Government contracts

Our dependence on revenue from U.S. Government contracts subjects us to a number of risks, including the risk that we may not be successful in bidding for future contracts and the risk that funding for these contracts may be delayed or diverted to other uses.

We perform work under a number of contracts with the U.S. Department of Defense and other agencies and departments of the U.S. Government. Sales under these contracts as a whole, including sales under contracts with the U.S. Department of Defense, as prime contractor or subcontractor, represented approximately 34% and 28% of our total revenue for fiscal years 2011 and 2010, respectively.

U.S. Government contracts are conditioned upon the continuing availability of Congressional appropriations. Congress typically appropriates funds for a given program on a fiscal-year basis even though contract performance may take more than one year. As a result, at the beginning of a major program, a contract is typically only partially funded, and additional monies are normally committed to the contract by the procuring agency only as appropriations are made by Congress for future fiscal years.

While the overall U.S. military budget declined in real dollars from the mid-1980s through the early 1990s, U.S. defense spending has increased in recent years. Increased defense spending does not necessarily correlate to increased business for us because not all the programs in which we participate or have current capabilities may be earmarked for increased funding.

Most of our U.S. Government contracts are subject to termination by the U.S. Government either at its convenience or upon our default. Termination-for-convenience provisions permit only the recovery of costs incurred or committed, settlement expenses, and profit on work completed prior to termination. Termination-for-default imposes liability on us for excess costs incurred by the U.S. Government in procuring undelivered items from another source.

A substantial majority of our U.S. Government contracts are fixed-price type contracts. A majority of these contracts are for mature products and costs are well established. However, some contracts include costs associated with product development. These types of contracts bear the inherent risk that actual performance cost may exceed the fixed contract price.

We, like other U.S. Government contractors, are subject to various audits, reviews and investigations (including private party “whistleblower” lawsuits) relating to our compliance with federal and state laws. In addition, we have a compliance program designed to uncover issues that may lead to voluntary disclosures to the U.S. Government. Generally, claims arising out of these inquiries and voluntary disclosures can be resolved without resorting to litigation. However, should the Company be charged with violation of law, or should the U.S. Government determine that the Company is not a “presently responsible contractor,” the Company could be temporarily suspended or, in the event of a violation, could be debarred for up to three years from receiving new U.S. Government contracts or government-approved subcontracts. In addition, we could expend substantial amounts in defending against such charges and in damages, fines and penalties if such charges are proven or result in negotiated settlements. If we were to be debarred from U.S. Government contracts, it would have a material adverse effect on our results of operations, revenue, liquidity, and capital resources.

As part of the aerospace industry our business is heavily regulated and the cost of non-compliance with applicable regulations could be significant

The aerospace industry is heavily regulated and failure to comply with applicable laws or regulations could reduce our sales, or require us to incur additional costs to achieve compliance, which could have a material adverse effect on our results of operations.

The FAA prescribes standards and licensing requirements for aircraft components, including virtually all of our products. Comparable agencies, such as the U.K. Civil Aviation Authority, the Japanese Civil Aviation Board and South Korea's Aviation Safety Authority regulate these matters in other countries.

If we fail to obtain a required license for one of our products or services or lose a license previously granted, the sale of the subject product or service would be prohibited by law until such license is obtained or renewed. In addition, designing new products to meet existing regulatory requirements and retrofitting installed products to comply with new regulatory requirements can be both expensive and time consuming.

From time to time the FAA proposes new regulations. These new regulations generally cause an increase in costs to bring our existing and developmental products into compliance.

We have to compete against larger well-established companies that are well capitalized

We compete with numerous well-established companies. Some of these companies have significantly greater financial, technological and marketing resources than us. Our ability to be an effective competitor depends in large part on our success in causing our products to be selected for installation in new aircraft, including next generation aircraft, and in avoiding product obsolescence. In addition some of our larger customers could develop the capability to manufacture products or provide services similar to the products we manufacture or the services we provide. This could result in these customers competing directly with us for sales of these products or services, all of which could significantly reduce our revenues. There can be no assurance that we will be able to compete successfully against our current or future competitors or that the competitive pressures we face will not result in reduced revenues and market share.

We are engaged in a highly competitive marketplace, which demands that producers continue to develop new products. Our business will be adversely affected if we are not able to continue to develop new and competitive products

Our customers continually seek improvements in the products that we manufacture and market. As a result, in order to meet our customers' needs, we must continue to develop new products and innovations and enhancements to existing products. Many of our competitors have significantly more capital than we have and as a result have the ability to devote more resources to research and development and to marketing of their products. In order to remain competitive, we must continue to devote a material portion of our financial resources to research and development and there is no assurance that we will be successful in our product improvement efforts in our competitive marketplace.

We face continuous pricing pressure from our customers and our competitors. This will affect our margins and therefore our profitability and cash flow unless we can manage efficiently our manufacturing costs and market our products based on superior quality

Our customers often award contracts based on product pricing, and we believe we have not received some awards due to pricing discounts given by our competitors. Many of our competitors have significantly greater financial resources than we have, and as a result may be able to withstand the adverse effect of discounted pricing and reduced margins in order to build market share. While one of our strategies is also to discount to retain and increase market share, and to seek to manage our manufacturing efficiently to sustain acceptable margins, we may not be able to maintain appropriate prices or to manage product manufacturing costs sufficiently to sustain acceptable margins. Similarly, we seek to compete based on product quality rather than price, but we may not be successful in these efforts with enough contract awards to offset the need to reduce prices for other products. This could adversely affect our profitability, our liquidity and our market share.

Increases in the prices paid for raw materials or labor costs may adversely affect profit margins

If we experience significant increases in the prices paid for raw materials or labor costs, we may not be able to pass through to our customers such increases in those costs. Even if we are able to pass through all or a portion of such cost increases to our customers, profit margins on such products may be reduced. Fixed-price contracts are especially susceptible to such profit margin reductions.

Our products are used in activities that are inherently risky. Accordingly, we may face product liability and exposure to other claims for which we may not be able to obtain adequate insurance

The products that we manufacture are typically used in applications and activities that involve high levels of risk of personal injury. Failure to use these products for their intended purposes, failure to use these products properly, malfunction of these products and, in some circumstances, even correct use of these products could result in serious bodily injury or death. We cannot guarantee that our insurance coverage would be sufficient to cover the payment of any potential claim arising out of the use of our products. In addition, we cannot guarantee that our current insurance or any other insurance coverage will continue to be available or, if available, that it will be obtainable at a reasonable cost. Any substantial uninsured loss thus would have to be paid out of our assets as applicable and may have a material adverse effect on our business, financial condition, results of operations and liquidity. If we are unable to obtain product liability coverage, then we may be prohibited from bidding for orders from certain government customers because many governmental agencies currently require such insurance coverage. Any inability to bid for government contracts as a result of insufficient insurance coverage would have a material adverse effect on our business, financial condition, results of operations and liquidity.

Our industry has rapid technological changes and products that are subject to obsolescence as a result thereof

Our operating results depend in part on our ability to introduce new and enhanced products on a timely basis. Successful product development and introduction depend on numerous factors, including our ability to anticipate customer and market requirements, changes in technology and aerospace industry standards, our ability to differentiate our offerings from offerings of our competitors, and market acceptance. The markets for a number of our products and services are generally characterized by rapid technological development, evolving aerospace industry standards, changes in customer requirements and new product introductions and enhancements. A faster than anticipated change in one or more of the technologies related to our products or services or in market demand for products or services based on a particular technology could result in faster than anticipated obsolescence of certain of our products or services and could have a material adverse effect on our business, results of operations and financial condition. Currently accepted aerospace industry standards are also subject to change, which may contribute to the obsolescence of our products or services and could have a material adverse effect on our business, results of operations and financial condition.

We may not realize the anticipated benefits of the acquisition of OP Tech

As part of our strategy of revenue growth into related industry markets, we acquired OP Tech in fiscal year 2008. Whether we realize the anticipated benefits from this transaction will depend in part upon the integration of the acquired business, the performance of the acquired products, capabilities of the technologies acquired as well as the personnel hired in connection therewith. Accordingly, our results of operations could be adversely affected from transaction-related charges, amortization of intangible assets and charges for impairment of long-term assets. While we believe that we have established appropriate and adequate procedures and processes to mitigate these risks, there can be no assurance that this transaction will be successful. There is a risk that we will not receive federal certification for OP Tech’s products or that the products may become obsolete in the market place, in which case the intangible assets recognized in connection with the OP Tech acquisition could become impaired.

We face unforeseen liabilities arising from possible acquisitions and dispositions of businesses

We have engaged in acquisitions of businesses in the past, and expect to continue to do so in the future. There could be unforeseen liabilities that arise in connection with the businesses that we may acquire in the future. In addition, there may be liabilities that we fail, or we are unable, to discover in the course of performing due diligence investigations on each business that we have acquired or may acquire.

We are dependent on the ability to maintain reasonable levels of working capital along with capital needs for expansion

Our need to expend resources on research and development to provide our customer base with new and enhanced products as well as to continuously upgrade our process technology and manufacturing capabilities requires us to expend up to 10% of revenues annually. If we elect to expand our operations in future periods, whether as a result of organic growth or through strategic acquisitions, our capital needs would increase. Our ability to raise capital to meet our existing and future needs may depend on a variety of factors, some of which will not be within our control, including investor perceptions of us, our businesses and the industries in which we operate, and general economic conditions. We may be unable to successfully raise additional capital, if needed. If we are unable to generate sufficient cash from operations or raise additional capital in the future, we may have to limit our growth, enter into less favorable financing arrangements, or scale back on planned research and development or upgrades, any of which could have a materially adverse effect on our profitability.

We rely significantly on our ability to fill orders on a timely basis and collect accounts receivable for liquidity needs

Our liquidity depends on cash generated from operations. We have been challenged during fiscal years 2011 and 2010 to efficiently process orders, ship finished goods, and collect receivables in order to maintain liquidity. Should we continue to experience operational inefficiencies in any of these areas it will have an adverse effect on our financial condition, operating results and cash flows and our ability to access credit markets and to obtain reasonable trade terms from our vendors.

We continue to experience liquidity challenges

In addition to debt service on our credit facilities, we have significant cash obligations that we must meet in the near future. Specifically, although we are not delinquent on payments of debt service under our credit facilities, we are delinquent on payments to vendors that provide critical services and inventory to us. Should we not be able to implement a business plan to meet our cash obligations, improve our cash flows from operations and continue to obtain reasonable vendor terms, our financial condition and operating results will continue to suffer. See "Management's Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources."

The terms of our credit facilities include various covenants, and continued failure to meet these covenants could affect our ability to borrow.

Our credit facility with M&I Marshall & Ilsley Bank (“M&I Bank”) requires us to maintain compliance with financial covenants that are based on total stockholders’ equity, ratio of funded debt to EBITDA covenant, and a fixed charge coverage ratio. We did not comply with our funded debt to EBITDA covenant for the period measured as of January 31, 2011. The lender waived this non-compliance and adjusted this covenant for our 2012 fiscal year, but there is no assurance that the lender will waive compliance or amend this credit facility in future periods, if such a waiver or amendment is needed. A continuing default under the credit facility would adversely affect us. See "Management's Discussion and Analysis of Financial Condition and Results of Operations – Liquidity and Capital Resources."

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Our credit facility with M&I Bank is also subject to renewal provisions, including a maturity date for a revolving line of credit of June 28, 2011. These renewals might become more challenging due to our financial position and credit constraints in the U.S. banking markets as a whole. Failure to obtain permanent financing would impair our liquidity and viability as a going concern into the future.

We face risks associated with handling and use of hazardous substances and related environmental matters

Our operations require the handling and use of hazardous substances, and we are subject to federal, state and local laws, regulations, rules and ordinances relating to pollution, the protection of the environment and the use or cleanup of hazardous substances and wastes. From time to time, our operations could result in violations under such environmental laws, including spills or other releases of hazardous substances into the environment. We may incur substantial costs or experience interruptions in our operations for actual or alleged violations or compliance requirements arising under environmental laws. Additionally, we may be liable for the costs of investigating and cleaning up environmental contamination on or from our properties. In the event of a major incident, we could incur material costs or experience interruption in our operations as a result of addressing the incident and implementing measures to prevent such incidents in the future, as well as potential litigation that could arise from such an incident. In addition, we could incur significant expenditures in order to comply with existing or future environmental laws.

We face risks associated with international sales

During fiscal years 2011 and 2010, international sales accounted for approximately 25% and 41%, respectively, of our total revenues. We anticipate that future international sales will continue to account for a significant percentage of our revenues. Risks associated with these sales include:

• Political and economic instability;

• Export controls and other trade restrictions;

• Changes in legal and regulatory requirements;

• U.S. and foreign government policy changes affecting the markets for our products;

• Changes in tax laws and tariffs;

• Convertibility and transferability of international currencies; and

• International currency exchange rate fluctuations.

Any of these factors could have a material adverse effect on our business, results of operations and financial condition. Currency exchange rate fluctuations may negatively affect the cost of our products to international customers and therefore reduce our competitive position.

If we are unable to successfully attract and retain executive leadership and other key personnel, our ability to successfully develop and market our products and operate our business may be harmed

Our future success depends to a significant extent upon the continued service of our executive officers and other key management and technical personnel and on our ability to continue to attract, retain and motivate qualified personnel. Recruiting and retaining skilled technical personnel is highly competitive. The loss of the services of one or more of our key employees or our failure to attract, retain and motivate qualified personnel could have a material adverse effect on our business, financial condition and results of operations.

Terrorism and world conflict could adversely affect our ability to market our product

United States and global responses to the Middle East conflict, terrorism, perceived nuclear, biological and chemical threats and other global crises increase uncertainties with respect to U.S. and other business and financial markets. Several factors associated, directly or indirectly, with such crises and perceptions, including responses thereto, may adversely affect us.

While some of our products that are sold to the U.S. Government may experience greater demand as a result of increased defense spending, various responses could realign U.S. Government programs and affect the composition, funding or timing of our government programs. U.S. Government spending could shift to defense programs in which we do not participate.

We have contracts with the government of South Korea. Continued actions and perceived provocations by the government of North Korea have resulted in increased concern regarding the stability of the Korean armistice. Additionally, reports indicate that North Korea may be moving to produce and test nuclear weapons or otherwise provoke the U.S. and international community. Resulting instability on the Korean peninsula, and any U.S., local or global responses to perceived provocations by the government of North Korea, could impact our contracts with South Korea. While an escalation of hostilities on the Korean peninsula might lead to increased military spending by South Korea, there is no certainty that our contracts with South Korea would benefit. Additionally, it is possible that any instability in that region could have a negative impact on our contracts.

Our stock price is volatile because it is affected by numerous factors outside of our control

The market price and trading volume of our common stock is subject to significant volatility and this trend may continue. The general economic, political, and stock market conditions that may affect the market prices of our common stock are outside our control. The value of our common stock may decline regardless of our operating performance or prospects. Factors affecting market price include, but are not limited to: (i) variations in our operating results and whether we have achieved our key business targets; (ii) the limited number of shares of our common stock available for purchase or sale in the public markets; (iii) sales or purchases of large blocks of stock; (iv) changes in, or failure to meet, earnings estimates; (v) changes in securities analysts' buy/sell recommendations; (vi) differences between reported results and those expected by investors and securities analysts; and (vii) announcements of new contracts by us or by our competitors. In the past, securities class action litigation has been instituted against companies following periods of volatility in the market price of their securities.

Other factors and general market conditions that could affect our stock price are:

• Our quarterly operating results and variations therein;

• Changes in earnings estimates by securities analysts;

• Changes in our business;

• Changes in the market's perception of our business;

• Changes in the businesses, earnings estimates or market perceptions of our competitors or customers;

• Changes in the outlook for the aerospace industry;

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• Changes in general market or economic conditions unrelated to our performance;

• Changes in the legislative or regulatory environment;

• Changes in U.S. defense spending or appropriations;

• Increased military or homeland defense activities;

• An outbreak or escalation of national or international hostilities;

• Terrorist attacks;

• Sales of significant blocks of our common stock; and

• Our ability to successfully maintain our line of credit.

Additionally, the stock market has experienced extreme price and volume fluctuations in recent years that have significantly affected the quoted prices of the securities of many companies, including companies in the aerospace industry. The changes often appear to occur without regard to specific operating performance. The price of our common stock could fluctuate based upon factors that have little or nothing to do with our business or performance and these fluctuations could materially reduce our stock price.

We do not plan to pay cash dividends on our common stock in the foreseeable future

We intend to retain our earnings to finance the development and expansion of our business. Additionally, covenants in our long-term debt agreements may restrict our ability to pay dividends. This lack of dividend could adversely affect the market for our common stock and the return on our common stock for our stockholders.

Our common stock may become subject to penny stock rules, which may make it more difficult for our stockholders to sell their common stock

Our common stock may become a “penny stock” pursuant to Rule 3a51-1 of the Exchange Act. Broker-dealer practices in connection with transactions in penny stocks are regulated by certain penny stock rules adopted by the SEC. Penny stocks generally are defined as equity securities with a price of less than $5.00 per share. The penny stock rules require a broker-dealer, prior to purchase or sale of a penny stock not otherwise exempt from the rules, to deliver to the customer a standardized risk disclosure document that provides information about penny stocks and the risks associated with the penny stock market. The broker-dealer also must provide the customer with current bid and offer quotations for the penny stock, the compensation of the broker-dealer and its salesperson in the transaction, and monthly account statements showing the market value of each penny stock held in the customer account. In addition, the penny stock rules generally require that, prior to a transaction in a penny stock, the broker-dealer make a special written determination that the penny stock is a suitable investment for the purchaser and receive the purchaser’s written agreement to the transaction. These disclosure requirements may have the effect of reducing the level of trading activity in the secondary market of a stock that becomes subject to the penny stock rules.

We have risks related to the inherent limitations of internal control systems

As more fully described in Item 9A, Controls and Procedures, for the fiscal year ended January 31, 2009, our management determined that a material weakness existed surrounding adequate accounting for our inventory. We implemented initiatives to remediate this material weakness in our internal controls as of January 31, 2009. Correction of any further “significant deficiencies" or "material weaknesses" (as defined under the Public Company Accounting Oversight Board guidelines) could require additional remedial measures, which could be costly and time-consuming. If a significant deficiency or material weakness existed at any year-end (including a material weakness identified prior to year-end for which there is an insufficient period of time to evaluate and confirm the effectiveness of the corrections or related procedures), our management will be unable to report favorably as to the effectiveness of our internal control over financial reporting or information systems, which could adversely affect us.

We cannot guarantee that our internal controls and disclosure controls will prevent all error, loss, and fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. In addition, the design of a control system must reflect resource constraints and the benefit of controls relative to their costs.

Our forward-looking statements and projections may prove to be inaccurate

Our actual financial results likely will be different from those projected due to the inherent nature of projections and may be better or worse than projected. Given these uncertainties, you should not rely on any forward-looking statements that we provide. The forward-looking statements contained in this Form 10-K speak only as of the date of this Form 10-K. We expressly disclaim a duty to provide updates to forward-looking statements after the date of this Form 10-K to reflect the occurrence of subsequent events, changed circumstances, changes in our expectations, or the estimates and assumptions associated with them. The forward-looking statements in this Form 10-K are intended to be subject to the safe harbor protection provided by the federal securities laws.

ITEM 1B. UNRESOLVED STAFF COMMENTS

None.

ITEM 2. PROPERTIES.

The following table sets forth the locations and general characteristics of our principal properties, two of which are owned by us while the third property is leased:

Location	Approximate Number of Square Feet of Plant and Office Area
Plant and office facilities, 1212 North Hercules Avenue, Clearwater, Florida (Owned)	61,000
Plant facility held for sale, 3369 Earlysville Road, Earlysville, Virginia (Owned)	53,000
Plant and office facilities, 1180 Seminole Trail, Charlottesville, VA (Leased)	9,000

On August 8, 2008, we suffered the destruction of one of the buildings comprising our Clearwater, Florida facility as a result of a fire. The Clearwater, Florida property, as reconfigured, is fully occupied by us and suitable for our present level of production.

In preparing to sell our Earlysville, Virginia facility, we engaged an environmental consulting firm to survey for possible soil or groundwater contamination. This survey revealed impacts to both shallow soils and groundwater that might have resulted from an accidental loss of solvents by a former owner. Based on this initial and a subsequent survey, we estimate the remaining contamination treatment costs at $808,000. We capitalized these contamination treatment costs as an increase to property held for sale, since these costs will be incurred in preparing for the sale of the Earlysville, Virginia facility and will not result in a carrying value in excess of the estimated fair value less cost to sell. Our costs incurred for treatment during our fiscal years 2011 and 2010 totaled $124,000 and $153,000, respectively. On September 20, 2007, we signed a five-year operating lease at a much smaller 9,000 square foot facility in Charlottesville, Virginia to serve as our new location for support and repair/overhaul activities for existing Avionics Specialties products.

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ITEM 3. LEGAL PROCEEDINGS

From time to time, we may be involved in certain claims and legal actions arising in the ordinary course of business. In the opinion of management, at this time, there are no material claims or legal actions at this time.

PART II

ITEM 5. MARKET FOR REGISTRANT'S COMMON STOCK AND RELATED STOCKHOLDER MATTERS AND ISSUER PURCHASES OF EQUITY SECURITIES

Market for Common Stock and Dividends

Our common stock is listed on the NYSE Amex under the symbol "AIM." The range of high and low sales prices as reported by the NYSE Amex for each of the quarters of the fiscal years ended January 31, 2011 and January 31, 2010 was as follows:

	COMMON STOCK MARKET PRICE	
2011	HIGH	LOW
Fourth quarter	$ 3.69	$ 2.52
Third quarter	$ 4.00	$ 2.50
Second quarter	$ 4.26	$ 2.51
First quarter	$ 4.40	$ 3.75
2010	HIGH	LOW
Fourth quarter	$ 6.13	$ 3.75
Third quarter	$ 6.51	$ 4.10
Second quarter	$ 7.44	$ 1.95
First quarter	$ 2.39	$ 0.45

As of May 2, 2011, our outstanding shares of common stock were owned by approximately 2,000 stockholders of record.

During those same periods, no cash dividends were paid. We do not anticipate or intend on paying a dividend in the foreseeable future. Rather, we intend to retain our earnings to finance the development and expansion of our business. Additionally, covenants in our long-term debt documents may restrict our ability to pay dividends. Any future payment of any dividends on our common stock and the amount thereof will depend on our earnings, financial requirements, compliance with the above described covenants, and other factors deemed relevant by our Board of Directors.

Securities Authorized for Issuance under Equity Compensation Plans

Information regarding our equity compensation plan at January 31, 2011 is summarized as follows:

Plan category	(a) Number of securities to be issued upon exercise of outstanding options, warrants and rights	(b) Weighted average exercise price of outstanding warrants and rights	(c) Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))
Equity compensation plans approved by security holders	320,200	$ 2.82	229,800
Equity compensation plans not approved by security holders	None	N/A	N/A
Total	320,200	$ 2.82	229,800

ITEM 6. SELECTED FINANCIAL DATA.

The following table represents selected financial data for the most recent five fiscal years ended January 31. The data set forth below does not purport to be complete. It should be read in conjunction with, and is qualified in its entirety by, the more detailed information, including the Consolidated Financial Statements and Notes, appearing elsewhere in this document. The selected financial data as of January 31, 2009, 2008 and 2007 and for the years ended January 31, 2009, 2008 and 2007 have been derived from audited financial information not separately presented herein.

	As of and for the Years Ended January 31,				
	2011	2010	2009	2008	2007
Revenues, net	$29,618,000	$31,136,000	$20,451,000	$25,410,000	$31,253,000
Cost of sales	(20,486,000)	(20,268,000)	(18,410,000)	(24,870,000)	(26,322,000)
Gross profit	9,132,000	10,868,000	2,041,000	540,000	4,931,000
Selling, general and administrative expenses	(7,415,000)	(6,725,000)	(7,550,000)	(5,861,000)	(3,989,000)
Gain on sale of property, plant and equipment	-	-	18,000	315,000	32,000
Operating income (loss)	1,717,000	4,143,000	(5,491,000)	(5,006,000)	974,000
Other (expense) income	(637,000)	(54,000)	197,000	(316,000)	(165,000)
Income (loss) before income taxes	1,080,000	4,089,000	(5,294,000)	(5,322,000)	809,000
Income tax (expense) benefit	(455,000)	172,000	(33,000)	1,941,000	(244,000)
Net income (loss)	$625,000	$4,261,000	$(5,327,000)	$(3,381,000)	$565,000
Basic earnings (loss) per share	$0.17	$1.15	$(1.48)	$(0.95)	$0.16
Fully diluted earnings (loss) per share	$0.15	$1.09	$(1.48)	$(0.95)	$0.16
Total assets	$23,678,000	$21,476,000	$17,761,000	$21,380,000	$17,735,000
Long-term debt (1)	$8,553,000	$7,933,000	$6,022,000	$7,328,000	$2,564,000

(1) Long-term debt is defined as all outstanding long-term debt and capital leases, including current maturities, and the revolving credit facility.

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

Management's Discussion and Analysis of Results of Operations and Financial Condition ("MD&A") is provided to help provide an understanding of our business, financial condition, changes in financial condition and results of operations. The following discussion and analysis should be read in conjunction with our Consolidated Financial Statements and Notes included elsewhere in this report. Our MD&A is organized as follows:

Overview. This section contains trend analysis, a summary of the challenges we encountered this fiscal year and steps we are taking to address these challenges. This section may contain forward-looking statements. These statements are based on our current expectations and actual results may materially differ from such expectations. Among the factors that could cause actual results to vary are those described in this "Overview" section and in "Item 1A. Risk Factors."

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

Liquidity and Capital Resources. This section provides an analysis of cash flows, a discussion of outstanding debt, working capital and capital expenditures, and commitments, both firm and contingent, that existed as of January 31, 2011, and trends, demands, events and uncertainties with respect to our ability to finance our continuing operations.

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

OVERVIEW

We are an aerospace industry leader in which we design and manufacture aircraft instrumentation and sensor systems. These products are used for both primary flight data as well as for standby purposes in cockpits where electronic displays are used for primary flight data. As cockpit panel space becomes more valuable in the new age of glass displays, we have maintained a strong position with Original Equipment Manufacturers (OEM) as a premier supplier of quality aircraft instrumentation in both the military and commercial aircraft marketplace. This allows us to offer a fully integrated avionics package, from air data collection products to display and backup instrumentation which reduces the number of suppliers required on an aircraft. Our unique capabilities in air data collection products continue to expand with the development of a flush port air data system for a leading international aircraft manufacturer for use on a new unmanned combat air vehicle and Level A certification of a stall warning transmitter for a major US manufacturer of business and military aircraft.

Building on our expertise with mechanical instrumentation, we have successfully developed and marketed digital instrumentation and displays for both primary flight data systems as well as standby redundant systems to complement our mechanical product line. In addition, we have made considerable progress in the development of electronic air data collection instrumentation for use in military and commercial aircraft applications.

Our current market focus has been, and will continue to be, the design, development and supply of electronic and mechanical primary and standby flight control systems components and instruments. These include altimeters, airspeed indicators, angle of attack indicators, stall warning systems, air data measurement systems and flight display systems. These products are critical to aircraft operation, performance and safety.

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In conjunction with our development and production activities, Aerosonic has developed expertise in the build, test and validation of critical test equipment, including environmental stress screening chambers and wind tunnels. Aerosonic is expanding that knowledge to offer customers the ability to order turnkey solutions for their test needs.

The trend in the aerospace industry continues toward digital cockpits and away from mechanical cockpit instrumentation that was our foundation. During fiscal year 2011, we continued to make progress in our ability to design and manufacture digital instrumentation that is integrated into cockpit flight management systems. We have maintained and strengthened our commitment to research and development to further enhance our product line as we anticipate continued movement toward digital cockpits in the aerospace industry. We plan to position ourselves such that we have the ability to offer both digital and mechanical instrumentation. While we believe that this strategy will, over time, strengthen our position in the aerospace industry, we cannot guarantee that this strategy will be successful or that we will have access to the capital resources needed to fully support this strategy.

A significant amount of our business relates to the sale of our products to United States (“U.S.”) and foreign military programs. As a consequence, our sales can fluctuate materially, either favorably or unfavorably, depending upon the level of government spending on those military programs which are the focus of our manufacturing efforts. While we have been successful in obtaining contracts to supply military needs in recent years, sudden reductions in government spending or delays in the government contract award process could have a material unfavorable effect on our current and future military sales and related cash flows. While we cannot predict the outcome of the U.S. government contract award or budget process, we expect that the majority of the military programs that we supply will be sustained at current or near current levels. Additionally, U.S. Government procurement offices often require long periods of time to issue requests for proposals and to negotiate contracts. Such lengthy contract cycle times may delay the award of certain anticipated contracts of significant value to the Company. Continued delays of such contract awards may have a significant adverse effect on the financial results of the Company.

Similarly, changes in the commercial sector of the aerospace industry can have a favorable or unfavorable impact on our future business. While we have historically invested heavily in product development for both funded and unfunded programs, OEM requirements may change such that additional product development efforts will be necessary to maintain or increase our revenue in the aerospace industry. With the recent economic conditions, several of our commercial customers continue to operate with reduced operations and manufacturing. While this may be offset by additional increases in aftermarket support, it is likely that our business will continue to be negatively affected until the economy recovers and our customers resume prior levels of production and growth. Recently, we are finding that with the negative effects of the ongoing recession, the general aviation and business jet markets may take longer to recover than previously believed. For example, certain key commercial customers are slowing their operations and are pushing contractual delivery dates into the future by six to eighteen months. Continued movements into the future of such customer deliveries may have a significant adverse effect on our financial results.

Recognizing the risks and challenges of the current environment in both our military and commercial markets, we continue to closely analyze our operations and our cost structure for opportunities to enhance our financial performance in the face of the difficult economic environment. As a result of these analyses, we recently announced the closure of our Virginia repair center and the transition of its business into our Florida facility. We will continue to evaluate our operations and implement actions we deem appropriate to counter the near term challenges in our markets while preserving our ability to be responsive to our customers as the economy improves.

RESULTS OF OPERATIONS

Our senior management regularly reviews the performance of our operations including reviews of key performance metrics and the status of operating initiatives. We review information on the financial performance of the operations, new business opportunities, customer relationships and initiatives, IR&D activities, human resources, manufacturing effectiveness, cost reduction activities, as well as other subjects. We compare performance against budget, against prior comparable periods and against our most recent internal forecasts.

We believe overall prospects for our financial performance to be very good over the long term, but expect our operations to remain challenging during the short term. Our backlog declined from prior year levels due to the worldwide slow economy that caused most aircraft manufacturers to scale back production in the near term. Our financial performance in fiscal year 2011 was adversely affected by the slower economy generally and in the aerospace industry in particular that contributed to reduced sales as well as by our continued investment in the development of new products. The Virginia property held for sale uses cash for continued maintenance and debt servicing without contributing to our operations, thereby adversely affecting our results of operations.

Our ability to enhance gross profit and operating results will require that we continuously improve throughput in our manufacturing processes while reducing costs and inefficiencies in our operations through better resource management. We are well engaged in implementing lean manufacturing principles, supported by training programs, to further develop a consistent, disciplined, and innovative engineering and production culture. We complement these initiatives with a marketing and sales strategy that builds on our market presence and core competencies in sensor, air data computation, and display technologies.

We believe that the investments that the Company has been making, and will continue to make in support of our customers, will pay off strongly as our markets continue their recovery. Greatly improved operating metrics, as well as direct customer feedback with respect to quality and delivery performance, is resulting in the Company being far better positioned to win new business. Our improved systems, focused value stream teams, and growing capabilities should enable us to far more reliably fulfill commitments to our customers, suppliers, and shareholders.

Fiscal year 2011 compared to fiscal year 2010

Net sales were $29,618,000 during fiscal year 2011, a decrease of $1,518,000, or 5%, compared to $31,136,000 for fiscal year 2010. During fiscal year 2011, our sales volume decreased from the prior year by approximately $5.1 million on reduced demand for air data products, sensing products, spares, electronic display instruments and air data test equipment, offset by approximately $3.1 million of increased sales volume of instrumentation and $0.5 million of repairs and other sales.

Gross profit for fiscal year 2011 was 30.8% compared to 34.9% for fiscal year 2010. The decrease in gross profit in fiscal year 2011, as a percent of sales, reflects (a) the effects of a significantly higher mix of mechanical products that produce lower gross margins versus the higher sales of transmitter products, sensor products and spares in the prior year, (b) lean investment activities, and (c) contract loss provisions of approximately $1,227,000 on three customer funded development contracts. These customer-funded programs generating the contract loss provisions are nearing their final stages of development and entering the qualification testing stage. We view these costs as investments in technology and capabilities that we expect to benefit future business opportunities.

Selling, general and administrative expenses for fiscal year 2011 increased $690,000, or 10%, compared to fiscal year 2010. The net increase was primarily due to (a) increases in IR&D costs, offset by (b) decreases in legal and consulting expenses.

Interest expense, net increased to $745,000 in fiscal year 2011 from $602,000 in fiscal year 2010, in large part because of interest expense relating to the Investors' Notes Payable (as defined below) and an increased debt balance.

Gains from casualty of $235,000 and $550,000 in fiscal years 2011 and 2010, respectively, relate to the insurance claim from our August, 2008 fire. We reported a loss on extinguishment of debt in fiscal year 2011 in the amount of $78,000 representing (a) accelerated accretion expense relating to the portion of the Notes Payables repaid early and (b) costs relating to the extinguishment of debt with our prior bank.

Income tax expense was $455,000 in fiscal year 2011 compared to a tax benefit of $172,000 for fiscal year 2010. Fiscal year 2010 was favorably impacted by the $1,900,000 reversal of the valuation allowance recorded in fiscal year 2009, the effects of which were partly offset by significantly increased profitability generated by operations in fiscal year 2010.

For fiscal year 2011, our net income was approximately $625,000, or $0.17 basic and $0.15 diluted income per share, compared to net income of approximately $4,261,000, or $1.15 basic and $1.09 diluted income per share for the year ended January 31, 2010. The decrease in net income for fiscal year 2011 was driven by the decreased sales volume combined with lower gross margin performance, while fiscal year 2010 significantly benefitted from the reversal of the $1,900,000 tax valuation allowance. For fiscal year 2010, basic and diluted income per share included approximately $0.51 and $0.49, respectively, that was attributable to the reversal of the tax valuation allowance.

LIQUIDITY AND CAPITAL RESOURCES

Our principal sources of capital have been cash flows from operations and borrowings under our credit facility. As of January 31, 2011, we had approximately $162,000 in cash and cash equivalents, compared to approximately $0 as of January 31, 2010. In addition, as of January 31, 2011, we had $1,687,000 available under the Credit Facility described below.

Our cash provided by operating activities was $511,000 for fiscal year 2011, an increase in cash provided of $543,000 compared to cash used of $32,000 for fiscal year 2010. This net increase in cash provided by operating activities is primarily attributable to increases in cash provided by operating activities of:

- $2,365,000 from decreased repayments of customer advances in fiscal year 2011, compared to repayments of customer advances in fiscal year 2010,
- $954,000 from an increase to the contract loss provision,
- $659,000 from increased accrual of expenses and other liabilities in fiscal year 2011 compared to expense accrual levels in fiscal year 2010 and
- $570,000 from a noncash provision for income taxes for fiscal year 2011 compared to the provision for income taxes for fiscal year 2010;

primarily offset by increases in cash used in operating activities of:

- $3,636,000 from decreased operating net income in fiscal year 2011 compared to operating net income in fiscal year 2010 and
- $800,000 from increased prepayment of expenses and other current assets in fiscal year 2011 compared to fiscal year 2010.

Our cash used in investing activities decreased $1,083,000 in fiscal year 2011 compared to fiscal year 2010 due primarily to purchases of $908,000 in capital improvements and equipment during fiscal year 2011 compared to purchases of $1,991,000 of capital improvements and equipment during fiscal year 2010 related primarily to the replacement of fixed assets lost in the August 2008 fire.

Our cash provided by financing activities for fiscal year 2011 was $559,000 compared to cash provided by financing activities in fiscal year 2010 of $2,023,000. The change was attributable to $611,000 of net proceeds from our refinancing of the Wachovia Bank debt facilities with our M&I Bank credit facility, as well as an additional $600,000 of proceeds from the Investors' Notes Payable described below, both during fiscal year 2011. We paid down the Notes Payable during fiscal year 2011 in the amount of $800,000 and fully paid the remaining balance of the Investors' Notes Payable on March 31, 2011.

Our days sales in accounts receivable unfavorably increased to 57 days at January 31, 2011, up from 40 days at January 31, 2010, due in large part to our customers' lengthening their payment cycles. Through cash management and purchasing practices, our outstanding balances with production suppliers favorably improved as days purchases in accounts payable decreased to 46 days at January 31, 2011, down from 52 days at January 31, 2010. We continue to be challenged to maintain favorable payment terms with certain suppliers. We continue to deal with residual production issues from the impact of the August 8, 2008 fire. During fiscal year 2011, we repaid the remaining $452,000 in customer advances outstanding at January 31, 2010, which those customers made to us to accommodate our financial circumstances following the fire. We have not yet sold the Earlysville, Virginia facility, although active marketing efforts are continuing.

Because of these circumstances and the decline in our income compared fiscal year 2010, we continue to experience liquidity constraints. We will depend on our ability to achieve expected operating results to maintain sufficient liquidity to (i) satisfy working capital requirements, (ii) fulfill necessary capital spending, and (iii) meet our debt obligations in fiscal year 2012 and beyond. Our failure to successfully achieve these results could have a material adverse effect on our liquidity and operations and could require us to implement curative measures, including raising capital, deferring planned capital expenditures, reductions in force, further facility consolidation, reducing discretionary spending, and selling assets.

M&I Bank Credit Facility

On April 30, 2010, we entered into a Loan Agreement (the "Loan Agreement") with M&I Bank with a maximum amount of credit facilities available to us of $10,100,000 (collectively, the "Credit Facility"). The Loan Agreement provides for (a) a $4,000,000 revolving line of credit (the "Revolving Credit Line Note") used for working capital, (b) a $3,500,000 first real estate mortgage loan (the "Real Estate Mortgage Note") used to refinance an existing loan related to our Clearwater, Florida facility, (c) a $1,900,000 term loan (the "Equipment Term Note" and together with the Real Estate Mortgage Note, the "Bank Notes") used to refinance an existing loan relating to the Earlysville, Virginia property and for working capital and capital expenditure needs, and (d) a $700,000 equipment line of credit (the "Equipment Credit Line Note" and together with the Revolving Credit Line Note, the "Credit Line Notes") used to purchase equipment for use in our business. The Credit Facility is secured by substantially all of our assets.

Actual amounts available under the Revolving Line Note are determined by a defined borrowing base consisting primarily of our eligible receivables and inventory. As of January 31, 2011, we had $1,687,000 available for advances under the Revolving Line Note. We are in discussions with our lender to extend the Revolving Credit Note, which is scheduled to mature on June 28, 2011. The interest rate on the Revolving Credit Line Note is one month LIBOR plus 300 basis points with a 4% floor.

The Real Estate Mortgage Note has a three-year term, a 15 year amortization period and the interest rate is one month LIBOR plus 340 basis points with a 4% floor. The Equipment Term Note has a three-year term, a five year amortization period and the interest rate is one month LIBOR plus 340 basis points with a 4% floor. The Equipment Credit Line Note has a three-year term, a five year amortization period, and the interest rate is one month LIBOR +325 basis points with a 4% floor.

We used proceeds from the Credit Facility, in part, to fully satisfy outstanding debt and fees owed to Wachovia Bank, our former lender, of $7,521,830. We will use available funds received and financing available under the Credit Facility for new product development, working capital, and capital expenditure needs.

Our Loan Agreement contains financial and other restrictive covenants which required that as of January 31, 2011, we maintain: (i) on a consolidated basis, Total Stockholders' Equity, defined as the value of total assets less total liabilities, equal to at least $7,419,000, which increases on a quarterly basis in an amount equal to ninety percent (90%) of our net income (calculated on a consolidated basis) for the quarter; (ii) on a consolidated basis, a ratio of Funded Debt, defined as all outstanding liabilities for borrowed money and other interest-bearing liabilities, including current and long term debt, less the non-current portion of Subordinated Liabilities, defined as liabilities subordinated to our obligations to the lender in a manner acceptable to the lender in its sole discretion, to EBITDA not exceeding 3.0:1.0; and (iii) on a consolidated basis, a Fixed Charge Coverage Ratio, defined as the ratio of (a) the sum of EBITDA plus lease expense and rent expense, minus income tax, minus dividends, withdrawals, and other distributions, to (b) the sum of cash interest expense, lease expense, rent expense, scheduled principal amortization actually paid to the lender during the measuring period (excluding any principal payments under the Revolving Credit Line Note and the Investors' Notes Payable), and scheduled payments on capitalized lease obligations during the measuring period, of at least 1.20:1.0. We calculate these covenants at the end of each quarterly reporting period for which the lender requires financial statements.

For the period measured as of January 31, 2011, we did not comply with the Funded Debt to EBITDA covenant in the Credit Facility. On April 28, 2011, the lender waived our non-compliance with the Funded Debt to EDITDA covenant. On April 29, 2011, pursuant to a Joint Amendment to Loan Agreement and Revolving Line of Credit Note, the lender amended the Funded Debt to EBITDA covenant to 4.0:1.0 for the balance of fiscal year 2012. The lender also extended the maturity date of the Revolving Credit Line Note to June 28, 2011. Although the lender waived our compliance with this covenant and amended the Credit Facility, there is no assurance that the lender will waive compliance or amend the Credit Facility in future periods, if such a waiver or amendment is needed. We are in discussions with the lender to further extend the maturity of the Revolving Credit Line Note for another year, but there is no assurance that the lender will do so.

On October 12, 2010, we borrowed an additional $700,000 on the Equipment Credit Line Note, which replenished cash that we used to purchase and construct equipment over the 12 months before that date. We used this borrowed cash to accelerate repayment of the Investors' Notes Payable, as described below.

Investors' Notes Payable

On May 14, 2009, we entered into separate unsecured loans (the "Notes Payable") with three separate private investors (collectively, "the Investors"): Bruce J. Stone, Redmond Family Investments, LLLP and Martin L. Schaffel. Each Note Payable contained a drawdown provision allowing us to borrow up to an aggregate of $2,000,000. Documentation for the Notes Payable provided for issuance of warrants with an exercise price of $0.64 per warrant issued at the rate of one warrant for every four dollars loaned to us and common shares at the rate of one share for every ten dollars loaned to us. Additionally, any amounts borrowed are subject to 14% interest per annum, payable monthly.

On May 21, 2009, we borrowed an aggregate principal amount of $800,000 under the Notes Payable. This transaction resulted in issuance of 200,000 warrants to the Investors that are exercisable until the warrants expire on April 10, 2015, as well as 80,000 common shares. This aggregate amount borrowed of $800,000 was initially payable in full under each of the three notes on or before April 10, 2010. The warrants and common shares are recorded as a separate component of interest and are being accreted into the loan balance over the term of the loan.

On February 19, 2010, we borrowed an additional $600,000 from the Investors under the Notes Payable and entered into amendments to the Notes Payable. These modifications (a) extended the maturity date of the subordinated notes for a period of one year from April 10, 2010 to April 10, 2011, (b) removed our obligation to issue shares of our common stock on each cash drawdown made on or after February 19, 2010, (c) revised the ratio of common shares underlying warrants issuable per each $1.00 of principal amount borrowed from ".25 shares per $1.00 of principal amount" to ".20 shares per $1.00 of principal amount" with respect to cash drawdowns made on or after February 19, 2010, and (d) deleted certain negative covenants relating to the issuance of securities. The warrant modifications (a) extended the expiration date of any warrants issued prior to February 19, 2010 for a period of five years from April 10, 2015 to April 10, 2020, (b) extended the expiration date of any warrants issued on or after February 19, 2010 from April 10, 2015 to the sixth anniversary date of the issuance of the warrant certificate, and (c) revised the purchase price for any warrants issued on or after February 19, 2010 from $0.64 per share to a price equal to 50% of the volume weighted average of the selling price of our common stock on February 12, 2010 and for the 19 trading days prior to February 12, 2010, or $1.98 per share. The related warrants (120,000 issued to the Investors pursuant to the additional $600,000 loan) are exercisable at any time before the warrants expire on February 19, 2016.

The warrants and common shares issued under the Notes Payable are recorded as a separate component of interest and are being accreted into the loan balances over the term of the loans. For the fiscal years ended 2011 and 2010, we recognized accretion of $263,000 and $294,000, respectively, presented as additional interest expense. In addition, as a result of early repayments to the Investors during fiscal year 2011, we recognized accelerated interest accretion expense in the amount of $78,000, which is reported as loss on extinguishment of debt.

On March 31, 2011, we completed repayment of the Notes Payable in full satisfaction of the remaining debt outstanding of $600,000 as of January 31, 2011.

Working Capital and Capital Expenditures

Our working capital at January 31, 2011 was $8,496,000 compared to $2,326,000 at January 31, 2010. An increase in working capital of $4,985,000 as of January 31, 2011 relates primarily to the reclassification of long-term debt from current liabilities to non-current liabilities due to the refinancing of our bank debt with Wachovia Bank by M&I Bank. Additionally, increases to accounts receivable and prepaid and other current assets in the amount of $1,232,000 and $1,367,000, respectively, contributed to the increase. These favorable working capital variances are offset in part by an unfavorable working capital variance associated with an increase in accrued liabilities of $1,175,000.

The collection of our accounts receivable is the primary source of cash used to fund our operations. Our banking line of credit is used as an additional source of cash as necessary from time to time, and we sweep any excess cash back against the line of credit on a daily basis to minimize interest expense. Provided we achieve expected operating results, we believe that cash collected from our accounts receivable, as further supplemented by advances under our banking facilities, will be adequate to fund our ongoing operations for the next twelve months.

Our future capital requirements depend on numerous factors, including research and development, expansion of product lines and other factors. Furthermore, we may need to develop and introduce new or enhanced products, respond to competitive pressures, invest or acquire businesses or technologies or respond to unanticipated requirements or developments, which would require additional resources. Currently, our constrained cash flow from operations prohibits us from meeting these challenges through organic growth.

Our capital expenditures for fiscal year 2011 were $908,000, compared to $1,991,000 for fiscal year 2010. Historically, our capital budget was intended to replace fixed asset equipment as needed and to take advantage of technological improvements that would improve productivity. We replaced certain critical fixtures, environmental test chambers and testing equipment that we lost in the August, 2008 fire during fiscal years 2011 and 2010. Additionally, we renovated and reconfigured our Florida production facility in those years to accommodate equipment previously located in our building destroyed in the fire.

Inflation and Changing Prices

Our profitability is dependent, among other things, on our ability to anticipate and react to changes in the cost of key operating resources, including labor and raw materials. Substantial increases in cost of sales and expenses could impact our operating results to the extent that such increases cannot be passed along to customers. While we are taking steps to mitigate our risk to rising prices with prudent purchasing practices and improving our inventory management techniques, there can be no assurance that future supplies of raw materials and labor will not fluctuate due to market conditions outside of our control.

Certain operating costs such as taxes, insurance and other outside services continue to increase at or above the general rate of inflation, and we may be subject to other cost and supply fluctuations outside of our control.

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Off-Balance Sheet Arrangements

We did not have any off-balance sheet arrangements as of January 31, 2011.

Contractual Obligations

The following table presents estimated cash requirements for contractual obligations outstanding as of January 31, 2011.

	Payments Due By Period				
	Less Than One Year	One Year to 3 Years	Greater Than 3 Years to 5 Years	After 5 Years	Total
Purchase commitments	$2,932,000	$522,000	$ -	$ -	$3,454,000
Long-term debt	1,255,000	4,658,000	327,000	-	6,240,000
Revolving credit facility	2,313,000	-	-	-	2,313,000
Operating leases	175,000	151,000	-	-	326,000
Total contractual obligations	$6,675,000	$5,331,000	$ 327,000	$ -	$12,333,000

Acquisitions

On August 21, 2007 (the "Closing Date") we purchased 100% of the outstanding stock of OP Tech, an Oregon-based developer and manufacturer of cockpit glass display solutions, from Optimization Technologies, Inc., an Oregon corporation (the "Seller"). The acquisition of OP Tech is consistent with our strategic plan for revenue growth into related industry markets. The acquisition was accounted for by the purchase method.

In connection with the acquisition, we, OP Tech, and the Seller, along with certain holders of the Seller's capital stock, entered into a Share Purchase Agreement (the "SPA"), whereby we paid $1,000,000 to the Seller. The SPA also provides for the Seller to additionally receive: (i) up to $80,000 payable in our common stock once we obtain certain federal certifications for OP Tech's products, subject to Seller's delivery of a duly executed subscription agreement, which provides for the Seller's receipt of such stock, and a duly executed lock-up agreement, which prohibits a transfer by Seller for two years from the date of issuance of such stock and (ii) up to $1,000,000 if certain sales targets ($10,000,000 or greater) are met with respect to OP Tech's products within three years of the Closing Date. As of January 31, 2011, no additional consideration has been recorded, nor have the contingencies been met.

Environmental Matters

In preparation for the sale of the Earlysville, Virginia facility, we engaged an environmental consulting firm to survey the property for any possible soil or groundwater contamination. This survey revealed impacts to both shallow soils and groundwater that may have resulted from the accidental loss of solvents by a former owner of the property. As a result of the initial and subsequent surveys, the remaining contamination treatment costs are estimated at $808,000 as of January 31, 2011. The Company has capitalized these contamination treatment costs as an increase to property held for sale, net, since such costs will be incurred in preparation for the sale of the Earlysville, Virginia facility and will not result in a carrying value in excess of the estimated fair value less costs to sell. Costs incurred during the year ended January 31, 2011 totaled $124,000 and costs incurred during the year ended January 31, 2010 totaled $153,000. At this time, we cannot predict how much, if any, we will incur for more costs in fiscal year 2012.

After the August 8, 2008 fire at our Clearwater, Florida facility, during a routine investigation by local environmental agencies we were cited for several violations relating to the storage, handling and disposal of normal chemicals, solvents and paints used in our production facility. Our remediation plan, to avoid future violations and the payment of the above civil penalties, was submitted and subsequently approved by the Florida DEP. During the three months ended April 30, 2010, the Company completed the construction of a materials handling building at a cost of $116,000. On June 7, 2010, the Company received a release of said violations and civil penalties from the Florida DEP.

CRITICAL ACCOUNTING POLICIES

The discussion and analysis of our financial condition and results of operations are based upon the accompanying consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States ("U.S. GAAP"). The preparation of those consolidated financial statements and this Annual Report on Form 10-K requires us to make estimates and judgments that affect the reported amount of assets and liabilities, revenues and expenses, and related disclosure items, including disclosure of contingent assets and liabilities, at the date of our consolidated financial statements. Actual results may differ from these estimates under different assumptions or conditions, and as a result of trends and uncertainties identified above under "Results of Operations" and "Liquidity and Capital Resources" and in "Item 1A. Risk Factors". Further, such differences could be material.

Set forth below is a discussion of our critical accounting policies. We consider critical accounting policies to be those (i) that require us to make estimates that are highly uncertain at the time the estimate is made, (ii) for which a different estimate which could have been made would have a material impact on our consolidated financial statements, (iii) that are the most important and pervasive policies utilized, and (iv) that are the most sensitive to material change from external factors. Additionally, the policies discussed below are critical to an understanding of the consolidated financial statements because their application places the most significant demands on our judgment, with financial reporting results relying on estimates about the effect of matters that are highly uncertain. Specific risks for these critical accounting policies are described in the following paragraphs. The impact and any associated risks related to these policies on business operations is discussed throughout this MD&A where such policies affect reported and expected financial results.

For a detailed discussion regarding the application of these and other accounting policies, see Note 1 to the accompanying consolidated financial statements. We have discussed the development and selection of the critical accounting estimates and the related disclosure included herein with the Audit Committee of the Board of Directors.

Revenue Recognition

The Company generally recognizes revenue from sales of its products when the following have occurred: evidence of a sale arrangement exists; delivery or shipment has occurred or services have been rendered; the price to the buyer is fixed or determinable; and collectability is reasonably assured.

For fixed-price contracts, the Company may recognize revenue on a Units of Accounting basis. The Units of Accounting method requires the Company to evaluate all deliverables in an arrangement to determine whether they represent separate units of accounting. The Company makes that determination at the inception of the arrangement and as each item in the arrangement is delivered. In an arrangement with multiple deliverables, the delivered item(s) shall be considered a separate unit of accounting if (a) the delivered item(s) have value to the customer on a standalone basis, (b) there is objective and reliable evidence of the fair value of the undelivered item(s) and (c) if the arrangement includes a general right of return relative to the delivered item(s), delivery or performance of the undelivered item(s) is considered probable and substantially in the control of the vendor.

The Company may also recognize its revenue under the completed contract method.

For long-term, fixed-price contracts meeting certain criteria, the Company may elect to follow the percentage-of-completion method of accounting for revenue recognition. Under this method, contract revenue is computed as that percentage of estimated total revenue that costs incurred to date bear to total estimated costs, after giving effect to the most recent estimates of costs to complete. From time to time, the Company will record costs and estimated profits in excess of billings for a contract. Revisions in costs and revenue estimates are reflected in the period in which the revisions are determined. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are determined without regard to the percentage-of-completion.

Occasionally the Company enters into research and development contracts with customers. When the contracts provide for milestone or other interim payments, the Company will recognize revenue either under the Milestone method or the Units of Accounting method. The Milestone method requires the Company to deem all milestone payments within each contract as either substantive or non-substantive. That conclusion is determined based upon a thorough review of each contract and the Company’s deliverables committed to in each contract. For substantive milestones, the Company concludes that upon achievement of each milestone, the amount of the corresponding defined payment is commensurate with the effort required to achieve such milestone or the value of the delivered item. The payment associated with each milestone relates solely to past performance and is deemed reasonable upon consideration of the deliverables and the payment terms within the contract. For non-substantive milestones, including advance payments, the recognition of such payments are pro-rated to the substantive milestones. Milestones may include, for example, the successful completion of design review or technical review, the submission and acceptance of technical drawings, delivery of hardware, software, spares, test equipment or regulatory agency certifications.

Accounts Receivable Allowance for Doubtful Accounts and Credit Losses

We continuously evaluate our customers and provide reserves for anticipated credit losses as soon as collection becomes compromised. While credit losses have historically been within expectations of the provisions established, we cannot guarantee that we will continue to experience the same credit loss rates that have been experienced in the past. Measurement of such losses requires consideration of historical loss experience, including the need to adjust for current conditions, and judgments about the probable effects of relevant observable data, including present economic conditions such as delinquency rates and financial health of specific customers.

Inventories

The Company values inventory at standard cost which generally reflects the most recent significant cost for manufactured or purchased inventory. Standards are revalued from time to time to reflect the lower of cost (using a method that approximates the first-in, first-out method “FIFO”) or net realizable value. The reserve for obsolete and slow moving inventory is based upon reviews of inventory quantities on hand, usage and sales history.

Work In Process Inventories

We employ certain methods to estimate the value of work in process inventories for financial reporting purposes. Our practice has been to conduct cycle counts of inventory throughout the year. Generally, for items that are in process at the end of a fiscal year, we will make an estimate during the cycle counting process regarding the percentage of completion of such items in order to accurately reflect costs incurred to date on the production of the items that are still in process. These estimates are affected by the nature of the operation at which the items are located at the time a physical inventory is conducted, and are subject to judgment. This practice was employed for fiscal years 2011 and 2010.

Manufacturing Overhead Cost Application

We establish our inventoriable cost of manufacturing overhead by calculating our overhead costs as a percentage of direct labor and applying that percentage to direct labor that has been charged to inventory on a twelve month rolling average basis. This application percentage is reviewed and adjusted annually.

Deferred Tax Asset Valuation Allowance

We account for income taxes in accordance with U.S. GAAP, which states that deferred tax liabilities and assets are determined based on the difference between the financial statement carrying amounts and tax bases of assets and liabilities using enacted tax rates in effect in the years in which the differences are expected to reverse. A valuation allowance is provided against the future benefit of deferred tax assets to the extent it is determined that it is more likely than not that the future tax benefits associated with the deferred tax asset will not be realized.

Property Held for Sale

Property held for sale is reported at the lower of its carrying amount or fair value less cost to sell. Depreciation on property held for sale is discontinued at the time the criteria, established by U.S. GAAP, are met. The Earlysville, Virginia property is presently held for sale. The property consists of a 53,000 square foot manufacturing facility on approximately 12 acres of land. In preparation for the sale of the Earlysville, Virginia facility, we engaged an environmental consulting firm to survey the property for any possible soil or groundwater contamination. This survey revealed impacts to both shallow soils and groundwater that may have resulted from the accidental loss of solvents by a former owner of the property. As a result of the initial and subsequent surveys, the remaining contamination treatment costs are estimated at $808,000 as of January 31, 2011. We have capitalized these contamination treatment costs as an increase to property held for sale, net, since such costs will be incurred in preparation for the sale of the Earlysville, Virginia facility and will not result in a carrying value in excess of the estimated fair value less cost to sell. Costs incurred during the year ended January 31, 2011 totaled $124,000 and costs incurred during the year ended January 31, 2010 totaled $153,000. At this time, we cannot predict how much, if any, we will incur for more costs in fiscal year 2012.

Goodwill and Intangible Assets

The carrying value of goodwill is reviewed at least annually for impairment and will be reviewed more frequently if current events and circumstances indicate a possible impairment. An impairment loss is charged to expense in the period identified. As current events and circumstances warrant, the Company examines the carrying value of its intangible assets with finite lives, such as capitalized software and development costs, purchased intangibles, and other long-lived assets, to determine whether there are any impairment losses. If indicators of impairment are present and future cash flows are not expected to be sufficient to recover the asset's carrying amount, an impairment loss is charged to expense in the period identified. Factors that may cause impairment include negative industry or economic trends or significant underperformance relative to historical or projected future operating results.

Long-Lived Assets

The useful lives of property, plant and equipment for purposes of computing depreciation are:

Land improvements	15-20 Years
Buildings and improvements	25-40 Years
Machinery and equipment	3-15 Years
Patterns, dies, and tools	3-5 Years

Furniture and fixtures	5-10 Years

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We periodically evaluate long-lived assets for potential impairment and will record an impairment charge whenever events or changes in circumstances indicate the carrying amount of the assets may not be fully recoverable. As of January 31, 2011 and 2010, we do not believe that any assets are impaired.

We will capitalize production costs for computer software that is to be utilized as an integral part of a product when both (a) technological feasibility is established for the software; and, (b) all research and development activities for the other components of the product have been completed. Amortization is charged to expense at the greater of the expected unit sales versus units sold or the straight line method for a period of three years from the date the product becomes available for general release to customers.

Income Taxes

The Company and its includable subsidiaries file a consolidated U.S. federal income tax return in accordance with the provisions of the Internal Revenue Code of 1986, as amended.

The Company's accounting for income taxes represents management's best estimate of various events and transactions.

Deferred tax assets and liabilities resulting from temporary differences between the financial reporting and tax bases of assets and liabilities are measured at the balance sheet date using enacted tax rates expected to apply to taxable income in the years the temporary differences are expected to reverse.

The realization of deferred tax assets depends upon the existence of sufficient taxable income within the carryback or carryforward periods under the tax law in the applicable tax jurisdiction. Valuation allowances are established when management determines, based on available information, that it is more likely than not that deferred income tax assets will not be realized. Significant judgment is required in determining whether valuation allowances should be established as well as the amount of such allowances. When making such determination, consideration is given to, among other things, the following:

- future taxable income exclusive of reversing temporary differences and carryforwards;
- future reversals of existing taxable temporary differences;
- taxable income in prior carryback years; and
- tax planning strategies.

The Company classifies tax related interest and tax related penalties as a component of income taxes.

Research and Development

Research and development costs are expensed in the period incurred.

Environmental Expenditures

The Company assesses its property held for sale, along with any property that is being taken out of its initially intended use, for the presence of hazardous or toxic substances that would result in an environmental liability. In addition, management assesses its current property in use for any environmental issues.

Liabilities for environmental remediation costs not related to retirements of tangible long-lived assets, and arising from claims, assessments, litigation, fines, and penalties and other sources, are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated.

Legal costs incurred in connection with environmental remediation are expensed as incurred. Recoveries of environmental remediation costs from third parties, which are probable of realization, are separately recorded as assets, and are not offset against the related environmental liability, in accordance with U.S. GAAP.

Stock-Based Compensation

The Company adopted the fair value recognition provisions of U.S. GAAP using the modified-prospective-transition method which requires us to recognize compensation expense on a prospective basis. U.S. GAAP requires that all stock-based compensation be recognized as an expense in the financial statements and that such cost be measured at the fair value of the award. Under this method, in addition to reflecting compensation for new share-based awards, expense is also recognized to reflect the remaining service period of awards that had been included in pro-forma disclosure in prior periods. The stock-based compensation expense is included in selling, general and administrative expenses in the consolidated statements of operations. During the fiscal years ended January 31, 2011 and January 31, 2010, the Company recorded stock-based compensation of $241,000 and $246,000, respectively.

Stock issued in payment for services provided by members of the board of directors is expensed in the period the services are provided. During both fiscal years ended January 31, 2011 and January 31, 2010, the Company recorded director-fees expense, through the issuance of stock, of $60,000.

Use of Estimates

We prepare our consolidated financial statements in conformity with U.S. GAAP. These principles require management to make estimates and judgments that affect reported and contingent amounts of assets, liabilities, revenues and expenses, including such items as (i) inventory, restructuring and environmental costs, (ii) percentage-of-completion estimates, (iii) other miscellaneous accruals and (iv) valuation allowances for accounts receivable, inventory and deferred tax assets. Actual results may differ from these estimates under different assumptions or conditions, and such differences could be material.

Adoption of New Accounting Pronouncements

In April 2011, the FASB issued new accounting guidance for purposes of measuring the impairment of receivables and evaluating whether a troubled debt restructuring has occurred. An entity should disclose the total amount of receivables and the allowance for credit losses as of the end of the period of adoption related to those receivables that are newly considered impaired under Section 310-10-35 for which impairment was previously measured under Subtopic 450-20, Contingencies–Loss Contingencies. Currently, this guidance is anticipated to be effective for interim and annual periods ending after June 15, 2011. The adoption of this guidance is not expected to have an impact on our consolidated financial position, results of operations, cash flows, or disclosures.

In December 2010, the FASB issued ASU 2010-28, Intangibles – Goodwill and Other (Topic 350): When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts . The ASU does not prescribe a specific method of calculating the carrying value of a reporting unit in the performance of step 1 of the goodwill impairment test (i.e. equity-value-based method or enterprise-value-based method). However, it requires entities with a zero or negative carrying value to assess, considering qualitative factors such as those used to determine whether a triggering event would require an interim goodwill impairment test (listed in ASC 350-20-35-30, Intangibles – Goodwill and Other – Subsequent Measurement), whether it is more likely than not that a goodwill impairment exists and perform step 2 of the goodwill impairment test if so concluded. ASU 2010-28 is effective for the Company beginning January 1, 2011 and early adoption is not permitted. The Company does not expect the adoption of ASU 2010-28 to have a material impact on its consolidated financial position or results of operations.

In April 2010, the FASB issued new authoritative guidance surrounding revenue recognition, specifically addressing the criteria for recognizing revenue tied to research and development efforts. The guidance adds the milestone method to the list of acceptable methods of revenue recognition when accounting for multiple element arrangements within research and development efforts. The guidance is effective for milestones achieved in fiscal years beginning on or after June 15, 2010, unless early adoption is elected. The Company adopted the guidance beginning the quarter ended July 30, 2010, which required retrospective application from the beginning of the fiscal year. The adoption of this guidance did not have a material impact on the Company's financial statements.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

We do not issue or invest in financial instruments or their derivatives for trading or speculative purposes. Our market risk is limited to fluctuations in interest rates pertaining to our borrowings under our existing debt facilities which require the payment of interest at a variable rate equal to one-month LIBOR plus 300 to 340 basis points. We therefore are exposed to market risk from changes in interest rates on funded debt. Any increase in these rates could adversely affect our interest expense. The extent of market rate risk associated with fluctuations in interest rates is not quantifiable or predictable because of the volatility of future interest rates and business financing requirements. We use no derivative products to hedge or mitigate interest rate risk.

Based on the outstanding balances on our credit facilities as of January 31, 2011, a 1% increase in interest rates would cost us approximately $80,000 annually.

We purchase materials for use in our products based on market prices established with our suppliers. Many of the materials purchased can be subject to volatility due to market supply and demand factors outside of our control. To mitigate this risk, in part, we attempt to enter into fixed-price purchase agreements with reasonable terms.

We also have a market risk exposure to fluctuations in foreign exchange rates. We have a limited number of purchase and sale transactions that are denominated in British Pounds. Our strategy in managing this risk exposure is to match the timing of British Pound-denominated cash inflows and outflows.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The consolidated financial statements and supplementary data required by Item 8 are listed in the index beginning on page F-1 and are included in this Form 10-K.

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

None

ITEM 9A. CONTROLS AND PROCEDURES

Evaluation of Disclosure Controls and Procedures

The Company maintains disclosure controls and procedures, as defined in Rules 13a-15(e) and 15(d)-15(e) under the Securities Exchange Act of 1934, as amended (the “Exchange Act”). These disclosure controls and procedures are designed to ensure that information required to be disclosed by the Company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized, and reported within the time periods specified in the SEC’s rules and forms, and that such information is accumulated and communicated to Company’s management, including its Chief Executive Officer and Chief Financial Officer, as appropriate, to allow timely decisions regarding required disclosure.

Evaluation of Disclosure Controls and Procedures as of January 31, 2010

For the fiscal year ended January 31, 2009, the Company's Chief Executive Officer and Acting Chief Financial Officer determined that a material weakness existed surrounding the adequate accounting for inventory. This material weakness was attributable to the loss of records and other financial data as a result of the August 8, 2008 fire that destroyed one of the buildings comprising our Clearwater, Florida facility and required re-creation of standard costing measurements for raw materials, work in process and finished goods inventory. We decided on a course of action to address specific areas for improvement in our standard cost accounting system, thereby addressing the contributors to the material weakness surrounding the adequate accounting for inventory. As of January 31, 2010, a number of improvements to the standard cost accounting system had been implemented and a number of mitigating controls had been established. However, as of the year ended January 31, 2010, the Company's Chief Executive Officer and Chief Financial Officer concluded that (i) a material weakness continued to exist surrounding the adequate accounting for inventory despite significant control improvements that were implemented in fiscal year 2010 and (ii) due to this material weakness, our disclosure controls and procedures were not effective, as of January 31, 2010, at a reasonable level of assurance, to ensure that information we are required to disclose in the reports that we file or submit under the Exchange Act is (1) recorded, processed, summarized and reported within the time periods specified in the SEC's rules and forms, and (2) accumulated and communicated to our management, including the Company's Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding required disclosure.

Clarification of Management's Conclusion Regarding the Effectiveness of Disclosure Controls and Procedures as of January 31, 2010

Although our annual report on Form 10-K for the year ended January 31, 2010 (the "2010 10-K") indicated management's implicit conclusion that our disclosure controls and procedures were not effective as of January 31, 2010, the Company failed to expressly state in the 2010 10-K that the Company's Chief Executive Officer and Chief Financial Officer concluded that, as of January 31, 2010, our disclosure controls and procedures were not effective. However, by way of clarification, the Company has included this express conclusion above under the heading "Evaluation of Disclosure Controls and Procedures as of January 31, 2010."

Evaluation of Disclosure Controls and Procedures as of January 31, 2011

During fiscal year 2011, the Company addressed the remaining issues in our standard cost system that contributed to the material weakness existing as of January 31, 2010 by significantly improving our internal controls relating to the adequate accounting for inventory, as described in more detail below under the heading "Management's Annual Report on Internal Control over Financial Reporting."

As of the end of the period covered by this report, the Company carried out, under the supervision and with the participation of the Company's management, including the Company's Chief Executive Officer and the Company's Chief Financial Officer, an evaluation of the effectiveness of the design and operation of the Company's disclosure controls and procedures, as such term is defined in Rules 13a-15(e) and 15d-15(e) of the Exchange Act. Based on that evaluation, the Company's Chief Executive Officer and the Company's Chief Financial Officer have concluded that, as of the end of the period covered by this report, our disclosure controls and procedures are effective to ensure that all material information required to be included in our reports filed or submitted under the Exchange Act is (1) recorded, processed, summarized and reported within the time periods specified in the rules and forms of the Securities and Exchange Commission and (2) accumulated and communicated to the Company's management, including the Company's Chief Executive Officer and Chief Financial Officer, to allow timely decisions regarding disclosure.

Management's Annual Report on Internal Control over Financial Reporting

Management is responsible for establishing and maintaining adequate internal control over financial reporting. Internal control over financial reporting is defined in Rule 13a-15(f) or 15d-15(f) promulgated under the Exchange Act as a process designed by, or under the supervision of, the Company's principal executive and principal financial officers and implemented by the Company's board of directors, management and other personnel, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with generally accepted accounting principles and includes those policies and procedures that:

- Pertain to the maintenance of records that in reasonable detail accurately and fairly reflect the transactions and dispositions of the assets of the company;
- Provide reasonable assurance that transactions are recorded as necessary to permit preparation of financial statements in accordance with Generally Accepted Accounting Principles, and that receipts and expenditures of the company are being made only in accordance with authorizations of management and directors of the Company; and
- Provide reasonable assurance regarding prevention or timely detection of unauthorized acquisitions, use or disposition of the company's assets that could have a material effect on the financial statements.

A significant deficiency is a deficiency or a combination of deficiencies, in internal control over financial reporting that is less severe than a material weakness, yet important enough to merit attention by those responsible for oversight of the registrant's financial reporting. A material weakness is a deficiency, or combination of deficiencies, in internal control over financial reporting such that there is a reasonable possibility that a material misstatement of the registrant's annual or interim financial statements will not be prevented or detected on a timely basis.

Because of its inherent limitations, internal control over financial reporting may not prevent or detect misstatements. Also, projections of any evaluation of effectiveness to future periods are subject to the risk that controls may become inadequate because of changes in conditions, or that the degree of compliance with the policies or procedures may deteriorate.

Financial management has documented and evaluated the effectiveness of the internal control of the Company as of January 31, 2011 pertaining to financial reporting in accordance with the criteria established in Internal Control-Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission ("COSO").

Based on management's assessment under the framework of the criteria in Internal Control-Integrated Framework issued by COSO, management concluded that our internal control over financial reporting was effective as of January 31, 2011.

Management, including our Chief Executive Officer and Chief Financial Officer, has evaluated the Company's internal control over financial reporting to determine whether any changes occurred during the year ended January 31, 2011 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. Based on that evaluation, there have been changes during the period covered by this report relating to the remediation of the material weakness concerning the adequate accounting for inventory.

The internal controls relating to the adequate accounting for inventory were significantly improved, including:

- The functionality and controls of the cost system are now understood and consistently applied,
- As additions to inventory occur, transactions are reviewed for proper coding and cost accounting,
- Standard costs are properly coded and costed to reflect production methods (i.e. manufactured processes versus purchased or subcontracted inventory),
- As inventory codes and standard costs are updated or initially established, we now have controls to ensure inventory valuations are calculated properly,
- Costs are updated in a test environment for thorough analysis prior to recording into inventory,
- We have enhanced our methods for identifying appropriate inventory provisions for obsolescence and slow moving inventory by analyzing inventory with more specificity and more routinely than in the past,
- We have improved our controls over physical inventory and we have established an effective cycle count program, and

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- We have also implemented a number of mitigating controls, including various analyses and reporting tools, to provide additional assurance that any material error will not be undetected.

As a result of these improvements, we believe that we now have proper review, application and control of the standard cost system and accounting for inventory.

ITEM 9B. OTHER INFORMATION

On January 10, 2011, we entered into a First Amendment to Loan Agreement (the “First Amendment”). The First Amendment amends Section 1.2 of the Loan Agreement by increasing the aggregate total inventory component of the borrowing base from $1.5 million to $2.0 million. The foregoing description of the amendment is not complete and is qualified in its entirety by the actual terms of the Amendment, a copy of which is incorporated herein by reference and attached as Exhibit 10.17.

On April 28, 2011, M&I Bank waived the Company’s January 31, 2011 non-compliance with the Funded Debt to EDITDA covenant in the Credit Facility.

On April 29, 2011, we entered into a Joint Amendment to Loan Agreement and Revolving Line of Credit Note (the “Amendment”). The Amendment amends the Funded Debt to EBITDA covenant within the Loan Agreement by changing this covenant to 4.0:1.0 for the balance of fiscal year 2012, and also extends the maturity date of the Revolving Credit Line Note to June 28, 2011. The foregoing description of the amendment is not complete and is qualified in its entirety by the actual terms of the Amendment, a copy of which is incorporated herein by reference and attached as Exhibit 10.18.

PART III

ITEM 10. DIRECTORS, EXECUTIVE OFFICERS AND CORPORATE GOVERNANCE

Information with respect to Directors and certain Executive Officers required by Item 10 shall be included in the Proxy Statement and is incorporated herein by reference.

ITEM 11. EXECUTIVE COMPENSATION

Information with respect to executive compensation required by Item 11 shall be included in the Proxy Statement and is incorporated herein by reference.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT AND RELATED STOCKHOLDER MATTERS

Information with respect to security ownership and the other matters required by Item 12 shall be included in the Proxy Statement and is incorporated herein by reference.

ITEM 13. CERTAIN RELATIONSHIPS, RELATED TRANSACTIONS AND DIRECTOR INDEPENDENCE

Information with respect to certain relationships and related transactions required by Item 13 shall be included in the Proxy Statement and is incorporated herein by reference.

ITEM 14. PRINCIPAL ACCOUNTANT FEES AND SERVICES

Information with respect to principal accountant fees and services required by Item 14 shall be included in the Proxy Statement and is incorporated herein by reference.

PART IV

ITEM 15. EXHIBITS AND FINANCIAL STATEMENT SCHEDULES

a) The following documents are filed as part of this Annual Report:

1. The financial statements listed in the index to Financial Statements following the signature pages hereof.
2. Exhibits

Exhibit No.	Description of Exhibit
3.1	Restated Certificate of Incorporation of Instrument Technology Corporation, filed on January 12, 1970, incorporated by reference to Exhibit 3.1 of the Company's Annual Report on Form 10-K for the year ended January 31, 2003, filed on October 31, 2003.
3.2	Certificate of Amendment to the Articles of Incorporation, changing the name Instrument Technology Corporation to Aerosonic Corporation, filed on September 21, 1970, incorporated by reference to Exhibit 3.3 of the Company's Annual Report on Form 10-K for the year ended January 31, 2003, filed on October 31, 2003.
3.3	Certificate of Amendment to the Articles of Incorporation of Aerosonic Corporation, filed on August 6, 1971, incorporated by reference to Exhibit 3.4 of the Company's Annual Report on Form 10-K for the year ended January 31, 2003, filed on October 31, 2003.
3.4	Certificate of Reduction of Capital of Aerosonic Corporation, filed on June 5, 1978, incorporated by reference to Exhibit 3.5 of the Company's Annual Report on Form 10-K for the year ended January 31, 2003, filed on October 31, 2003.
3.5	Certificate of Amendment to Articles of Incorporation of Aerosonic Corporation, filed on February 12, 1993, incorporated by reference to Exhibit 3.6 of the Company's Annual Report on Form 10-K for the year ended January 31, 2003, filed on October 31, 2003.
3.6	Amended and Restated Bylaws of the Company, incorporated by reference to Exhibit 3.8 of the Company's Annual Report on Form 10-K for the year ended January 31, 2005, filed on April 18, 2005.
4.1	Amendment to Aerosonic Corporation 2004 Stock Incentive Plan (as amended and restated on July 26, 2007), incorporated by reference to Appendix A of the Company's Definitive Proxy Statement on Schedule 14A, filed on June 1, 2009.
10.1*	Employment Agreement, dated April 17, 2008, between the Company and Douglas Hillman, incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K, filed on April 23, 2008.
10.2*	Amended and Restated Employment Agreement, dated November 28, 2005, between the Company and Mark Perkins, incorporated by reference to Exhibit 10.3 of the Company's Quarterly Report on Form 10-Q for the quarter ended October 28, 2005, filed on November 28, 2005.
10.3	

Employment Agreement, dated August 25, 2008, between the Company and Thomas Cason, incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K, filed on August 25, 2008.

10.4*	Aerosonic Corporation 2004 Stock Incentive Plan (as amended and restated on July 26, 2007), incorporated by reference to Exhibit 4.1 of the Company's Registration Statement on Form S-8, filed on August 31, 2007.
10.5	Share Purchase Agreement, dated August 21, 2007, between the Company, OP Technologies, Inc., Optimization Technologies, Inc. and certain shareholders thereof, incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K, filed on August 24, 2007.
10.6	Form of Loan Agreement, dated May 14, 2009, between the Company and Investors, incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K, filed on May 20, 2009.
10.7	Form of 14% Subordinated Note, dated May 14, 2009, between the Company and its wholly-owned subsidiaries, Avionics Specialties, Inc. and OP Technologies, Inc., and Investors incorporated by reference to Exhibit 10.2 of the Company's Current Report on Form 8-K, filed on May 20, 2009.
10.8	Form of Warrant Certificate between the Company and Investors, incorporated by reference to Exhibit 10.3 of the Company's Current Report on Form 8-K, filed on May 20, 2009.
10.9	Employment Agreement, dated May 26, 2009, between the Company and Kevin J. Purcell, incorporated by reference to Exhibit 10.1 of the Company's Current Report on Form 8-K, filed on May 29, 2009.
10.10	$4,000,000 Revolving Line of Credit Note dated as of April 30, 2010 between Aerosonic Corporation and M&I Marshall & Ilsley Bank, incorporated by reference to Exhibit 10.28 of the Company's Current Report on Form 10-K, filed on May 3, 2010.
10.11	$3,500,000 Real Estate Term Loan Note dated as of April 30, 2010 between Aerosonic Corporation and M&I Marshall & Ilsley Bank, incorporated by reference to Exhibit 10.29 of the Company's Current Report on Form 10-K, filed on May 3, 2010.
10.12	$1,900,000 Equipment Term Loan Note dated as of April 30, 2010 between Aerosonic Corporation and M&I Marshall & Ilsley Bank, incorporated by reference to Exhibit 10.30 of the Company's Current Report on Form 10-K, filed on May 3, 2010.
10.13	$700,000 Equipment Line of Credit Note dated as of April 30, 2010 between Aerosonic Corporation and M&I Marshall & Ilsley Bank, incorporated by reference to Exhibit 10.31 of the Company's Current Report on Form 10-K, filed on May 3, 2010.
10.14	Security Agreement dated as of April 30, 2010 between the Company and M&I Marshall & Ilsley Bank, incorporated by reference to Exhibit 10.32 of the Company's Current Report on Form 10-K, filed on May 3, 2010.
10.15	Mortgage, Security Agreement and Assignment of Rents dated as of April 30, 2010 between the Company and M&I Marshall & Ilsley Bank, incorporated by reference to Exhibit 10.33 of the Company's Current Report on Form 10-K, filed on May 3, 2010.
10.16	Guaranty Agreement dated as of April 30, 2010 between the Company and M&I Marshall & Ilsley Bank, incorporated by reference to Exhibit 10.35 of the Company's Current Report on Form 10-K, filed on May 3, 2010.

10.17	First Amendment to Loan Agreement dated as of January 10, 2011 between the Company and M&I Marshall & Ilsley Bank.
10.18	Joint Amendment to Loan Agreement and Revolving Line of Credit Note dated as of April 29, 2011 between the Company and M&I Marshall & Ilsley Bank.

21	Subsidiaries of the Registrant, as of January 31, 2011
23.1	Consent of Independent Registered Public Accounting Firm-Mayer Hoffman McCann P.C.
23.2	Consent of Independent Registered Public Accounting Firm- Kirkland, Russ, Murphy & Tapp, P.A.
24	Power of Attorney, incorporated into the Signature Page hereto.
31.1	Section 302 Certifications
31.2	Section 302 Certifications
32.1	Section 906 Certifications
32.2	Section 906 Certifications

* Indicates management contract or compensatory plan

SIGNATURES

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

AEROSONIC CORPORATION
(Registrant)

By: /s/ Douglas J. Hillman Date: May 2, 2011
President and Chief Executive Officer

By: /s/ Kevin J. Purcell Date: May 2, 2011
Chief Financial Officer

Power of Attorney

Each person whose signature appears below authorizes Douglas J. Hillman to execute in the name of each such person who is then an officer or director of the Registrant and to file any amendments to this annual report on Form 10-K necessary or advisable to enable the Registrant to comply with the Securities Exchange Act of 1934, as amended, and any rules, regulations and requirements of the Securities and Exchange Commission in respect thereof, which amendments may make such changes in such report as such attorney-in-fact may deem appropriate.

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

/s/ Douglas J. Hillman Date: May 2, 2011

Douglas J. Hillman,
President, Chief Executive Officer and Director

/s/ P. Mark Perkins

P. Mark Perkins, Date: May 2, 2011
Executive Vice President and Director

/s/ Donald Russell Date: May 2, 2011

Donald Russell, Director

/s/ Thomas E. Whytas, Jr. Date: May 2, 2011
Thomas E. Whytas, Jr., Director

/s/ Roy Robinson Date: May 2, 2011

Roy Robinson, Director

AEROSONIC CORPORATION AND SUBSIDIARIES

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REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders
Aerosonic Corporation and Subsidiaries

We have audited the accompanying consolidated balance sheet of Aerosonic Corporation and Subsidiaries as of January 31, 2011 and the related consolidated statements of operations, stockholders' equity, and cash flows for the year then ended. The Company's management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

We conducted our audit in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform, an audit of its internal control over financial reporting. Our audit included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company's internal control over financial reporting. Accordingly, we express no such opinion. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Aerosonic Corporation and Subsidiaries as of January 31, 2011 and the results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ Mayer Hoffman McCann P.C.

Clearwater, Florida
May 2, 2011

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Board of Directors and Stockholders
Aerosonic Corporation and Subsidiaries

We have audited the accompanying consolidated balance sheet of Aerosonic Corporation and Subsidiaries as of January 31, 2010 and the related consolidated statements of operations, stockholders' equity, and cash flows for the year then ended. The Company's management is responsible for these consolidated financial statements. Our responsibility is to express an opinion on these consolidated financial statements based on our audit.

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In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Aerosonic Corporation and Subsidiaries as of January 31, 2010 and the results of its operations and its cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ Kirkland, Russ, Murphy & Tapp, P.A.

Clearwater, Florida
April 29, 2010

AEROSONIC CORPORATION AND SUBSIDIARIES
Consolidated Balance Sheets
January 31, 2011 and 2010

	2011	2010
ASSETS		
Current assets:		
Cash and cash equivalents	$162,000	$-
Accounts receivable, net	4,653,000	3,421,000
Inventories, net	7,363,000	7,743,000
Prepaid expenses and other current assets, net	2,402,000	1,035,000
Property held for sale	2,062,000	2,062,000
Deferred income taxes	1,617,000	1,613,000
Total current assets	18,259,000	15,874,000
Property, plant and equipment, net	3,518,000	2,917,000
Deferred income taxes	1,198,000	1,831,000
Intangible assets, net	255,000	450,000
Goodwill	366,000	366,000
Other assets, net	82,000	38,000
Total assets	$23,678,000	$21,476,000
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current liabilities:		
Revolving credit facility	$2,313,000	$2,165,000
Current maturities of long-term debt	1,255,000	5,768,000
Accounts payable, trade	2,544,000	2,717,000
Customer advances	-	452,000
Compensation and benefits	780,000	720,000
Income taxes payable	-	67,000
Accrued sales commissions	79,000	42,000
Accrued expenses and other liabilities	2,792,000	1,617,000
Total current liabilities	9,763,000	13,548,000
Long-term debt	4,985,000	-
Unrecognized tax benefits	-	40,000
Deferred income taxes	95,000	168,000
Total liabilities	14,843,000	13,756,000
Commitments and contingencies (Note 16)		
Stockholders' equity:		
Common stock, $.40 par value: authorized 8,000,000 shares; issued 4,180,239 shares and 4,162,289 shares at January 31, 2011 and 2010, respectively; outstanding 3,749,472 shares and 3,731,522 shares at January 31, 2011 and 2010, respectively.	1,672,000	1,665,000
Additional paid-in capital	6,232,000	5,749,000
Retained earnings	4,094,000	3,469,000
Less treasury stock: 430,767 shares at both January 31, 2011 and 2010, at cost	(3,163,000)	(3,163,000)
Total stockholders' equity	8,835,000	7,720,000
Total liabilities and stockholders' equity	$23,678,000	$21,476,000

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

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AEROSONIC CORPORATION AND SUBSIDIARIES
Consolidated Statements of Operations
For the Years Ended January 31, 2011 and 2010

	2011	2010
Sales, net	$29,618,000	$31,136,000
Cost of sales	20,486,000	20,268,000
Gross profit	9,132,000	10,868,000
Selling, general and administrative expenses	7,415,000	6,725,000
Operating income	1,717,000	4,143,000
Other (expense) income:		
Interest expense, net	(745,000)	(602,000)
Gain from casualty loss	235,000	550,000
Other expense	(49,000)	(2,000)
Loss on extinguishment of debt	(78,000)	-
	(637,000)	(54,000)
Income before income taxes	1,080,000	4,089,000
Income tax (expense) benefit	(455,000)	172,000
Net income	$625,000	$4,261,000
Basic income per share	$0.17	$1.15
Diluted income per share	$0.15	$1.09
Weighted average shares outstanding basic	3,739,211	3,689,914
Weighted average shares outstanding fully diluted	4,053,299	3,905,868

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

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AEROSONIC CORPORATION AND SUBSIDIARIES
Consolidated Statements of Stockholders' Equity
For the Years Ended January 31, 2011 and 2010

	Common Stock Shares Outstanding	Common Stock Amount	Additional Paid-In Capital	Retained Earnings (Deficit)	Treasury Stock	Total
Balance at January 31, 2009	3,620,343	$ 1,621,000	$ 5,141,000	$ (792,000)	$ (3,163,000)	$ 2,807,000
Net income	-	-	-	4,261,000	-	4,261,000
Directors' equity compensation	31,179	12,000	48,000	-	-	60,000
Stock issued for short-term note	80,000	32,000	91,000	-	-	123,000
Warrants issued for short-term note	-	-	283,000	-	-	283,000
Stock-based compensation	-	-	186,000	-	-	186,000
Balance at January 31, 2010	3,731,522	1,665,000	5,749,000	3,469,000	(3,163,000)	7,720,000
Net income	-	-	-	625,000	-	625,000
Directors' equity compensation	16,950	7,000	53,000	-	-	60,000
Exercise of stock options	1,000	-	1,000	-	-	1,000
Warrants issued for short-term note	-	-	249,000	-	-	249,000
Stock-based compensation	-	-	180,000	-	-	180,000
Balance at January 31, 2011	3,749,472	$ 1,672,000	$ 6,232,000	$ 4,094,000	$ (3,163,000)	$ 8,835,000

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

AEROSONIC CORPORATION AND SUBSIDIARIES
Consolidated Statements of Cash Flows
For the Years Ended January 31, 2011 and 2010

	2011	2010
Cash flows from operating activities:		
Net income	$625,000	$4,261,000
Adjustments to reconcile net income to net cash provided by (used in) operating activities:		
Depreciation	307,000	271,000
Amortization	229,000	246,000
Accretion on long-term debt	263,000	294,000
Loss on early extinguishment of debt	78,000	-
Provision for bad debt	60,000	224,000
Provision for obsolete and slow-moving inventory	399,000	230,000
Provision for warranty	23,000	70,000
Provision for contract losses	1,227,000	273,000
Stock-based compensation	241,000	246,000
Gain from casualty	(235,000)	(550,000)
Proceeds from insurance	235,000	550,000
Provision for deferred income taxes	556,000	(14,000)
Unrecognized tax benefits	(40,000)	(214,000)
Changes in assets and liabilities:		
Accounts receivable, net	(1,292,000)	(1,827,000)
Inventories, net	(19,000)	89,000
Prepaid expenses and other current assets, net	(1,367,000)	(901,000)
Other assets	(109,000)	225,000
Accounts payable, trade	(173,000)	(170,000)
Customer advances	(452,000)	(2,817,000)
Compensation and benefits	60,000	112,000
Income tax payable	(67,000)	67,000
Accrued expenses and other liabilities	(38,000)	(697,000)
Net cash provided by (used in) operating activities	511,000	(32,000)
Cash flows from investing activities:		
Capital expenditures	(908,000)	(1,991,000)
Net cash used in investing activities	(908,000)	(1,991,000)
Cash flows from financing activities:		
Net increase in revolving credit facility	148,000	1,618,000
Principal payments on notes payable	(800,000)	-
Proceeds from issuance of notes payable	600,000	800,000
Principal payments on long-term debt	(5,501,000)	(395,000)
Proceeds from refinancing of long-term debt	6,112,000	-
Net cash provided by financing activities	559,000	2,023,000
Change in cash and cash equivalents	162,000	-
Cash and cash equivalents, beginning of year	-	-
Cash and cash equivalents, end of year	$162,000	$-

Supplemental disclosures of cash flow information:		
Net cash paid during the year for:		
Interest	$467,000	$306,000
Income taxes	$67,000	$-
Non-cash financing and other transactions:		
Common stock issued	$-	$123,000
Common stock warrants issued	$249,000	$283,000
Accrued environmental costs related to property held for sale	$-	$350,000

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

AEROSONIC CORPORATION AND SUBSIDIARIES
Notes to the Consolidated Financial Statements

1. Description of Business, Basis of Presentation and Summary of Significant Accounting Policies

Description of Business

Aerosonic Corporation ("Aerosonic") and its wholly-owned subsidiaries, Avionics Specialties, Inc. and OP Technologies, Inc. (collectively referred to herein as the "Company") manufacture and sell aircraft instrumentation and sensors systems, including integrated cockpit displays, digital and mechanical standby displays, sensors and probes. Our customers include government and commercial users located worldwide. The Company's production facilities are located in Florida and Virginia.

Financial Condition and Management's Plans

On April 30, 2010, the Company refinanced its Wachovia Bank, N.A. ("Wachovia") debt totaling $7,481,000 with new debt facilities from M&I Marshall & Ilsley Bank ("M&I Bank") with a maximum credit availability of $10,100,000. On May 1, 2010, the Wachovia debt was repaid with proceeds available under the M&I Bank facilities.

Prior to the debt refinancing, and as of January 31, 2010, the Company was not in compliance with certain debt covenants with Wachovia Bank, N.A.. As a result, the Company's total debt with Wachovia, which was $7,245,000 at January 31, 2010, was subject to acceleration and was classified as current on the consolidated balance sheet at January 31, 2010. The Company received a written waiver from Wachovia through June 30, 2010 relating to its covenant for noncompliance.

For the period measured as of January 31, 2011, the Company did not comply with the Funded Debt to EBITDA covenant in its credit facility with M&I Bank.

Basis of Presentation

The Company prepares its consolidated financial statements in conformity with accounting principles generally accepted in the United States of America ("U.S. GAAP"). These principles require management to make estimates and judgments that affect reported and contingent amounts of assets, liabilities, revenues and expenses, including such items as (i) inventory, restructuring and environmental costs, (ii) other miscellaneous accruals and, (iii) valuation allowances for accounts receivable, inventory and deferred tax assets. Actual results may differ from these estimates under different assumptions or conditions, and such differences could be material.

The accompanying consolidated financial statements include the accounts of the Company. All significant intercompany balances and transactions have been eliminated in consolidation. The Company operates on a fiscal year that ends on January 31, consisting of four quarters, each of the first three quarters ending on the Friday of each successive 13 week period. Accordingly, all references to the third quarter mean the third quarter ended on the 39th Friday of the fiscal year. For example, references to the third quarter of fiscal year 2011 mean the quarter ended October 29, 2010.

Reclassifications

Certain amounts in the fiscal year 2010 financial statements have been reclassified to conform to the fiscal year 2011 presentation. Such reclassifications had no effect on net loss or stockholders' equity as previously reported.

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Accounts Receivable, Allowance for Doubtful Accounts and Credit Losses

The Company continuously evaluates its customers and provides specific reserves for anticipated credit losses as soon as collection becomes compromised. Measurement of such losses requires consideration of historical loss experience, including the need to adjust for current conditions, and judgments about the probable effects of relevant observable data, including present economic conditions such as delinquency rates and financial health of specific customers.

Inventories

The Company values inventory at the lower of cost using a method that approximates the first-in, first-out method (“FIFO”), or net realizable value. The reserve for obsolete and slow moving inventory is based upon reviews of inventory quantities on hand, usage and sales history.

During production, the Company uses standards to estimate product costs. These standards are reviewed and updated periodically by management and approximate costing under the FIFO method.

Work In Process Inventories

The Company employs certain methods to estimate the value of work in process inventories for financial reporting purposes. The Company’s practice has been to conduct cycle counts of inventory throughout the year. Generally, for items that are in process at the end of a fiscal year, the Company will make an estimate during the cycle counting process regarding the percentage of completion of such items in order to accurately reflect costs incurred to date on the production of the items that are still in process. These estimates are affected by the nature of the operation at which the items are located at the time a physical inventory is conducted, and are subject to judgment. This practice was employed for fiscal years 2011 and 2010.

Manufacturing Overhead Cost Application

The Company establishes its inventoriable cost of manufacturing overhead by calculating its overhead costs as a percentage of direct labor and applying that percentage to direct labor that has been charged to inventory on a twelve month rolling average basis. This application percentage is reviewed and adjusted annually.

Property Held for Sale

Property held for sale is reported at the lower of its carrying amount or fair value less cost to sell. Depreciation on property held for sale is discontinued at the time the criteria, established by U.S. GAAP, are met. The Earlysville, Virginia property is presently held for sale. The property consists of a 53,000 square foot manufacturing facility on approximately 12 acres of land. In preparation for the sale of the Earlysville, Virginia facility, the Company engaged an environmental consulting firm to survey the property for any possible soil or groundwater contamination. This survey revealed impacts to both shallow soils and groundwater that may have resulted from the accidental loss of solvents by a former owner of the property. As a result, of the initial and subsequent surveys, remaining contamination treatment costs are estimated at $808,000. The Company has capitalized these contamination treatment costs as an increase to property held for sale, net, since such costs will be incurred in preparation for the sale of the Earlysville, Virginia facility and will not result in a carrying value in excess of the estimated fair value less cost to sell. Costs incurred during the year ended January 31, 2011 totaled $124,000 and costs incurred during the year ended January 31, 2010 totaled $153,000.

Property, Plant and Equipment

Property, plant and equipment are stated at cost less accumulated depreciation. Depreciation is calculated on the straight-line method over the estimated useful lives of the assets. Upon disposition, the cost and related accumulated depreciation are removed from the accounts and any related gain or loss is included in earnings. Expenditures for repairs and improvements that significantly add to the productive capacity or extend the useful life of an asset are capitalized. Repair and maintenance charges are expensed as incurred.

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The useful lives of property, plant and equipment for purposes of computing depreciation are:

Land improvements	15-20 Years
Buildings and improvements	25-40 Years
Machinery and equipment	3-15 Years
Patterns, dies and tools	3-5 Years
Furniture and fixtures	5-10 Years

Goodwill and Intangible Assets

The carrying value of goodwill is reviewed at least annually for impairment and will be reviewed more frequently if current events and circumstances indicate a possible impairment. An impairment loss is charged to expense in the period identified. As current events and circumstances warrant, the Company examines the carrying value of its intangible assets with finite lives, such as capitalized software and development costs, purchased intangibles, and other long-lived assets, to determine whether there are any impairment losses. If indicators of impairment are present and future cash flows are not expected to be sufficient to recover the asset’s carrying amount, an impairment loss is charged to expense in the period identified. Factors that may cause impairment include negative industry or economic trends or significant underperformance relative to historical or projected future operating results.

Other Assets

Capitalized loan fees are recorded at cost less accumulated amortization. The costs are determined at the time the loan transactions are closed and are amortized over the life of the loan using a method which approximates the effective interest method.

Income Taxes

The Company and its includable subsidiaries file a consolidated U.S. federal income tax return in accordance with the provisions of the Internal Revenue Code of 1986, as amended.

The Company’s accounting for income taxes represents management’s best estimate of various events and transactions.

The Company records provisions dealing with uncertain tax positions as required in ASC740.

Deferred tax assets and liabilities resulting from temporary differences between the financial reporting and tax bases of assets and liabilities are measured at the balance sheet date using enacted tax rates expected to apply to taxable income in the years the temporary differences are expected to reverse.

The realization of deferred tax assets depends upon the existence of sufficient taxable income within the carryback or carryforward periods under the tax law in the applicable tax jurisdiction. Valuation allowances are established when management determines, based on available information, that it is more likely than not that deferred income tax assets will not be realized. Significant judgment is required in determining whether valuation allowances should be established as well as the amount of such allowances. When making such determination, consideration is given to, among other things, the following:

- future taxable income exclusive of reversing temporary differences and carryforwards;

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- future reversals of existing taxable temporary differences;
- taxable income in prior carryback years; and
- tax planning strategies.

The Company classifies tax related interest as interest expense and tax related penalties as a component of income taxes.

Revenue Recognition

The Company generally recognizes revenue from sales of its products when the following have occurred: evidence of a sale arrangement exists; delivery or shipment has occurred or services have been rendered; the price to the buyer is fixed or determinable; and collectability is reasonably assured.

For fixed-price contracts, the Company may recognize revenue on a Units of Accounting basis. The Units of Accounting method requires the Company to evaluate all deliverables in an arrangement to determine whether they represent separate units of accounting. The Company makes that determination at the inception of the arrangement and as each item in the arrangement is delivered. In an arrangement with multiple deliverables, the delivered item(s) shall be considered a separate unit of accounting if (a) the delivered item(s) have value to the customer on a standalone basis, (b) there is objective and reliable evidence of the fair value of the undelivered item(s) and (c) if the arrangement includes a general right of return relative to the delivered item(s), delivery or performance of the undelivered item(s) is considered probable and substantially in the control of the vendor.

The Company may also recognize its revenue under the completed contract method.

For long-term, fixed-price contracts meeting certain criteria, the Company may elect to follow the percentage-of-completion method of accounting for revenue recognition. Under this method, contract revenue is computed as that percentage of estimated total revenue that costs incurred to date bear to total estimated costs, after giving effect to the most recent estimates of costs to complete. From time to time, the Company will record costs and estimated profits in excess of billings for a contract. Revisions in costs and revenue estimates are reflected in the period in which the revisions are determined. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are determined without regard to the percentage-of-completion.

Occasionally the Company enters into research and development contracts with customers. When the contracts provide for milestone or other interim payments, the Company will recognize revenue either under the Milestone method or the Units of Accounting method. Contracts in process at January 31, 2011, presented as contracts A, B and C, are being accounted for under the Milestone method. The Milestone method requires the Company to deem all milestone payments within each contract as either substantive or non-substantive. That conclusion is determined based upon a thorough review of each contract and the Company's deliverables committed to in each contract. For substantive milestones, the Company concludes that upon achievement of each milestone, the amount of the corresponding defined payment is commensurate with the effort required to achieve such milestone or the value of the delivered item. The payment associated with each milestone relates solely to past performance and is deemed reasonable upon consideration of the deliverables and the payment terms within the contract. For non-substantive milestones, including advance payments, the recognition of such payments are pro-rated to the substantive milestones. Milestones may include, for example, the successful completion of design review or technical review, the submission and acceptance of technical drawings, delivery of hardware, software, spares, test equipment or regulatory agency certifications. During the fiscal year ended January 31, 2011, revenue recognized through the achievement of two substantive milestones (#2 and #3) within contract A, amounted to $108,000.

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Milestone considerations for contracts in process at January 31, 2011 include:

Contract A	Milestone consideration
Milestone 1 (Non-Substantive)	218,000
Milestone 2 (Substantive)	32,000
Milestone 3 (Substantive)	33,000
Milestone 4 (Substantive)	65,000
Milestone 5 (Substantive)	65,000
Milestone 6 (Substantive)	65,000
Milestone 7 (Substantive)	66,000
	544,000

Contract B	Milestone consideration
Milestone 1 (Substantive)	100,000
Milestone 2 (Substantive)	29,000
Milestone 3 (Substantive)	100,000
Milestone 4 (Substantive)	41,000
Milestone 5 (Substantive)	10,000
Milestone 6 (Substantive)	115,000
Milestone 7 (Substantive)	38,000
Milestone 8 (Substantive)	73,000
Milestone 9 (Substantive)	51,000
Milestone 10 (Substantive)	82,000
Milestone 11 (Substantive)	23,000
	662,000

Contract C	Milestone consideration
Milestone 1 (Substantive)	2,000
Milestone 2 (Substantive)	24,000
Milestone 3 (Substantive)	47,000
Milestone 4 (Substantive)	19,000
Milestone 5 (Substantive)	92,000
Milestone 6 (Substantive)	38,000
Milestone 7 (Substantive)	38,000
Milestone 8 (Substantive)	81,000
Milestone 9 (Substantive)	28,000
Milestone 10 (Substantive)	17,000
Milestone 11 (Substantive)	6,000
Milestone 12 (Substantive)	37,000
Milestone 13 (Substantive)	121,000
Milestone 14 (Substantive)	550,000

When there is no milestone or other interim payments, revenue is generally recognized at completion.

As a general matter, the terms specified in customer purchase orders determine whether the Company or the customer bears the obligation for payment of freight charges. While customers pay for freight in most transactions, the

Company does occasionally pay freight charges on behalf of customers and may bill all or a portion to customers.

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Research and Development

R&D costs that are not associated with specific customer contract requirements are included in selling, general and administrative expenses and approximated $1,500,000 and $559,000 for the years ended January 31, 2011 and 2010, respectively. R&D costs associated with specific products, as part of one of the Company's product development programs, are presented as a deferred charge in prepaid expenses and other current assets, net and approximated $2,287,000 and $864,000 for the year ended January 31, 2011 and January 31, 2010, respectively. See Note 11 for further discussion of the Company's product development programs.

Environmental Expenditures

The Company assesses its property held for sale, along with any property that is being taken out of its initially intended use, for the presence of hazardous or toxic substances that would result in an environmental liability.

Liabilities for environmental remediation costs not related to retirements of tangible long-lived assets, and arising from claims, assessments, litigation, fines, and penalties and other sources, are recorded when it is probable that a liability has been incurred and the amount of the assessment and/or remediation can be reasonably estimated.

Legal costs incurred in connection with environmental remediation are expensed as incurred. Recoveries of environmental remediation costs from third parties, which are probable of realization, are separately recorded as assets, and are not offset against the related environmental liability, in accordance with U.S. GAAP.

Treasury Stock

The Company accounts for the acquisition of treasury shares at cost. The Company has not reissued acquired shares.

Stock-Based Compensation

U.S. GAAP requires that all stock-based compensation be recognized as an expense in the financial statements and that such cost be measured at the fair value of the award. Under this method, in addition to reflecting compensation for new share-based awards, expense is also recognized to reflect the remaining service period of awards that had been included in pro-forma disclosure in prior periods. U.S. GAAP requires that the cost of all share-based transactions be measured at fair value and recognized over the period during which a grantee is required to provide goods or services in exchange for the award. Although the terms of the Company's share-based plans do not accelerate vesting upon retirement, or the attainment of retirement eligibility, the requisite service period subsequent to attaining such eligibility is considered non-substantive. Accordingly, the Company recognizes compensation expense related to share-based awards over the shorter of the requisite service period or the period to attainment of retirement eligibility. U.S. GAAP also requires an estimation of future forfeitures of share-based awards to be incorporated into the determination of compensation expense when recognizing expense over the requisite service period.

The Company issued 171,500 stock options to employees during fiscal year 2010. The Company did not issue stock options to employees during fiscal year 2011. The weighted average per share fair value of options granted was determined using the Black-Scholes option-pricing model with the following assumptions (See Note 13 for further discussion of stock-based compensation):

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	2010	
Volatility	63% - 75	%
Risk-free interest rate	0.36% - 0.72	%
Expected life in years	10.00	
Dividend yield	0	%

Income per Share

Basic income per share is computed using the weighted average number of shares of common stock outstanding. Diluted income per share is computed by dividing net income available to common stockholders by the weighted average number of shares of common stock outstanding for the period, adjusted for the dilutive effect of potential common stock, using the treasury stock method.

Concentrations of Credit Risk

Financial instruments which potentially subject the Company to concentrations of credit risk consist principally of cash and receivables. As of January 31, 2011 and 2010, substantially all of the Company's cash balances were deposited with financial institutions determined by management to be of high credit quality. During the normal course of business, the Company extends credit, without collateral, to customers conducting business in the aerospace industry worldwide.

Exchange Rate Fluctuation

The Company conducts a limited amount of business in transactions that are denominated in foreign currencies. The Company employs a method of matching accounts receivable denominated in foreign currencies with accounts payable denominated in foreign currencies to mitigate this risk. These amounts have been insignificant.

Financial Instruments

U.S. GAAP requires disclosure of the fair value of certain financial instruments. Cash, accounts receivable, short-term borrowings and certain accrued liabilities are included in the consolidated financial statements at amounts which approximate fair value because of the short term nature of these instruments. The carrying amount of long-term debt at January 31, 2011 and 2010 approximates fair value as these instruments have adjustable rates which change in accordance with the market.

Adoption of New Accounting Pronouncements

In April 2011, the FASB issued new accounting guidance for purposes of measuring the impairment of receivables and evaluating whether a troubled debt restructuring has occurred. An entity should disclose the total amount of receivables and the allowance for credit losses as of the end of the period of adoption related to those receivables that are newly considered impaired under Section 310-10-35 for which impairment was previously measured under Subtopic 450-20, Contingencies–Loss Contingencies. Currently, this guidance is anticipated to be effective for interim and annual periods ending after June 15, 2011. The adoption of this guidance is not expected to have an impact on our consolidated financial position, results of operations, cash flows, or disclosures.

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In December 2010, the FASB issued ASU 2010-28, Intangibles – Goodwill and Other (Topic 350): When to Perform Step 2 of the Goodwill Impairment Test for Reporting Units with Zero or Negative Carrying Amounts . The ASU does not prescribe a specific method of calculating the carrying value of a reporting unit in the performance of step 1 of the goodwill impairment test (i.e. equity-value-based method or enterprise-value-based method). However, it requires entities with a zero or negative carrying value to assess, considering qualitative factors such as those used to determine whether a triggering event would require an interim goodwill impairment test (listed in ASC 350-20-35-30, Intangibles – Goodwill and Other – Subsequent Measurement), whether it is more likely than not that a goodwill impairment exists and perform step 2 of the goodwill impairment test if so concluded. ASU 2010-28 is effective for the Company beginning January 1, 2011 and early adoption is not permitted. The Company does not expect the adoption of ASU 2010-28 to have a material impact on its consolidated financial position or results of operations.

In April 2010, the FASB issued new authoritative guidance surrounding revenue recognition, specifically addressing the criteria for recognizing revenue tied to research and development efforts. The guidance adds the milestone method to the list of acceptable methods of revenue recognition when accounting for multiple element arrangements within research and development efforts. The guidance is effective for milestones achieved in fiscal years beginning on or after June 15, 2010, unless early adoption is elected. The Company adopted the guidance beginning the quarter ended July 30, 2010, which required retrospective application from the beginning of the fiscal year. The adoption of this guidance did not have a material impact on the Company's financial statements.

2. Acquisition

On August 21, 2007, the Company purchased 100% of the outstanding stock of OP Tech from Optimization Technologies, Inc., an Oregon corporation (the "Seller"). In connection with the acquisition, the Company, OP Tech, and the Seller, along with certain holders of the Seller's capital stock, entered into a Share Purchase Agreement (the "SPA"), whereby the Company paid $1,000,000 to the Seller. The SPA also provides for the Seller to additionally receive: (i) up to $80,000 payable in Company common stock once the Company obtains certain federal certifications for OP Tech's products, subject to Seller's delivery of a duly executed subscription agreement, which provides for the Seller's receipt of such stock, and a duly executed lock-up agreement, which prohibits a transfer by Seller for two years from the date of issuance of such stock and (ii) up to $1,000,000 if certain sales targets ($10,000,000 or greater) are met with respect to OP Tech's products within three years of the Closing Date. The aforementioned contingencies were not met as of January 31, 2011.

3. Consolidation Plan and Restructuring Costs

On March 9, 2007, the Company announced the consolidation of the manufacturing functions of its Earlysville, Virginia, operation into its Clearwater, Florida facility. This consolidation was a continuation of the Company's actions to be more responsive to customers' demands. Avionics' existing support and repair/overhaul activities have remained in the Earlysville area and have relocated to a new facility more appropriately sized for the Company's streamlined structure.

In accordance with U.S. GAAP, the Company, for the years ended January 31, 2011 and 2010, recognized a total of approximately $154,000 and $262,000, respectively, in restructuring costs including severance, benefits, facilities and other costs, which are included in selling, general and administrative expenses. See Note 19 for further discussion on the consolidation of the Virginia operation into the Florida facility.

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4. Accounts Receivable

Accounts receivable at January 31, 2011 and 2010 consisted of the following:

	2011	2010
Accounts receivable, trade	$ 5,261,000	$ 4,074,000
Less: allowance for doubtful accounts	(608,000)	(653,000)
Accounts receivable, net	$ 4,653,000	$ 3,421,000

The Company's allowance for doubtful accounts activity for the years ended January 31, 2011 and 2010 was as follows:

	2011	2010
Beginning balance	$ 653,000	$ 551,000
Amounts written off	(105,000)	(16,000)
Recoveries of amounts provided for	-	(106,000)
Amounts provided for	60,000	224,000
Ending balance	$ 608,000	$ 653,000

5. Prepaid Expenses and Other Current Assets

Included in, and making up the majority of, prepaid expenses and other current assets was $2,287,000 and $864,000 of deferred charges related to several current engineering contracts as of January 31, 2011 and January 31, 2010, respectively. The Company has been retained for the development of customer specific engineering projects. All the contracts are short-term in nature and not expected to extend beyond twelve months. As of January 31, 2011, the deferred charges consist of $1,951,000 of internal engineering labor, including overhead, and $336,000 of external engineering contract labor. As of January 31, 2010, the deferred charges consist of $546,000 of internal engineering labor, including overhead, and $318,000 of external engineering contract labor. The deferred charges are offset by interim payments from customers of $223,000 and $218,000 as of January 31, 2011 and January 31, 2010, respectively. Related to the deferred charges are accrued contract losses of $1,500,000 and $273,000 as of January 31, 2011 and January 31, 2010, respectively, which are included in accrued expenses and other liabilities.

Prepaid expenses and other current assets, net consisted of the following:

	2011	2010
Deferred charges on engineering contracts, net	$ 2,064,000	$ 646,000
Prepaid insurance expenses	232,000	133,000
Other prepaid expenses	106,000	256,000
Prepaid expenses and other current assets, net	$ 2,402,000	$ 1,035,000

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6. Inventories

Inventories at January 31, 2011 and 2010 consisted of the following:

	2011	2010
Raw materials	$ 7,498,000	$ 6,622,000
Work in process	1,906,000	2,758,000
Finished goods	383,000	388,000
Reserve for obsolete and slow moving inventory	(2,424,000)	(2,025,000)
Inventories, net	$ 7,363,000	$ 7,743,000

The Company's reserve for obsolete and slow moving inventory activity for the years ended January 31, 2011 and 2010 was as follows:

	2011	2010
Beginning balance	$ 2,025,000	$ 1,795,000
Amounts charged to operations	399,000	230,000
Ending balance	$ 2,424,000	$ 2,025,000

7. Property, Plant and Equipment

Property, plant and equipment at January 31, 2011 and 2010 consisted of the following:

	2011	2010
Land and improvements	$ 173,000	$ 173,000
Building and improvements	2,502,000	2,384,000
Machinery and equipment	5,038,000	4,404,000
Patterns, dies and tools	578,000	578,000
Furniture and fixtures	1,576,000	1,433,000
Construction in progress	1,495,000	1,482,000
	11,362,000	10,454,000
Less: accumulated depreciation	(7,844,000)	(7,537,000)
Property, plant and equipment, net	$ 3,518,000	$ 2,917,000

Depreciation expense was $307,000 and $271,000 for the years ended January 31, 2011 and 2010, respectively. Certain components of property, plant and equipment are pledged as collateral for debt obligations. See Note 12 for further discussion of collateralized property, plant and equipment.

Gain from Casualty Loss

On August 8, 2008, as a result of a fire at its Clearwater, Florida facility, the Company suffered a casualty loss of one of its production buildings that was destroyed. The building was primarily used for general storage and product testing, probes and sensor manufacturing, as well as for shipping and receiving. While the Company's main operating facility was not damaged by the fire, production was affected through loss of staged incoming raw materials inventory and outgoing finished goods. During the third quarter of fiscal year 2009 and the first quarter and second quarter of fiscal year 2010, the Company's insurer extended advances to the Company totaling $2,600,000, $500,000 and

$50,000, respectively. Portions of the insurance proceeds were applied towards replacement of raw materials inventory and production assets lost in the fire, as well as retooling and reengineering of production equipment in the unaffected main operating facility that were necessary to accommodate the loss of production activities within the destroyed building.

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The net book value of inventory and fixed assets destroyed in the fire was $1,009,000 and $647,000, respectively, resulting in a gain from casualty loss of $550,000 and $944,000 for the years ended January 31, 2010 and 2009, respectively.

Additionally, the Company's insurance coverage provided for business interruption recovery. The Company engaged the services of outside legal counsel and a cost recovery specialist to assist with this recovery. Professional fees associated with these services were $200,000 for the year ended January 31, 2010, which is included in selling, general and administrative expenses. The Company has also incurred additional costs for travel, rent and clean-up associated with the fire, which totaled $89,000 for the year ended January 31, 2010, and are included in cost of sales and selling, general and administrative expenses.

On February 4, 2010, the Company settled its claims against its insurance carrier and insurance broker in consideration of payment to the Company of $235,000. The settlement released both defendants from all future claims relating to the fire loss on August 8, 2008 at the Company's Clearwater, Florida facility.

8. Intangible Assets

Intangible assets as of January 31, 2011 and 2010 consisted of the following:

	Useful Lives		2011		2010
Intangible assets subject to amortization:					
Acquired product prototype	5	$	730,000	$	730,000
Non-compete agreeements	3		175,000		175,000
Acquired customer base	5		75,000		75,000
Total intangible assets subject to amortization			980,000		980,000
Accumulated amortization			(725,000)		(530,000)
Net		$	255,000	$	450,000
Intangible assets with indefinite lives:					
Goodwill		$	366,000	$	366,000

Amortization expense related to intangible assets for the years ended January 31, 2011 and 2010 was $195,000 and $219,000, respectively. Amortization expense for the remaining useful lives of the intangible assets is $161,000 and $94,000 for the years ending January 31, 2012 and 2013, respectively.

Amortization expense related to capitalized debt issuance costs for both years ended January 31, 2011 and 2010 was $34,000 and $27,000, respectively.

Amortization expense related to intangible assets and capitalized debt issuance costs is included in selling, general and administrative expenses. Capitalized debt issuance costs are included in other assets.

9. Notes Payable

On May 14, 2009, the Company entered into three separate unsecured notes payable, herein referred to as "Notes Payable", with three separate private lenders, Bruce J. Stone, Redmond Family Investments, LLLP and Martin L. Schaffel, herein referred to as "the Investors", each containing a drawdown provision allowing the Company to borrow up to an aggregate of $2,000,000. The loan agreements initially provided for the issuance of warrants with an exercise price of $0.64 per warrant issued at the rate of one warrant for every four dollars loaned to the Company and common shares at the rate of one share for every ten dollars loaned to the Company. Additionally, any amounts borrowed are subject to 14% interest per annum, payable monthly.

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On May 21, 2009, the Company borrowed an aggregate principal amount of $800,000 based upon the cash drawdown provision of each of the three unsecured loan agreements. The 200,000 warrants issued to the Investors pursuant to the $800,000 drawdown are exercisable at any time during the period after May 21, 2010 and before the warrant expiration date of April 10, 2015. The Company also issued 80,000 common shares in connection with the $800,000 cash. The aggregate amount borrowed of $800,000 was initially payable in full under each of the three Notes Payable on or before April 10, 2010.

On February 19, 2010, the Company borrowed an additional $600,000 from the Investors under the three unsecured loan agreements entered into on May 14, 2009 and also entered into amendments to each of the three unsecured loan agreements with the Investors. The note modifications (a) extended the maturity date of the subordinated notes for a period of one year from April 10, 2010 to April 10, 2011, (b) removed Aerosonic's obligation to issue shares of its common stock upon each cash drawdown made on or after February 19, 2010, (c) revised the ratio of common shares underlying warrants issuable per each $1.00 of principal amount borrowed from ".25 shares per $1.00 of principal amount" to ".20 shares per $1.00 of principal amount" with respect to cash draw downs made on or after February 19, 2010 and (d) deleted certain negative covenants relating to the issuance of securities. The warrant modifications (a) extended the expiration date of any warrants issued prior to February 19, 2010 for a period of five years from April 10, 2015 to April 10, 2020, (b) extended the expiration date of any warrants issued on or after February 19, 2010 from April 10, 2015 to the sixth anniversary date of the issuance of the warrant certificate and (c) revised the purchase price for any warrants issued on or after February 19, 2010 from $0.64 per share to a price equal to 50% of the volume weighted average of the selling price of the Company's common stock on February 12, 2010 and for the 19 trading days prior to February 12, 2010, or $1.98 per share. The 120,000 warrants issued to the Investors pursuant to the additional $600,000 loan are exercisable at any time before the expiration date of February 19, 2016.

On October 13, 2010, the Company repaid $700,000 of the outstanding balance of the Notes Payable, with each Investor receiving a pro-rata portion of the aggregate repayment amount based on the Investors' balance on that date.

On December 31, 2010, the Company repaid an additional $100,000 of the outstanding balances of the Notes Payable, with each Investor receiving a pro-rata portion of the aggregate repayment amount based on the Investors' balance on that date.

The warrants and common shares issued under the unsecured loan agreements described above are recorded as a separate component of interest and are being accreted into the loan balances over the term of the loans. For the years ended January 31 2011 and 2010, the Company recognized accretion of $263,000 and $294,000, respectively, presented as additional interest expense. In addition, as a result of the early repayments to the Investors in October and December of 2010, the Company recognized accelerated interest accretion expense in the amount of $78,000, for the year ended January 31, 2011, which is reported as loss on extinguishment of debt.

10. Customer Advances

In September 2008, the Company began receiving advances from certain customers for unbilled product orders. Such advances were used to fund production, thus alleviating some of the Company's liquidity challenges resulting from the August 2008 fire. The total of such advances approximated $4,965,000. These advances represent non-interest bearing prepayments and are recognized in revenue at the time of product shipments. See Note 7 for further discussion on the August 2008 casualty loss.

During fiscal year 2011, the Company fulfilled its repayment obligation by completing delivery of the Company's products in full satisfaction of the advances.

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11. Accrued Expenses and Other Liabilities

Accrued expenses and other liabilities at January 31, 2011 and 2010 consisted of the following:

		2011		2010
Environmental liability (see Note 16)	$	808,000	$	932,000
Contract loss provision		1,500,000		273,000
Warranty liability		144,000		167,000
Other		340,000		245,000
Accrued expenses and other liabilities	$	2,792,000	$	1,617,000

Contract Loss Provision

As of January 31, 2011 and January 31, 2010, the Company recognized contract loss provisions of $1,500,000 and $273,000, respectively, associated with the outsourcing of the Company's engineering personnel and resources to several fixed fee research and development projects. As of January 31, 2011, remaining revenues contracted to the projects are fixed at $1,071,000. As of January 31, 2011, the Company estimates total costs of the projects to approximate $2,571,000.

Warranty Liability

The Company has established a liability for warranty claims based on historical experience, which has not been significant. The Company's warranty activity for the years ended January 31, 2011 and 2010 was as follows:

		2011		2010
Beginning balance	$	167,000	$	167,000
Cost incurred		(46,000)		(70,000)
Provision for warranty cost		23,000		70,000
Ending balance	$	144,000	$	167,000

Product Development Programs

During fiscal year 2003, the Company secured a long-term fixed-price contract for the development of instrumentation for the Joint Strike Fighter ("JSF") product development program, a customer-funded program that concluded the majority of its developmental activity during fiscal year 2008 and generated total project revenues of approximately $15,368,000.

Costs and estimated earnings on this contract were as follows:

		2010
Costs incurred to date	$	18,437,000
Estimated losses		(3,165,000)
		15,272,000
Less: billings to date		(15,272,000)
Billings in excess of costs less estimated losses as of January 31	$	-

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During fiscal year 2010, the Company completed its obligation associated with the JSF product development program by completing and shipping all required prototype instruments. As a result, the Company was released from further obligation associated with the JSF program.

12. Long-term Debt and Revolving Credit Facility

On April 30, 2010, the Company entered into a Loan Agreement (the "Loan Agreement") with M&I Bank with a maximum amount of credit facilities (the "Credit Facility") available to the Company of $10,100,000. The Loan Agreement provides for (a) a $4,000,000 revolving line of credit (the "Revolving Credit Line Note"), (b) a $3,500,000 first real estate mortgage loan (the "Real Estate Mortgage Note"), (c) a $1,900,000 term loan (the "Equipment Term Note" and together with the Real Estate Mortgage Note, the "Bank Notes"), and (d) a $700,000 equipment line of credit (the "Equipment Credit Line Note" and together with the Revolving Credit Line Note, the "Credit Line Notes"). The proceeds from the Credit Facility were used, in part, to fully satisfy the outstanding debt and fees with Wachovia of $7,521,830. The available funds received and financing available under the Loan Agreement will be used for new product development, working capital and capital expenditure needs.

The Credit Facility is secured by substantially all assets of the Company. Details of the Credit Facility are as follows:

- The Revolving Credit Line Note, which supports a $4,000,000 revolving line of credit, has a 364 day term and provides a line of credit in an amount equal to the lesser of (a) the Revolving Credit Limit of $4,000,000; or (b) a Borrowing Base determined based on eligible accounts receivable and inventory. The interest rate on the Revolving Credit Line Note is one month LIBOR plus 300 basis points with a 4% floor. Interest is paid monthly. The interest rate on the M&I Bank Revolving Credit Line Note was one-month LIBOR (which was 0.26% at January 31, 2011), plus 300 basis points with a 4% floor. Available borrowings on the Revolving Credit Line Note at January 31, 2011 were $1,687,000.
- The Real Estate Mortgage Note, which supports a $3,500,000 first real estate mortgage loan, has a three year term, a 15 year amortization period, and the interest rate is one month LIBOR plus 340 basis points with a 4% floor. Interest and principal are paid monthly. The proceeds of the Real Estate Mortgage Note were used for refinancing an existing loan relating to the Clearwater, Florida property and for working capital and capital expenditure needs.
- The Equipment Term Note, which supports a $1,900,000 term loan, has a three year term, a five year amortization period, and the interest rate is one month LIBOR plus 340 basis points with a 4% floor. Interest and principal are paid monthly. The proceeds of the Equipment Term Note were used for refinancing an existing loan relating to the Earlysville, Virginia property and for working capital and capital expenditure needs. The Company must pay any proceeds from the sale of the Earlysville, Virginia property to M&I Bank to be applied as a principal payment under the Equipment Term Note.
- The Equipment Credit Line Note, which supports a $700,000 equipment line of credit, has a three year term, a five year amortization period, and the interest rate is one month LIBOR plus 325 basis points with a 4% floor. Interest is paid monthly. Principal is to be paid monthly beginning June 2011. Proceeds are used to purchase equipment for use in the Company's business.

The Credit Facility contains certain financial and other restrictive covenants, including the requirement to maintain: (i) on a consolidated basis, Total Stockholders' Equity, defined as the value of total assets less total liabilities, equal to at least $7,419,000, which amount shall increase on a quarterly basis in an amount equal to ninety percent (90%) of the Company's net income (calculated on a consolidated basis) for such quarter; (ii) on a consolidated basis, a ratio of Funded Debt, defined as all outstanding liabilities for borrowed money and other interest-bearing liabilities, including current and long term debt, less the non-current portion of Subordinated Liabilities, defined as liabilities subordinated to the Company's obligations to the lender in a manner acceptable to the lender in its sole discretion, to EBITDA not exceeding 3.0:1.0; and (iii) on a consolidated basis, a Fixed Charge Coverage Ratio, defined as the ratio of (a) the sum of EBITDA plus lease expense and rent expense, minus income tax, minus dividends, withdrawals, and other distributions, to (b) the sum of cash interest expense, lease expense, rent expense, scheduled principal amortization actually paid to the lender during the measuring period (excluding any principal payments under the Revolving Credit Line Note and the Investors' Notes Payable), and scheduled payments on capitalized lease obligations during the measuring period, of at least 1.20:1.0. These covenant amounts are calculated at the end of each quarterly reporting period for which the lender require financial statements.

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On October 12, 2010, the Company borrowed an additional $700,000 against the Equipment Credit Line Note which replenished cash used by the Company to purchase and construct equipment over the 12 months before that date. The borrowed amount was used to accelerate repayment of the Investors' Notes Payable.

For the period measured as of January 31, 2011, the Company did not comply with the Funded Debt to EBITDA covenant in the Credit Facility.

Prior to the refinancing with M&I Bank on April 30, 2010, the Company's credit facilities were with Wachovia. In fiscal year 2008, the Company increased the maximum amount available to the Company under its credit facilities with Wachovia to $8,420,000 and delivered to Wachovia two replacement promissory notes as follows: (i) a Renewal and Future Advance Promissory Note in the amount of $3,920,000 (the "Future Advance Note"), and (ii) a Renewal and Amended Term Promissory Note in the amount of $2,000,000 (the "Term Note" and together with the Future Advance Note, the "Notes"). Additionally, the Company's revolving credit facility of $2,500,000 was continued under the original terms of the revolving promissory note. The Future Advance Note was collateralized by the Company's real estate in Clearwater, Florida. The revolving credit facility was collateralized by the Company's assets, with the exception of the Company's real estate located in Earlysville, Virginia and Clearwater, Florida. The Term Note was collateralized by the Company's real estate in Earlysville, Virginia. The Notes were scheduled to mature on: (i) with respect to the Future Advance Note, September 1, 2022, and (ii) with respect to the Term Note, June 1, 2011. The interest rate on the Wachovia revolving credit facility, as well as on the Notes was one-month LIBOR (which was 0.25% at April 30, 2010, the date of refinancing), plus 300 basis points.

The Company's long-term debt agreements with Wachovia contained certain financial and other restrictive covenants, including the requirement to maintain: (i) at all times, a ratio of total liabilities to tangible net worth that does not exceed 1.30 to 1.00; and (ii) at the end of each fiscal quarter, a cash flow coverage ratio (with regard to the debt service) of at least 1.25 to 1.00.

As of January 31, 2010, the Company was not in compliance with Wachovia's cash flow coverage ratio covenant and the total liability to tangible net worth covenant. Wachovia provided a written waiver of the non-compliance to the Company through April 30, 2010. Consequently, the entire amount of long-term debt was classified as current maturities at January 31, 2010.

Wachovia's other restrictive covenants, among other things, required the Company to obtain consent from the lender prior to making a material change of management, guarantee or otherwise become responsible for obligations of any other person or entity or assuming or becoming liable for any debt, contingent or direct, in excess of $100,000.

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Long-term debt and Notes Payable at January 31, 2011 and January 31, 2010 consisted of the following:

	2011	2010
Future Advance Note	$ -	$ 3,294,000
Term Note	-	1,786,000
Real Estate Mortgage Note	3,344,000	-
Equipment Term Note	1,647,000	-
Equipment Credit Line Note	700,000	-
Notes Payable	549,000	688,000
	6,240,000	5,768,000
Less: current maturities	(1,255,000)	(5,768,000)
Long-term debt, less current maturities	$ 4,985,000	$ -

Interest and accretion expense on long-term debt and revolving credit facility for the years ended January 31, 2011 and 2010 was $745,000 and $602,000, respectively.

13. Stockholders' Equity

Income Per Share

Basic income per share is based upon the Company's weighted average number of common shares outstanding during each period. Diluted income per share is based upon the weighted average number of common shares outstanding during each period, assuming the issuance of common shares for all dilutive potential common shares outstanding during the period, using the treasury stock method. Potential common stock of 118,000 shares were not included in the computation of diluted loss per share for both years ended January 31, 2011 and 2010, respectively, as the inclusion of the potential common stock would be anti-dilutive.

	Years Ended January 31,	
	2011	2010
Weighted average shares outstanding-basic	3,739,211	3,689,914
Dilutive effect of stock options and warrants	314,088	215,954
Weighted average shares outstanding-diluted	4,053,299	3,905,868

Options to Purchase Stock

In July 2004, the Company adopted the Aerosonic Corporation 2004 Stock Incentive Plan ("2004 SIP"), which authorized the awarding of options to purchase up to a total of 400,000 shares of the Company's common stock. For option awards, the 2004 SIP provides that the strike price shall not be less than the fair market value of the common stock on the date of grant and that no portion of any option award may be exercised beyond ten years from that date. In addition, no incentive stock option can be granted and exercised beyond five years to a stockholder owning 10% or more of the Company's outstanding common stock. On July 13, 2009, stockholders approved an amendment to the Aerosonic Corporation 2004 Stock Incentive Plan (the Plan) that extended the duration of the Plan for five years to July 14, 2014 and increased the total number of shares of Aerosonic common stock issuable pursuant to the Plan from 400,000 shares of common stock to 550,000 shares.

On October 5, 2009, the Company issued to a key employee, options to purchase 3,000 shares of the Company's common stock at the common stock's market price on that day of $5.05. These options vest from one to three years from the date of grant.

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During the second quarter of fiscal year 2010, the Company issued to certain key employees, options to purchase in the aggregate 7,500 shares of the Company's common stock at the common stock's market price on those dates ranging from $1.87 to $2.62. These options vest from one to three years from the date of grant.

On May 26, 2009, the Company issued to its Executive Vice President and Chief Financial Officer, options to purchase 25,000 shares of the Company's common stock at the common stock's market price on that day of $2.36. These options vest from one to three years from the date of grant.

On May 11, 2009, the Company issued to its Vice President of Technology and Product Development, options to purchase 25,000 shares of the Company's common stock at the common stock's market price on that day of $2.65. These options vest from one to three years from the date of grant.

On March 2, 2009, the Company issued to certain key employees, options to purchase in aggregate 15,000 shares of the Company's common stock at the common stock's market price on that date of $1.01. These options vest from one to three years from the date of grant.

On February 27, 2009, the Company issued to its President and Chief Executive Officer, its Executive Vice President of Sales and Marketing and its Executive Vice President of Operations, options to purchase 48,000, shares, 24,000 shares and 24,000 shares, respectively, of the Company's common stock at the common stock's market price on that day of $1.00. These options vest from one to three years from the date of grant.

A summary of the activity related to the Company's stock options during fiscal year 2011 is presented in the table below:

	Years Ended January 31,					
	2011			2010		
	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (In years)	Shares	Weighted Average Exercise Price	Weighted Average Remaining Contractual Life (In years)
Beginning options outstanding	324,600	$ 2.80		168,100	$ 4.48	
Options granted	-	$ -		171,500	$ 1.56	
Options exercised	(1,000)	$ 1.01		-	$ -	
Options expired, cancelled or forfeited	(3,400)	$ 2.25		(15,000)	$ 7.25	
Ending options outstanding	320,200	$ 2.82	7.67	324,600	$ 2.80	8.65
Options exercisable at January 31,	156,000	$ 3.39	7.38	59,000	$ 4.71	7.68

Stock options vest over a period of two to four years and have 10-year terms. Exercise prices of stock options awarded for all periods were equal to the market price of the stock on the date of grant. The weighted average grant date fair value per share of options granted during the years ended January 31, 2011 and 2010, vested and unvested, was $0 and $1.13, respectively.

As of January 31, 2011, there was approximately $139,000 of unrecognized compensation cost related to unvested options. This cost is expected to be recognized over a weighted average period of approximately 1.1 years.

The Company recorded equity-based compensation expense on its options in accordance with U.S. GAAP of approximately $180,000 and $186,000 for the years ended January 31, 2011 and 2010, respectively, which is included in selling, general and administrative expenses.

During fiscal year 2011, 1,000 options were exercised. There were no options exercised in fiscal year 2010.

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14. Income Taxes

Income tax (benefit) expense for the years ended January 31, 2011 and 2010 consisted of:

	2011	2010
Current:		
Federal	$ (91,000)	$ 1,637,000
State	(9,000)	159,000
	(100,000)	1,796,000
Deferred:		
Federal	506,000	(1,794,000)
State	49,000	(174,000)
	555,000	(1,968,000)
Income tax (benefit) expense	$ 455,000	$ (172,000)

The following table illustrates the difference between the statutory income tax rates applicable to the Company versus the effective tax expense (benefit) rate for the years ended January 31, 2011 and 2010:

	2011	2010
Federal tax rate	34.0 %	34.0 %
Increase (decrease) in taxes resulting from:		
State income taxes, net of federal tax benefit	4.9	3.6
Valuation allowance	-	(46.5)
Change in unrecognized tax benefit and related interest	(3.7)	(5.2)
Intrinsic costs warrants	9.7	2.5
Stock based compensation	5.6	1.5
Adjustment of NOL and other deferred tax accounts (primarily fixed assets)	(3.5)	7.1
Domestic manufacturing deduction	-	(1.2)
Other - primarily non-deductible expenses	(4.9)	-
Effective tax rate	42.1 %	(4.2) %

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The tax effects of temporary differences that give rise to significant portions of the deferred tax assets and deferred tax liabilities at January 31, 2011 and 2010 were as follows:

	2011	2010
Current deferred tax assets:		
Accounts receivable	$ 227,000	$ 244,000
Inventories	1,243,000	1,086,000
Compensation expense	75,000	189,000
Contract loss	13,000	-
Other	59,000	94,000
Total current deferred tax assets	1,617,000	1,613,000
Non-current deferred tax assets:		
Property, plant and equipment, principally due to differences in depreciation and capitalized interest	142,000	128,000
Building held for sale	77,000	124,000
Research and experimentation and alternative minimum tax credits	325,000	392,000
Stock-based compensation	-	15,000
Net operating loss carryforward	654,000	1,172,000
Total non-current deferred tax assets	1,198,000	1,831,000
Total deferred tax asset	2,815,000	3,444,000
Non-current deferred tax liabilities:		
Identifiable intangibles	95,000	168,000
Net deferred tax asset	$ 2,720,000	$ 3,276,000

At January 31, 2011, the Company has a total net operating loss carryforward for U.S. Federal tax purposes of approximately $1,756,000 and research and development tax credits of $234,000 which expire in various years through 2029.

Realization of the Company’s net deferred tax asset is dependent upon the Company generating sufficient taxable income in future years to obtain a benefit from the reversal of deductible temporary differences and from tax loss carryforwards. The Company has concluded, based on expected future results and the future reversals of existing taxable temporary differences, a reserve is not needed at January 31, 2011.

The Company records provisions dealing with uncertain tax positions as required in ASC740. As a result, the Company has recorded a liability for $0 and $40,000 at January 31, 2011 and 2010, respectively, of unrecognized tax benefits, inclusive of estimated accrued interest and penalties. At January 31, 2011, there was no accrued interest or accrued penalties related to uncertain tax positions.. At January 31, 2010, accrued interest was $12,000 and accrued penalties were $5,000, for a total of $17,000. If unrecognized tax benefits were to be recognized in a future period it would reduce the statement of operations tax provision, thereby impacting the effective tax rate. The impact of recognition on the income tax provision reflects the amounts for unrecognized tax benefits net of the deferred tax benefit on accrued interest and state income tax items, and reversal of accrued interest and penalties. Interest and penalties related to underpayment of income taxes are classified as a component of income taxes in the consolidated statement of operations.

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A reconciliation of the total amount of unrecognized tax benefits is as follows:

Unrecognized tax benefits: February 1, 2010	$40,000
Lapse of statute of limitations	(40,000)
Unrecognized tax benefits: January 31, 2011	$-

The Company is generally no longer subject to examinations with respect to returns that have been filed for years prior to 2008.

The Company is not currently under examination by any taxing authority. We do not anticipate that the amount of the unrecognized benefit will significantly increase or decrease within the next twelve months.

15. Major Customer Information

Direct and indirect sales to U.S. Government agencies, when combined, represented 10% or more of net sales and amounted to approximately $10,104,000 and $8,841,000 for the years ended January 31, 2011 and 2010, respectively. Of these amounts, approximately $4,976,000 and $2,493,000 were sales directly to U.S. Government agencies for the years ended January 31, 2011 and 2010, respectively. The remaining amount of $5,128,000 represents sales to commercial customers for government applications.

Sales to Korea Aerospace Industries represented approximately 14% of total sales for the year ended January 31, 2011. Foreign sales for the years ended January 31, 2011 and 2010 were approximately $7,630,000 and $12,766,000, respectively. Substantially all foreign sales contracts are payable in U.S. dollars. No other customer sales totaled greater than 10 percent of revenue for the years ended January 31, 2011 and 2010.

Accounts receivable at January 31, 2011 included approximately $825,000 due from Korea Aerospace Industries. Accounts receivable at January 31, 2010 included approximately $425,000 and $23,000 due from Korea Aerospace Industries and The Boeing Company, respectively. No other customer represented greater than 10 percent of accounts receivable at January 31, 2011 or 2010.

16. Contingencies and Commitments

Contingencies

Litigation

From time to time, the Company may be involved in certain claims and legal actions arising in the ordinary course of business. As of January 31, 2011, there were no claims or legal actions that will have a material adverse effect on the Company’s financial position, results of operations, or liquidity.

Environmental

In preparation for the sale of the Earlysville, Virginia facility, the Company engaged an environmental consulting firm to survey the property for possible soil or groundwater contamination. This survey revealed impacts to both shallow soils and groundwater that may have resulted from the accidental loss of solvents. As a result of the initial and subsequent surveys, contamination treatment was determined to be necessary at an estimated total cost of $808,000 as of January 31, 2011, as determined by an environmental compliance specialist, and which is included in the environmental liability. Thus, in accordance with U.S. GAAP, the Company capitalized these contamination treatment costs in its fiscal year 2008 financial statements as an increase to property held for sale, net, since such costs will be incurred in preparation for the sale of the Earlysville, Virginia facility.

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The Company has had discussions with the former owner of the property concerning responsibility for contamination treatment. The former owner of the property and the Company solicited proposals from environmental consulting firms and received a proposal from which management estimates the cost of contamination treatment to be approximately $625,000. Depending on the findings of this additional study, the scope and cost of the contamination treatment may change. Current estimates of future monitoring, oversight and other related costs are estimated between $175,000 and $225,000. The Company and the former owner of the property met with the Virginia Department of Environmental Quality (Virginia DEQ) in October 2009 to review the contamination characterization and treatment plans. We continue to be in communication with the former owner of the property concerning its responsibility to cover the costs of the contamination characterization and treatment. We will reassess the accrued liability and record any appropriate adjustments in our financial statements following completion of the characterization process and negotiations with the former owner. Costs to pay an environmental consulting firm to characterize contamination that may be present in the ground between the Company's property and nearby homes was incurred during the fiscal years ended January 31, 2011 and 2010 totaled $124,000 and $153,000, respectively.

After the August 8, 2008 fire at our Florida facility, during a routine investigation by the Florida Department of Environmental Protection ("Florida DEP"), the Company was cited with violations, and potential civil penalties estimated at $100,000, relating to the storage, handling and disposal of normal chemicals, solvents and paints used in our production facility. The Company's remediation plan, to avoid future violations and the payment of the above civil penalties, was submitted and subsequently approved by the Florida DEP. During the three months ended April 30, 2010, the Company completed the construction of a materials handling building at a cost of $116,000. On June 7, 2010, the Company received a release of said violations and civil penalties from the Florida DEP.

Commitments

Purchase commitments

At January 31, 2011, the Company was committed to future purchases of approximately $3,454,000 for materials and services as well as a development contract. These purchase commitments are supported by firm underlying contracts with customers and contain provisions permitting the Company to terminate such purchase commitments in the event the underlying contracts should be terminated or discontinued.

Purchase commitments as of January 31, 2011 are as follows:

	Payments Due By Period				
	Less Than One Year	One Year to 3 Years	Greater Than 3 Years to 5 Years	After 5 Years	Total
Purchase commitments	$ 2,932,000	$ 522,000	$ -	$ -	$ 3,454,000

Leases

On September 20, 2007, the Company entered into a five year operating lease at a location near Charlottesville, Virginia, which represents the new facility for the support and repair/overhaul employees of Avionics who were retained subsequent to the consolidation of the Earlysville operations into the Clearwater facility. Total rental expense was approximately $154,000 and $181,000 for the years ended January 31, 2011 and 2010, respectively, which is included in cost of sales.

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The future minimum rental payments under leases that have initial or remaining non-cancelable lease terms in excess of one year at January 31, 2011 are as follows:

For the years ending January 31,		Operating Leases
2012		175,000
2013		151,000
	$	326,000

17. Employee Retirement Plan

The Company's employees are eligible, after completing three months of service, to participate in a 401(k) plan (the "Plan") sponsored by Aerosonic Corporation. Under the terms of the Plan, employees may contribute up to 15% of their gross earnings subject to IRS limitations. The Company may match up to 100% of the first 3% of employees' contributions. The Company's matching contributions to the Plan were $86,000 and $0 for the years ended January 31, 2011 and 2010, respectively and are included in selling, general and administrative expenses. The Company, having elected to discontinue voluntary matching contributions during the year ended January 31, 2010, reinstated the voluntary matching contribution during the year ended January 31, 2011.

18. Quarterly Data (Unaudited)

Set forth below are the Company's quarterly data (unaudited) for the years ended January 31, 2011 and 2010.

	Quarters Ended			
	April 30	July 30	October 29	January 31
2011				
Sales, net	$6,931,000	$6,813,000	$7,049,000	$8,825,000
Gross profit	$2,154,000	$2,099,000	$2,069,000	$2,810,000
Operating income	$399,000	$280,000	$345,000	$693,000
Net income	$259,000	$18,000	$93,000	$255,000
Basic income per share	$0.07	$-	$0.02	$0.07
Diluted income per share	$0.06	$-	$0.02	$0.06
	May 1	July 31	October 30	January 31
2010				
Sales, net	$8,774,000	$8,114,000	$7,537,000	$6,711,000
Gross profit	$3,060,000	$2,913,000	$2,487,000	$2,408,000
Operating income	$1,741,000	$1,004,000	$918,000	$480,000
Net income	$1,375,000	$556,000	$728,000	$1,602,000
Basic income per share	$0.38	$0.15	$0.20	$0.43
Diluted income per share	$0.38	$0.14	$0.18	$0.40

19. Subsequent Events

On February 15, 2011, the Corporation decided to close its repair facility in Charlottesville, Virginia and transfer the repair operations to its Clearwater, Florida facility. The Company's decision resulted from its efforts to reduce costs by utilizing the enhanced capacity at its Clearwater facility created through recent "lean manufacturing" and other operational improvement programs. The Company is assessing the cost of the facility closure and expects those costs to result in a future cash expenditure. The Company expects the closure to be completed by June 30, 2011.

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On March 31, 2011, the Company completed repayment of the Investors' Notes Payable in full satisfaction of the remaining debt outstanding of $600,000 as of January 31, 2011.

On April 28, 2011, M&I Bank waived the Company's January 31, 2011 non-compliance with the Funded Debt to EDITDA covenant in the Credit Facility.

On April 29, 2011, pursuant to a Joint Amendment to Loan Agreement and Revolving Line of Credit Note, M&I Bank amended the Credit Facility's Funded Debt to EBITDA covenant to 4.0:1.0 for the balance of fiscal year 2012. The lender also extended the maturity date of the Revolving Credit Line Note to June 28, 2011.