

**Frequency Electronics, Inc.**

**ANNUAL REPORT**

**2013**

## **FISCAL YEAR 2013 CHAIRMAN'S LETTER TO STOCKHOLDERS**

"Do More With Less" is becoming the top priority mission for many U.S. Government/DOD agencies and commercial enterprises. Frequency Electronics is providing products and technologies which materially help fulfill this mission.

Our world-leading precision time and frequency technologies are used to improve the performance and functionality of many electronic systems at affordable cost. Upgrades are needed for a wide variety of sophisticated electronic platforms and systems on land, sea, in air and in space, including manned aircraft, UAVs, secure communication, missile deployment and detection, fossil fuel exploration techniques, navigation and positioning systems like GPS, intelligence and surveillance operations, smart energy distribution networks and more. Millions of dollars will be spent to save billions of dollars. For example, developing a new communication satellite platform is a multi-billion dollar project but increasing the capacity of existing satellite designs can be accomplished with millions. We are now supplying precision timing and microwave frequency generation products which enhance satellite designs already proven in space, providing more bandwidth and greater throughput at a fraction of the cost.

Frequency is a company with the right legacy, products, and resources at the right time. We are growing and profitable.

### **THE YEAR IN REVIEW**

Revenues grew by 8% to \$68.9 million in Fiscal 2013 which ended April 30<sup>th</sup> of this year. On an even more positive note, satellite payload revenues grew 11% year-over-year. Satellite payloads are our dominant and fastest growing business, now over 50% of consolidated revenues, with long-range space programs representing over 75% of our consolidated backlog. Sales for non-space, U.S. Government/DOD end-use grew for the ninth successive year and accounted for over 25% of consolidated revenues.

Operating profit was \$4.7 million. Net income was \$3.7 million, or \$0.43 per share. (Our prior year's net income included a non-cash tax valuation benefit of \$3.1 million or \$0.36 per share.) Our non-GAAP EBITDA was \$10.5 million.

We were anticipating record levels of operating profit and EBITDA for last year until the final quarter. We now expect to reach those record levels this current year.

### **LOOKING AHEAD**

For the foreseeable future, space will be the area of greatest expansion in communication bandwidth. Frequency will introduce a new family of products, Ku and Ka band receivers and up/down frequency converters, for satellite payloads. These new products feature smaller size, less weight, reduced power, lower cost and shorter time for delivery than products currently available. We will offer these new assemblies this year in addition to our legacy products now successfully flying on existing satellite payloads. Certainly the outlook for our space business is bright, as is the outlook for low g-sensitivity generators and state-of-the-art timing systems for non-space applications.

We look forward to continued productive collaboration with FEI-Elcom, our newest subsidiary. FEI-Elcom has made promising inroads in the electronic warfare, intelligence and surveillance areas which are their primary markets. In the first quarter of last year, FEI-Elcom recorded a \$900,000 operating loss. Since that quarter, FEI-Elcom has generated increased revenues and operating profits. In addition, FEI-Elcom is applying major engineering resources to our corporate product development initiatives.

FEI-Zyfer has an impressive legacy in GPS receiver technology especially in relation to security and anti-hostile spoofing (SAASM) applications. Although in the final quarter of last year, FEI-Zyfer experienced losses from delays in orders and lower than expected revenues, we maintain a positive

near- and longer-term outlook for FEI-Zyfer. Our outlook is supported by new, heightened and compelling requirements for defending GPS transmissions against corruption by cyber warfare.

We are optimistic about the prospects for Gillam-FEI. Gillam-FEI has participated for several years in designing hardware and creating software in connection with the French government's smart electrical grid initiative. Based on slower than anticipated rollout of this project, we have less visibility regarding the probable schedule for obtaining production-level orders, which are now anticipated to occur in our next fiscal year 2015. Accordingly, the Company elected to write down \$1.4 million of accumulated costs in fiscal 2013. Gillam-FEI's assemblies, which incorporate sophisticated software, are currently being field-tested by the French electrical utility company. Gillam-FEI anticipates being a major participant in this program which requires deployment of such assemblies in over 600,000 electric substations in France.

Partnering, acquisitions and mergers will continue to be prominent on our agenda. Based on the high level of proposal activity, our excellent bookings during the first four months of this year and our increasing backlog, we look ahead to continued growth and profitability this year and beyond.

I will close my remarks by giving a well-deserved "Thank you" to our officers, directors, and employees for their many contributions to the success we have achieved over these past several years. This letter also offers sincere thanks to our shareholders for their continued investment in our future. All of us at Frequency are very grateful for the confidence that you have placed in us.

*/s/ Joseph P. Franklin*

JOSEPH P. FRANKLIN

Major General, US Army (Retired)

Chairman of the Board

**Financial Highlights**

<b>For the years ended April 30:</b>	<b>2013</b>	<b>2012</b>
Revenues .....	\$68,932,000	\$63,595,000
Net Income .....	\$3,686,000	\$7,374,000
Earnings per share (diluted).....	\$0.43	\$0.86
Average number of common and common equivalent shares (diluted)	8,604,651	8,540,955

**At April 30:**

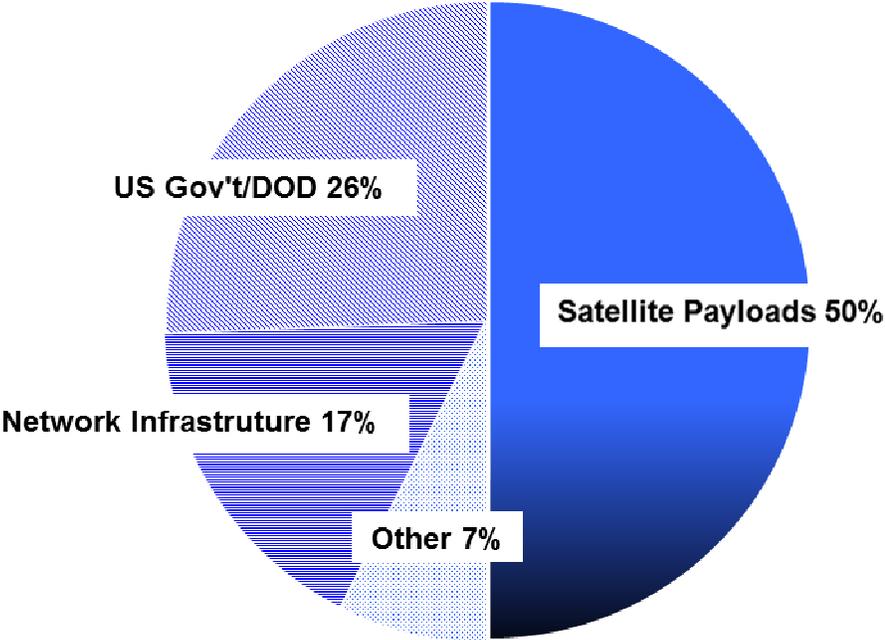
Working Capital .....	\$71,689,000	\$63,253,000
Current Ratio .....	8.7 to 1	4.9 to 1
Total Assets.....	\$108,900,000	\$106,227,000
Stockholders' Equity	\$82,452,000	\$79,132,000

**Market Prices of Common Stock**

The common stock of the Company is listed on the NASDAQ Global Market under the symbol "FEIM"

<b>Fiscal Quarter</b>	<b>High Sale</b>	<b>Low Sale</b>
<b>2013</b>		
First Quarter.....	\$ 9.50	\$ 7.02
Second Quarter.....	9.74	8.39
Third Quarter.....	9.88	6.71
Fourth Quarter .....	10.25	8.52
<b>2012</b>		
First Quarter.....	\$ 11.79	\$ 8.80
Second Quarter.....	10.75	8.15
Third Quarter.....	9.16	6.91
Fourth Quarter .....	8.89	7.28

**Fiscal Year 2013 Revenues by Market Area**



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

FORM 10-K

(Mark one)

ANNUAL REPORT PURSUANT TO SECTION 13 or 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Fiscal Year ended April 30, 2013

OR

TRANSITION REPORT PURSUANT TO SECTION 13 or 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from \_\_\_\_\_ to \_\_\_\_\_

Commission File No. 1-8061

**FREQUENCY ELECTRONICS, INC.**

(Exact name of Registrant as specified in its charter)

**Delaware**

(State or other jurisdiction of incorporation or organization)

**11-1986657**

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

**55 CHARLES LINDBERGH BLVD., MITCHEL FIELD, N.Y.**

(Address of principal executive offices)

**11553**

(Zip Code)

Registrant's telephone number, including area code: **516-794-4500**

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

\_\_\_\_\_  
Title of each class  
**Common Stock (par value \$1.00 per share)**

\_\_\_\_\_  
Name of each exchange on which registered  
**NASDAQ Global Market**

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 Exchange 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 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 web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (para 232.405 of this chapter) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes X No \_\_\_

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

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 the definitions of "large accelerated filer," "accelerated filer" and "smaller reporting company" in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer \_\_\_ Accelerated filer \_\_\_ Non-accelerated filer \_\_\_ 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 voting stock held by non-affiliates of the Registrant as of October 31, 2012 - \$45,300,000

APPLICABLE ONLY TO CORPORATE ISSUERS:

The number of shares outstanding of Registrant's Common Stock, par value \$1.00 as of July 22, 2013 - 8,493,333

DOCUMENTS INCORPORATED BY REFERENCE: PART III incorporates information by reference from the definitive proxy statement to be filed for the Annual Meeting of Stockholders to be held on or about October 8, 2013.

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

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## PART I

### Item 1. Business

#### GENERAL DISCUSSION

Frequency Electronics, Inc. (sometimes referred to as "Registrant", "Frequency Electronics" or the "Company") is a world leader in precision time and frequency technology which is employed in commercial, government, C4ISR and other military electronic systems. Its technology is used for a wide range of terrestrial and space applications.

Unless the context indicates otherwise, references to the Registrant or the Company are to Frequency Electronics, Inc. and its subsidiaries. References to "FEI" are to the parent company alone and do not refer to any of the subsidiaries. Frequency Electronics, a Delaware corporation, has its principal executive office at 55 Charles Lindbergh Boulevard, Mitchel Field, New York 11553. Its telephone number is 516-794-4500 and its website is [www.frequencyelectronics.com](http://www.frequencyelectronics.com).

Frequency Electronics was founded in 1961 as a research and development firm generating proprietary precision time and frequency technology primarily under contracts for the United States ("U.S.") Government end-use. In the mid-1990's, the Company evolved into a designer, developer and manufacturer of state-of-the-art products for both commercial and government end-use. The Company's present mission is to be the world leader in providing precision time and low phase noise frequency generation systems, from 1 Hz to 46 GHz for space and other challenging environments. The Company's technology is the key element in enhancing the functionality and performance of many electronic systems.

#### MARKETS

The Company's dominant business area is satellite payloads. It has a unique legacy of providing master timing systems, power converters, and frequency generation, synthesis and distribution systems. It is currently addressing new opportunities in frequency converters, transmitters and receivers, representing a significant increase in the potential revenue for FEI products on any one satellite. These products support primary and hosted payloads for both commercial and U.S. government end-use. Currently, approximately one thousand satellites with varying remaining years of useful life are operating in High/Geostationary, Medium and Low Earth Orbits. This number of operational satellites is expected to continue to grow over the next ten years as many new satellites are added and older ones are replaced.

The Company's products support multiple C4ISR ("Command, Control, Communication, Computer, Intelligence, Security and Reconnaissance"), counter measures and additional defense electronic applications for the U.S. government on land, sea and air-borne platforms.

Commercial markets include network infrastructure and other industrial uses. The Company's products support precise signal synchronization in mobile communication networks to maintain quality of service. Its products support expanded bandwidth and security in public and enterprise networks. The vast world-wide wireline network infrastructure incorporates thousands of central offices which provide network integrity and interconnectivity. The Company provides remote terminal units ("RTU") for management of networks such as power grids and gas lines as well as specialized timing technology for oil and gas exploration.

To address these markets, the Company has several corporate entities which operate under three reportable segments primarily based on the geographic locations of its subsidiaries. For additional information about these reportable segments, see "Item 1 – REPORTABLE SEGMENTS AND PRODUCTS.":

1. **FEI-NY** The Company's satellite payload products for U.S. Government and commercial satellite programs are designed, developed and manufactured at its Long Island, New York facility. At this location the Company also applies its technology and legacy to products for the U.S. military and other U.S. Government agencies, for certain terrestrial commercial communication products and for other industrial applications.

Frequency Electronics, Inc. Asia ("FEI-Asia") was established in fiscal year 2002 to be the Company's Asian-based low cost manufacturer of certain commercial communications products

used primarily in the wireless and wireline markets. FEI-Asia is located in the Free-Trade Zone in Tianjin, China.

In February 2012, the Company completed the acquisition of Elcom Technologies, Inc. (now FEI-Elcom Tech, Inc. or "FEI-Elcom"). FEI-Elcom designs and manufactures RF microwave devices and subsystems up to 46 GHz including fast switching, ultra low phase noise synthesizers, up-down converters, receivers, ceramic resonant oscillators and dielectric resonant oscillators. These instruments and components are critical for communication, surveillance, signal intelligence, automatic testing, satellite ground stations and satellite payloads.

2. **Gillam-FEI** - The Company's Belgian subsidiary, acquired in September 2000, develops and manufactures products for various network management and synchronization systems for different industries, utilities and telecommunications providers in Europe, Africa, the Middle East and Asia.
3. **FEI-Zyfer** - Precision time and frequency products that incorporate global positioning systems ("GPS") technology are manufactured by the Company's subsidiary FEI-Zyfer, Inc. ("FEI-Zyfer"), which was acquired in fiscal year 2004. FEI-Zyfer's GPS capability complements the Company's existing technologies and permits the combined entities to provide a broader range of embedded systems for a variety of timing functions and anti-spoofing ("SAASM") applications. FEI-Zyfer also provides sales and support in the U.S. for the Company's wireline telecommunications family of products.

In addition to its subsidiaries, the Company has a strategic investment in Morion, Inc. ("Morion"), a Russian crystal oscillator manufacturer located in St. Petersburg, Russia. The Company's ownership of 4.6% of the outstanding shares of Morion's common stock permits the Company to secure a cost-effective source for high precision quartz resonators and crystal oscillators. The Morion investment is accounted for under the cost method. (See "NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – 9. Investment in Morion, Inc.")

#### FISCAL YEAR 2013 SUBSEQUENT EVENT

##### **Refinance Debt with Revolving Credit Agreement.**

On June 6, 2013, the Company obtained a five-year credit facility (the "Facility") from JPMorgan Chase Bank, N.A. ("JPMorgan") pursuant to a credit agreement (the "Credit Agreement") between the Company and JPMorgan. The maximum aggregate amount of the Facility is \$25.0 million, of which the Company immediately borrowed \$7.2 million, using the proceeds to repay the outstanding balance under the \$9.3 million line of credit with another financial institution which formerly managed a substantial portion of the Company's investment portfolio. As a result of this refinancing of short-term credit with a long-term obligation, as of April 30, 2013, the Company reclassified the \$6.0 million balance payable under the replaced line of credit to long-term debt. For a full description of the Facility, see NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – 7. Debt Obligations and Subsequent Event." Proceeds from the Facility will be used for working capital and to finance acquisitions.

#### REPORTABLE SEGMENTS AND PRODUCTS

The Company operates under three reportable segments, primarily aligned with the geographical locations of its subsidiaries: (1) FEI-NY, (2) Gillam-FEI; and (3) FEI-Zyfer. Within each segment the Company designs, develops, manufactures and markets precision time and frequency control products for different markets as described below. The Company's Chief Executive Officer measures segment performance based on total revenues and profits generated by each geographic center rather than on the specific types of customers or end-users. Consequently, the Company determined that the segments indicated above appropriately reflect the way the Company's management views the business. The FEI-NY segment, which operates out of the Company's Long Island, New York headquarters facility also includes the operations of the Company's wholly-owned subsidiaries, FEI-Asia and FEI-Elcom. FEI-Asia functions as a manufacturing facility for FEI-NY and other segments with minimal sales to outside customers. FEI-Elcom, in addition to its own product line, provides design and technical support for the FEI-NY segment's satellite business.

The products for the FEI-NY segment are principally marketed to the commercial and U.S. Government satellite markets, to other U.S. Department of Defense ("DOD") programs and to wireless

communications networks. The Gillam-FEI segment operates out of Belgium and France and designs, develops and manufactures products for network synchronization and monitoring. Its products are currently sold primarily to non-U.S. customers. The primary business of the FEI-Zyfer segment, which operates out of California, is the design and manufacture of products which incorporate GPS technologies. FEI-Zyfer sells its products to both commercial and U.S. Government customers, collaborates with other FEI segments on joint product development activities and provides sales and support for network synchronization products.

During fiscal years 2013 and 2012, approximately 76% and 70%, respectively, of the Company's consolidated revenues were from products sold by the FEI-NY segment. Sales by Gillam-FEI were approximately 17% and 20% of consolidated revenues for fiscal years 2013 and 2012, respectively. In fiscal years 2013 and 2012, sales for the FEI-Zyfer segment were 15% and 18% of consolidated revenues, respectively. (The sum of annual sales percentages exceeds 100% due to intersegment sales.)

Consolidated revenues include sales to end-users in countries located outside of the U.S. During fiscal years 2013 and 2012, foreign sales comprised 26% and 33%, respectively, of consolidated revenues. For segment information, see "NOTES TO CONSOLIDATED FINANCIAL STATEMENTS – 15. Segment Information."

#### **FEI-NY SEGMENT:**

The Company provides precision time, frequency generation and synchronization products and subsystems that are found in ground-based communication stations, on-board satellites and imbedded in moving platforms operated by the U.S. military. The Company has made a substantial investment in research and development to apply its core technologies to satellite payloads, non-space DOD programs and network infrastructure markets. Revenues from satellite payloads, both for commercial and U.S. Government applications have increased in recent years while the portion of network infrastructure sales was reduced. The Company expects to continue to generate substantial revenues from deployment of new and replacement satellites and other U.S. Government/DOD applications including sales of ruggedized subsystems for moving platforms of the U.S. military.

#### **Satellite Payloads**

The use of satellites launched for communications, navigation, weather forecasting, video and data transmissions and Internet access has expanded the need to transmit increasing amounts of voice, video, and data to earth-based receivers. This requires more precise timing and frequency control at the satellite. The Company manufactures the master timing systems (quartz, rubidium and cesium) and other significant timing and frequency generation products for communication satellite, and many of the Company's other space assemblies are used onboard spacecraft for command, control and power distribution. Efficient and reliable DC-DC power converters are also manufactured for the Company's own assemblies and as stand-alone products for space applications. The Company's oven-controlled quartz crystal oscillators are cost-effective precision clocks suited for high-end performance required in satellite transmissions, airborne telephony and geophysical survey positioning systems. Newly developed and upgraded frequency generators, synthesizers, and up/down converters and receivers have augmented the Company's product offerings and positioned the Company to provide a greater share of a typical satellite's payload. Commercial satellite programs which utilize the Company's space-qualified products include Iridium NEXT, MexSat, MSV, ICO, TerreStar, GlobalStar, Intelsat, Inmarsat and numerous others.

In the years ahead, the Company expects that the U.S. DOD will require more secure communication capabilities, more assets in space and greater bandwidth. The Global Positioning Satellite System, the MILSTAR Satellite System and the AEHF Satellite System are examples of the programs in which the Company participates - programs which management believes are important to the success of the U.S. Government's security, communication and intelligence needs. The Company has manufactured the master clock for the Trident missile, the basic timing system for the Voyager I and Voyager II deep space exploratory missions and the quartz timing system for the Space Shuttle. The Company's product offerings for U.S. Government satellite programs are similar in design and function to those used on commercial satellites, as described above.

### **U.S. Government- non-space:**

In addition to space-based programs, the Company's proprietary products have been used in airborne and ground-based guidance, navigation, communications, radar, sonar surveillance and electronic countermeasure and timing systems. The Company has developed and patented a low g-sensitivity (gravity) technology which offers a 100-fold improvement in performance under shock, vibration and other environmental effects. Products are built in accordance with DOD standards and are in use on many of the U.S.' important military applications. The Company anticipates that adequate funds will be provided by the U.S. Government to ensure that these programs are sustained.

FEI-Elcom designs and manufactures RF microwave devices and subsystems up to 46 GHz including fast switching, ultra low phase noise synthesizers, up-down converters, receivers, ceramic resonant oscillators and dielectric resonant oscillators. These instruments and components are important for communication, surveillance, signal intelligence, automatic testing, satellite ground stations and satellite payloads.

The Company's sales on U.S. Government programs for both space and non-space applications are generally made under fixed price contracts either directly with U.S. Government agencies or indirectly through subcontracts intended for government end-use. The price paid to the Company is not subject to adjustment by reason of the costs incurred by the Company in the performance of the contract, except for costs incurred due to contract changes ordered by the customer. These contracts are negotiated on terms under which the Company bears the risk of cost overruns and derives the benefit from cost savings.

In March 2013, the Budget Control Act of 2011 went into effect to reduce the federal deficit by a process known as sequestration. Unless Congress passes a subsequent law to offset it, expenditures by the Department of Defense will be significantly reduced for the foreseeable future. As indicated above, many of the programs and platforms for which Frequency supplies products and systems, are used by the U.S. Government for maintaining secure communications world-wide, for obtaining vital intelligence and enabling precision targeting capabilities. It is the belief of management that the future success of the mission of the U.S. military and intelligence gathering community is heavily dependent on successful and timely deployment of these systems. Thus, the Company anticipates that adequate funds will be provided by the U.S. Government to ensure that the programs are completed. It is possible, however, that some programs or product sales could be slowed or delayed due to U.S. Government spending constraints.

Recently the Company has also received several cost-plus-fee contracts. Under these contracts, the Company may be able to recover all of its direct and indirect costs related to the programs plus a pre-determined fee. In the event of substantial cost overruns, the fee may be reduced.

Negotiations on U.S. Government contracts are sometimes based in part on Certificates of Current Costs. An inaccuracy in such certificates may entitle the government to an appropriate recovery. From time to time, the Defense Contracts Audit Agency ("DCAA") audits the Company's accounts with respect to these contracts.

All U.S. Government end-use contracts are subject to termination by the purchaser for the convenience of the U.S. Government and are subject to various other provisions for the protection of the U.S. Government. In the event of such termination, the Company is entitled to receive compensation as provided under such contracts and in the applicable U.S. Government regulations.

### **Network Infrastructure**

The development of new and enhanced technologies brings expanded and more reliable telecommunications and Internet services to the public. As digital cellular systems and Personal Communication Systems ("PCS") networks grow they require more base stations to meet the demand for better connectivity, higher data rates and dependable high quality for cell phone service. Cellular infrastructure integrators and original equipment manufacturers, consisting of some of the world's largest telecommunications companies, are building out existing networks even as they develop new technologies for future systems.

In conjunction with its European subsidiary, Gillam-FEI, the Company has developed state-of-the-art network synchronization equipment. These products are intended to provide synchronization and timing references for communication and enterprise networks within the U.S. and overseas.

**GILLAM-FEI SEGMENT:**

Gillam-FEI extends the Company's competencies into network synchronization, network management, and specialized test equipment. With the advent of new digital broadband transmission technologies, reliable synchronization remains the warranty to quality of service for telecommunications operators. Gillam-FEI is among the world leaders in the field of wireline synchronization technology and its products are targeted for telecommunication operators and network equipment manufacturers that utilize modular and flexible platforms to build reliable digital-network-systems worldwide. Telecommunications operators such as Belgacom, France Telecom, Telefonica and other service providers are among Gillam-FEI's major customers. Gillam-FEI also provides ancillary products intended for deployment in the European, Middle Eastern, Asian and African markets. Included in its family of products is a remote terminal unit ("GRTU") that Gillam-FEI developed in concert with a major French electric utility company. The GRTU is intended to monitor the electrical current in a power grid and relay the information to a central location. Gillam-FEI intends to market this product to other electric utility companies in projects to create "smart" grids.

**FEI-ZYFER SEGMENT:**

FEI-Zyfer designs, develops and manufactures products for precision time and frequency generation and synchronization, primarily incorporating GPS technology. FEI-Zyfer's products make use of both "in-the-clear" civil and "crypto-secured" military signals from GPS. In most cases, FEI-Zyfer's products are integrated into communications systems, computer networks, test equipment, and military command and control terminals for ground and satellite link applications. More than 60% of revenues are derived from sales where the end user is the U.S. Government. FEI-Zyfer's products are an important extension of FEI's core product line, specifically in the area of GPS capabilities. In addition, FEI-Zyfer provides sales and support for the Company's family of wireline telecommunications and derivative products.

**BACKLOG**

As of April 30, 2013, the Company's consolidated backlog amounted to approximately \$51 million compared to approximately \$57 million at the end of the prior fiscal year. Approximately 70% of the current backlog is expected to be filled during the Company's fiscal year ending April 30, 2014. Included in the backlog at April 30, 2013 is approximately \$700,000 under cost-plus-fee contracts which the Company believes represent firm commitments from its customers for which the Company has not received full funding to date. The Company excludes from backlog any contracts or awards for which it has not received authorization to proceed. On fixed price contracts, the Company excludes any unfunded portion which, as of April 30, 2013, was approximately \$3 million. The Company expects these contracts to become fully funded over time and will be added to its backlog at that time. The backlog is subject to change by reason of several factors including possible cancellation of orders, change orders, terms of the contracts and other factors beyond the Company's control. Accordingly, the backlog is not necessarily indicative of the revenues or profits (losses) which may be realized when the results of such contracts are reported.

**CUSTOMERS AND SUPPLIERS**

The Company markets its products both directly and through approximately 30 independent sales representative organizations located in the U.S., Europe and Asia. Sales to non-U.S. end-users, including the revenues of its overseas subsidiaries, totaled approximately 26% and 33% of net revenues in fiscal years 2013 and 2012, respectively.

The Company's products are sold to both commercial and governmental customers. For the years ended April 30, 2013 and 2012, approximately 62% and 46%, respectively, of the Company's sales were made under contracts to the U.S. Government or subcontracts for U.S. Government end-use.

During fiscal year 2013 and 2012, Northrop Grumman Corporation ("Northrop"), Boeing Corporation ("Boeing") and Thales Alenia Space each accounted for more than 10% of consolidated and FEI-NY segment revenues.

During fiscal years 2013 and 2012, Belgacom was a major customer of the Gillam-FEI segment, accounting for more than 10% of that segment's revenues each year.

During fiscal year 2013, AT&T and Raytheon Corporation were major customers of the FEI-Zyfer segment as each accounted for more than 10% of the segment's revenues. During fiscal year 2012, AT&T accounted for more than 10% of FEI-Zyfer's revenues.

The loss by the Company of any one of these customers could have a material adverse effect on the Company's business. The Company believes its relationship with these companies to be mutually satisfactory and is not aware of any prospect for the cancellation or significant reduction of any of its commercial or existing U.S. Government contracts.

The Company purchases a variety of components such as transistors, resistors, capacitors, connectors and diodes for use in the manufacture of its products. The Company is not dependent upon any one supplier or source of supply for any of its component part purchases and maintains alternative sources of supply for all of its purchased components. The Company has found its suppliers generally to be reliable and price-competitive.

#### RESEARCH AND DEVELOPMENT

The Company's technological leadership continues to be an important factor to support future growth in revenues and earnings. The Company has focused its internal research and development efforts on improving the core physics and electronic packages in its time and frequency products, conducting research to develop new time and frequency technologies, improving product manufacturability by seeking to reduce its production costs through product redesign and process improvements and other measures to take advantage of lower cost components.

The Company continues to focus a significant portion of its own resources and efforts on developing hardware for satellite (commercial and U.S. Government) and terrestrial commercial communications systems, including wireless, wireline and GPS-related systems. During fiscal years 2013 and 2012, the Company expended \$5.7 million and \$3.9 million of its own funds, respectively, on such research and development activity. See "Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations." During fiscal years 2013 and 2012, many of the Company's development resources were applied to certain cost-plus-fee contracts and the design-stage of fixed-price satellite payload programs. As a result, some of the Company's development efforts were customer-funded and the costs appear in cost of revenues resulting in reduced internal research and development spending. For fiscal year 2014, the Company is targeting to spend between \$5.0 million and \$6.0 million on internal research and development projects. The actual amount spent in fiscal year 2014 will depend on market conditions and identification of new opportunities.

#### PATENTS AND LICENSES

The Company believes that its business is generally not dependent on patent or license protection. Rather, it is primarily dependent upon the Company's technical competence, the quality of its products and its prompt and responsible contract performance. However, employees working for the Company assign all rights to inventions to the Company and the Company presently holds such patents and licenses. In certain limited circumstances, the U.S. Government may use or permit the use by the Company's competitors of certain patents or licenses the government has funded. During fiscal year 2003, the Company received a broad and significant patent for new, proprietary quartz oscillator technology which the Company intends to exploit in both legacy and new applications. In 2006, the Company obtained a basic patent for its low g-sensitivity technology which management believes will permit greatly enhanced performance of devices on moving platforms and under externally imposed shock or vibration.

#### COMPETITION

The Company experiences competition in all areas of its business. Many of the Company's competitors are larger, have greater financial resources and have larger research and development and marketing staffs. The Company has a strong history of competing successfully in this environment due to the quality, reliability and outstanding record of performance its products have achieved. The Company competes primarily on the basis of the accuracy, performance and reliability of its products, the ability of its products to function under severe conditions, in space or in extreme hostile environments, prompt and responsive contract performance and technical competence. The Company has a unique and broad product line which includes quartz, rubidium, and cesium based timing references and specialized RF

microwave technology. On very high precision products, the Company encounters fewer competitors than for lower precision products for which there are a significant number of suppliers.

The Company's principal competition for space products is the in-house capability of its major customers such as the Boeing Corporation, Northrop Grumman, Lockheed Martin and Space Systems Loral as well as a number of other firms capable of providing high-reliability microwave frequency generators. With respect to non-space products, instruments and systems for timing and synchronization, the Company competes with large domestic companies such as Agilent Technologies, EG&G, Inc., Symmetricom, Inc., and Vectron, Inc., a division of Dover Corp. The Company also competes against multiple foreign entities including Indian, Korean and other Far East enterprises such as the Chinese company, Huawei. In Europe large competitors include Siemens, Schneider Electric and Oscilloquartz, a division of Swatch.

The Company has successfully outsourced certain manufacturing processes to third parties and to its wholly-owned subsidiary, FEI-Asia in Tianjin, China and to Russian-based Morion, Inc., in which the Company is a minority shareholder. The Company conducts this outsourcing to maintain a competitive position on cost while adhering to its high quality standards. The Company believes its ability to obtain raw materials, manufacture finished products, integrate them into systems and sub-systems and interface these systems with highly sophisticated end-user applications provides a strong competitive edge.

#### EMPLOYEES

The Company employs approximately 420 full-time persons worldwide. None of the U.S., European or Chinese employees is represented by labor unions.

#### OTHER ASPECTS

The Company's business is not seasonal although it expects to experience some fluctuation in revenues during the second fiscal quarter as a result of summer holiday periods. No unusual working capital requirements exist.

#### EXECUTIVE OFFICERS OF THE COMPANY

The executive officers hold office until the annual meeting of the Board of Directors following the annual meeting of stockholders, subject to earlier removal by the Board of Directors.

The names of all executive officers of the Company and all positions and offices with the Company which they presently hold are as follows:

Joseph P. Franklin	-	Chairman of the Board of Directors
Martin B. Bloch	-	President, Chief Executive Officer and Director
Markus Hechler	-	Executive Vice President, President of FEI Government Systems, Inc. and Assistant Secretary
Oleandro Mancini	-	Senior Vice President, Business Development
Steven Strang	-	President, FEI-Zyfer
Leonard Martire	-	Vice President, Program Management
Thomas McClelland	-	Vice President, Advanced Development
Adrian Lalicata	-	Vice President, RF & Microwave Systems
Alan Miller	-	Secretary/Treasurer and Chief Financial Officer

None of the officers and directors is related.

Joseph P. Franklin, age 79, has served as a Director of the Company since March 1990. In December 1993 he was elected Chairman of the Board of Directors. He also served as Chief Executive Officer from December 1993 through October 1998 and as Chief Financial Officer from September 1996 through October 1998. From August 1987 to November 1993, he was the Chief Executive Officer of Franklin S.A., a Spanish business consulting company located in Madrid, Spain, specializing in joint ventures, and was a director of several prominent Spanish companies. General Franklin was a Major General in the U.S. Army until he retired in July 1987.

Martin B. Bloch, age 77, has been a Director of the Company and of its predecessor since 1961. Mr. Bloch is the Company's President and Chief Executive Officer and has held such positions since

inception of the Company, except for the period from December 1993 through October 1998 when General Franklin held the CEO position. Previous to forming the Company, Mr. Bloch served as chief electronics engineer of the Electronics Division of Bulova Watch Company.

Markus Hechler, age 67, joined the Company in 1967. He was elected to the position of Executive Vice President in February 1999, prior to which he served as Vice President, Manufacturing since 1982. In October 2001, he was named President of the Company's subsidiary, FEI Government Systems, Inc. He has served as Assistant Secretary since 1978.

Oleandro Mancini, age 64, joined the Company in August 2000 as Vice President, Business Development and was promoted to Senior Vice President in 2010. Prior to joining the Company, Mr. Mancini served from 1998 as Vice President, Sales and Marketing at Satellite Transmission Systems, Inc. and from 1995 to 1998 as Vice President, Business Development at Cardion, Inc., a Siemens A.G. company. From 1987 to 1995, he held the position of Vice President, Engineering at Cardion, Inc.

Steven Strang, age 49, was named President of FEI-Zyfer, Inc., effective May 1, 2005. Previously, Mr. Strang was Executive Vice President of this subsidiary and its predecessor companies where he has served for 19 years in various technical and management positions.

Leonard Martire, age 76, joined the Company in August 1987 and served as Executive Vice President of FEI Microwave, Inc., the Company's wholly-owned subsidiary, until May 1993 when he was elected Vice President, Marketing and Sales. In fiscal year 2007, Mr. Martire assumed the role of Vice President Program Management.

Thomas McClelland, age 58, joined the Company as an engineer in 1984 and was elected Vice President, Commercial Products in March 1999. In fiscal year 2011, Mr. McClelland's title was modified to Vice President Advanced Development to describe his expanded role in the Company.

Adrian Lalicata, age 66, joined the Company in 2006 as Vice President, RF & Microwave Systems. Prior to joining the Company, Mr. Lalicata served as Vice President of Engineering at Herley-CTI and Communication Techniques, a Dover Company. Mr Lalicata has served as Director of Engineering at Microphase Corp. and Adcomm, Inc. He also held leading engineering positions at Loral Electronic Systems, Cardion Electronics, and Airborne Instruments Laboratories.

Alan Miller, age 64, joined the Company in November 1995 as its corporate controller and was elected to the position of Treasurer and Chief Financial Officer in October 1998. In May 2010, Mr. Miller was also named corporate Secretary. Prior to joining the Company, Mr. Miller served as an operations manager and a consultant to small businesses from 1992 through 1995 and as a Senior Audit Manager with Ernst & Young, L.L.P. from 1980 to 1991.

## Item 2. Properties

The Company operates out of several facilities located around the world. Each facility is used for manufacturing its products and for administrative activities. The following table presents the location, size and terms of ownership/occupation:

<u>Location</u>	<u>Size (sq. ft.)</u>	<u>Own or Lease</u>
Long Island, NY	93,000	Lease
Garden Grove, CA	27,850	Lease
Liege, Belgium	34,000	Own
Chalon Sur Saone, France	5,000	Lease
Tianjin, China	28,000	Lease
Rockleigh, NJ	32,000	Lease

The Company's facility located in Mitchel Field, Long Island, New York, is part of the building that the Company constructed in 1981 and expanded in 1988 on land leased from Nassau County. In January 1998, the Company sold this building and the related land lease to Reckson Associates Realty Corp. ("Reckson"), leasing back the space that it presently occupies.

The Company leased its manufacturing and office space from Reckson under an initial 11-year lease. The Company has exercised its option to renew the lease for an additional 5-year period at an annual rental of \$600,000 per year with the Company paying its pro rata share of real estate taxes along with the costs of utilities and insurance. During fiscal year 2013, the Company renewed the lease with Reckson for the second 5-year renewal period at an annual rental of \$800,000 to begin in February 2014. The lease will end in January 2019. The leased space is adequate to meet the Company's domestic operational needs which encompass the principal operations of the FEI-NY segment and also serves as the Company's world-wide corporate headquarters.

The Garden Grove, California facility is leased by the Company's subsidiary, FEI-Zyfer, Inc. The facility consists of a combination office and manufacturing space. The lease, which expires in August 2017, currently requires monthly payments of \$28,700 and will increase each year over the remaining 52 months of the lease term.

The Company's subsidiary, Gillam-FEI, owns a manufacturing and office facility in Liege, Belgium. Gillam-FEI's French operation leases space in Chalon Sur Saone, France. These facilities are adequate to meet the present and future operational requirements of Gillam-FEI.

The Tianjin, China facility is the location of the Company's wholly-owned subsidiary, FEI-Asia. The subsidiary's office and manufacturing facility is located in the Tianjin Free-Trade Zone. The lease is renewable annually with monthly rent of \$6,800 through February 2014. The facility is adequate for the near-term manufacturing expectations for the Company.

FEI-Elcom operates out of a leased facility located in Rockleigh, New Jersey. The facility consists of a combination office and manufacturing space. The lease, which expires in March 2016, requires monthly payments of \$26,700.

### Item 3. Legal Proceedings

From time to time, the Company is a defendant in litigation arising out of the ordinary course of business. As of July 22, 2013, the Company is not a party to any material, pending legal proceeding other than routine litigation incidental to its business.

## PART II

### Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

The Common Stock of the Company is listed on The Nasdaq Global Market ("NASDAQ") under the ticker symbol "FEIM." The following table shows the high and low sale price for the Company's Common Stock for the quarters indicated, as reported on the NASDAQ.

<u>FISCAL QUARTER</u>	<u>HIGH SALE</u>	<u>LOW SALE</u>
2013—		
FIRST QUARTER	\$ 9.50	\$ 7.02
SECOND QUARTER	9.74	8.39
THIRD QUARTER	9.88	6.71
FOURTH QUARTER	10.25	8.52
2012 –		
FIRST QUARTER	\$11.79	\$ 8.80
SECOND QUARTER	10.75	8.15
THIRD QUARTER	9.16	6.91
FOURTH QUARTER	8.89	7.28

As of July 22, 2013, the approximate number of holders of record of common stock was 700. The closing share price of the Company's stock on April 30, 2013 was \$10.02. The closing share price of the Company's stock on July 22, 2013 was \$10.60.

## DIVIDEND POLICY

The Board of Directors reviews the Company's dividend policy at each regular meeting. On December 12, 2012, the Company's Board of Directors declared a special cash dividend of \$0.20 per share, payable on December 31, 2012 to shareholders of record on December 24, 2012. Accordingly, the Company paid a cash dividend of \$1,684,000 during fiscal year 2013.

## STOCK BUYBACK PROGRAM

In March 2005, the Company's Board of Directors authorized a stock repurchase program for up to \$5 million of the Company's outstanding common stock. This program does not have an expiration date. Shares may be purchased in open market purchases, private transactions or otherwise at such times and from time to time, and at such prices and in such amounts as the Company believes appropriate and in the best interests of its shareholders. The timing and volume of repurchases will vary depending on market conditions and other factors. Purchases may be commenced or suspended at any time without notice. During fiscal year 2009, the Company repurchased 724,632 shares under the buyback program, including a block purchase of 615,000 shares from its former largest institutional shareholder. The average purchase price was \$4.29 per share or an aggregate amount of approximately \$3.1 million. With these purchases, the Company has acquired approximately \$4 million of its common stock out of the total authorization of \$5 million. The Company did not make any purchases of stock for the treasury during fiscal years 2013 or 2012.

## EQUITY COMPENSATION PLAN INFORMATION

<u>Plan Category</u>	<u>Number of securities to be issued upon exercise of outstanding options warrants and rights</u>	<u>Weighted-average exercise price of outstanding options warrants and rights</u>	<u>Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a))</u>
	<u>(a)</u>	<u>(b)</u>	<u>(c)</u>
Equity Compensation Plans			
Approved by Security Holders (1)	1,678,625	\$ 8.25	166,743
Equity Compensation Plans Not			
Approved by Security Holders (1)	<u>67,500</u>	\$10.27	<u>-</u>
TOTAL	<u>1,746,125</u>	<u>\$ 8.32</u>	<u>166,743</u>

(1) The Company's equity compensation plans are described in Note 12 of the Consolidated Financial Statements.

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

### **"Safe Harbor" Statement under the Private Securities Litigation Reform Act of 1995:**

The statements in this Annual Report on Form 10-K regarding future earnings and operations and other statements relating to the future constitute "forward-looking" statements pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. Forward-looking statements inherently involve risks and uncertainties that could cause actual results to differ materially from the forward-looking statements. Factors that would cause or contribute to such differences include, but are not limited to, inability to integrate operations and personnel, actions by significant customers or competitors, general domestic and international economic conditions, consumer spending trends, reliance on key customers, continued acceptance of the Company's products in the marketplace, competitive factors, new products and technological changes, product prices and raw material costs, dependence upon third-party vendors, competitive developments, changes in manufacturing and transportation costs, the availability of capital, and the outcome of any litigation and arbitration proceedings. The factors listed above are not

exhaustive. Other sections of this Form 10-K include additional factors that could materially and adversely impact the Company's business, financial condition and results of operations. Moreover, the Company operates in a very competitive and rapidly changing environment. New factors emerge from time to time and it is not possible for management to predict the impact of all these factors on the Company's business, financial condition or results of operations or the extent to which any factor, or combination of factors, may cause actual results to differ materially from those contained in any forward-looking statements. Given these risks and uncertainties, investors should not rely on forward-looking statements as a prediction of actual results. Any or all of the forward-looking statements contained in this Form 10-K and any other public statement made by the Company or its management may turn out to be incorrect. The Company expressly disclaims any obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

### **Critical Accounting Policies and Estimates**

The Company's significant accounting policies are described in Note 1 to the Consolidated Financial Statements. The Company believes its most critical accounting policies to be the recognition of revenue and costs on production contracts and the valuation of inventory. Each of these areas requires the Company to make use of reasonable estimates including estimating the cost to complete a contract, the realizable value of its inventory or the market value of its products. Changes in estimates can have a material impact on the Company's financial position and results of operations.

#### Revenue Recognition

Revenues under larger, long-term contracts which generally require billings based on achievement of milestones rather than delivery of product, are reported in operating results using the percentage of completion method. On fixed-price contracts, which are typical for commercial and U.S. Government satellite programs and other long-term U.S. Government projects, and which require initial design and development of the product, revenue is recognized on the cost-to-cost method. Under this method, revenue is recorded based upon the ratio that incurred costs bear to total estimated contract costs with related cost of sales recorded as the costs are incurred. Each month management reviews estimated contract costs through a process of aggregating actual costs incurred and estimating additional costs to completion based upon the current available information and status of the contract. The effect of any change in the estimated gross margin percentage for a contract is reflected in revenues in the period in which the change is known. Provisions for anticipated losses on contracts are made in the period in which they become determinable.

On production-type orders, revenue is recorded as units are delivered with the related cost of sales recognized on each shipment based upon a percentage of estimated final program costs.

Changes in job performance on long-term contracts and production-type orders may result in revisions to costs and income and are recognized in the period in which revisions are determined to be required. Provisions for anticipated losses on customer orders are made in the period in which they become determinable.

For customer orders in the Company's Gillam-FEI and FEI-Zyfer segments or smaller contracts or orders in the FEI-NY segment, sales of products and services to customers are reported in operating results based upon (i) shipment of the product or (ii) performance of the services pursuant to terms of the customer order. When payment is contingent upon customer acceptance of the installed system, revenue is deferred until such acceptance is received and installation completed.

#### Costs and Expenses

Contract costs include all direct material, direct labor costs, manufacturing overhead and other direct costs related to contract performance. Selling, general and administrative costs are charged to expense as incurred.

#### Inventory

In accordance with industry practice, inventoried costs contain amounts relating to contracts and programs with long production cycles, a portion of which will not be realized within one year. Inventory write downs are established for slow-moving materials, obsolete items and costs incurred on programs for which production-level orders cannot be determined as probable. Such write downs are based upon

management's experience and expectations for future business. Any changes arising from revised expectations are reflected in cost of sales in the period the revision is made.

#### Marketable Securities

All of the Company's investments in marketable securities are Level 1 securities which trade on public markets and have current prices that are readily available. In general, investments in fixed price securities are only in the commercial paper of financially sound corporations or the bonds of U.S. Government agencies. Although the value of such investments may fluctuate significantly based on economic factors, the Company's own financial strength enables it to wait for the securities to either recover their value or to mature such that any interim unrealized gains or losses are deemed to be temporary.

#### Impact of FEI-Elcom Acquisition

Fiscal year 2013 results include the results of operations of the Company's subsidiary, FEI-Elcom Tech, Inc. (formerly Elcom Technologies, Inc. or "Elcom" and after the acquisition, "FEI-Elcom"), which was acquired during the fourth quarter of fiscal year 2012. FEI-Elcom's operations are included in the FEI-NY segment. For the year ended April 30, 2013, FEI-Elcom's third-party revenues were approximately \$8.7 million and this subsidiary recorded an operating loss of approximately \$490,000. In the comparable twelve-month period of the prior fiscal year, including the periods before and after the acquisition, Elcom recorded revenues of approximately \$7.4 million, an operating loss of approximately \$660,000 and a net loss of approximately \$400,000. In the discussion below, all amounts for the year ended April 30, 2012, include FEI-Elcom only for the two and one-half months from the date of acquisition through the end of the fiscal year, with the exception of the Company's "Other income (expenses)" which includes a \$730,000 gain on its Elcom investment, a \$650,000 equity loss from the Company's minority interest in Elcom through the date of acquisition and a \$350,000 impairment charge against the Company's investment in Elcom and certain notes receivable from Elcom.

### **RESULTS OF OPERATIONS**

The table below sets forth for the fiscal years ended April 30, 2013 and 2012, the percentage of consolidated net sales represented by certain items in the Company's consolidated statements of operations:

	<u>2013</u>	<u>2012</u>
Revenues		
FEI-NY	76.3%	70.3%
Gillam-FEI	17.1	20.1
FEI-Zyfer	15.3	18.1
Less intersegment revenues	<u>(8.7)</u>	<u>(8.5)</u>
	100.0	100.0
Cost of Revenues	<u>63.6</u>	<u>61.3</u>
Gross Margin	36.4	38.7
Selling and Administrative expenses	21.3	22.1
Research and Development expenses	<u>8.3</u>	<u>6.1</u>
Operating Profit	6.8	10.5
Other Income (Expenses), net	0.6	0.2
(Provision) Benefit for Income Taxes	<u>(2.0)</u>	<u>0.9</u>
Net Income	<u>5.4%</u>	<u>11.6%</u>

## Revenues

	Fiscal years ended April 30, (in thousands)			
	<u>2013</u>	<u>2012</u>	<u>Change</u>	
			<u>\$</u>	<u>%</u>
FEI-NY	\$52,567	\$44,711	\$7,856	18%
Gillam-FEI	11,825	12,811	(986)	(8%)
FEI-Zyfer	10,523	11,494	(971)	(8%)
Intersegment sales	<u>(5,983)</u>	<u>(5,421)</u>	<u>(562)</u>	
	\$68,932	\$63,595	\$5,337	8%

### Fiscal year 2013 compared to fiscal year 2012:

For the year ended April 30, 2013, FEI-NY revenues from commercial and U.S. Government satellite programs increased 11% over the prior year. Revenues from these programs accounted for 50% of fiscal year 2013 consolidated sales, approximately the same ratio as for fiscal year 2012. Revenues on these long-term contracts are recognized primarily under the percentage of completion method. For the year ended April 30, 2013, sales from the non-space U.S. Government/DOD business area accounted for more than 25% of consolidated revenues and increased by more than 40% over fiscal year 2012. This increase is due to the impact of FEI-Elcom which was acquired by the Company in late fiscal year 2012 and is part of the FEI-NY segment. For the year ended April 30, 2013, total revenues from both satellite and non-space programs for which the U.S. Government is the end-user, accounted for approximately 60% of consolidated revenues compared to approximately 45% in the prior fiscal year. Such revenues are recorded in the FEI-Zyfer segment as well as FEI-NY (including FEI-Elcom). For the year ended April 30, 2013, network infrastructure sales, which are recorded in all three segments, accounted for approximately 17% of consolidated revenues as compared to approximately 20% of revenues in the prior fiscal year. Network infrastructure sales were 8% lower in fiscal year 2013 compared to fiscal year 2012 and is the partial cause of decreased revenue at the FEI-Zyfer and Gillam-FEI segments. The decline in revenues at the Gillam-FEI segment is also partially attributable to a 6% year-over-year decrease in the rate of exchange between the U.S. dollar and the euro. The revenue decline at FEI-Zyfer is also due to delays in orders from U.S. Government customers as a result of recent U.S. budget issues.

### Fiscal year 2012 compared to fiscal year 2011:

The 20% increase in consolidated revenues in fiscal year 2012 over the prior year is primarily due to satellite payload revenues generated by the FEI-NY segment. For the year ended April 30, 2012, revenues from commercial and U.S. Government satellite programs accounted for approximately half of consolidated revenues compared to approximately 30% of revenues during fiscal year 2011. Revenues on these long-term contracts are recognized primarily under the percentage of completion method. Fiscal year 2012 revenues from FEI-Elcom, after the acquisition, were less than \$1.0 million and are included in the FEI-NY segment's revenues. Increased network infrastructure revenues generated by the FEI-Zyfer segment were offset by declines in that business area in the Gillam-FEI segment and lower wireless infrastructure sales in the FEI-NY segment. Network infrastructure revenues were less than 20% of consolidated revenues for the year ended April 30, 2012 compared to approximately 25% for fiscal year 2011. In fiscal year 2012, revenues from the non-space U.S. Government/DOD business area, which are recorded in the FEI-NY and FEI-Zyfer segments, were approximately 20% of consolidated revenues compared to 25% for fiscal year 2011. Fiscal year 2012 revenues were lower due to completion of certain long-term programs and delays in new program awards.

Based on the Company's current backlog, over three-fourths of which represent satellite payload business, and the potential for additional new orders, fiscal year 2014 revenues are expected to grow. Satellite payload revenues will remain the dominant portion of the Company's business and represent the Company's best opportunity for long-term growth, benefiting from both commercial and U.S. Government programs. Fiscal year 2014 revenues from the other major business areas, U.S. Government/DOD non-space and network infrastructure, are expected to remain in approximately the same range as realized in fiscal year 2013.

## Gross Margin

Fiscal years ended April 30,  
(in thousands)

	<u>2013</u>	<u>2012</u>	<u>Change</u>	
			<u>\$</u>	<u>%</u>
	\$25,110	\$24,618	\$492	2%
GM Rate	36.4%	38.7%		

For each of the years ended April 30, 2013 and 2012, gross margin increased as a result of increased revenues. In the fourth quarter of fiscal year 2013 gross margin was reduced by \$1.4 million (2% of consolidated revenues) as a result of the write down of certain inventory recorded in the Gillam-FEI segment due to lack of certainty regarding the realizability of such inventory. Based on slower than anticipated rollout of implementation of the French government's plans to initiate a "smart grid," the Company has less visibility regarding the probable schedule for obtaining production-level orders which are now anticipated to occur no earlier than fiscal year 2015. Improved gross margins from satellite payload revenues in the FEI-NY segment were offset by historically lower gross margins at FEI-Elcom. Gross margin rates in the FEI-Zyfer and Gillam-FEI segments were also lower on reduced sales. For fiscal year 2012, the gross margin rate improved over the 37.5% rate recorded in the prior fiscal year. The largest gross margin rate improvement during fiscal year 2012 occurred in the Company's FEI-NY segment as a higher volume of business covered more of that segment's fixed costs. During the fiscal year ended April 30, 2013, cost of sales included approximately \$2.4 million of inventory write downs, including the Gillam-FEI inventory write down. During fiscal year 2012, cost of sales included increases to warranty reserves and inventory write downs which aggregated approximately \$1.1 million. These charges reduced gross margin rates by 3.4% in fiscal year 2013 and by 1.8% in fiscal year 2012. Fiscal year 2012 gross margin was also reduced by the fourth quarter acquisition of FEI-Elcom whose operating results are included in the FEI-NY segment. With the current mix of programs and orders in its backlog, the Company expects its gross margin rate to approach its target rate of 40%. As revenues increase in future periods, the Company expects to realize a higher gross margin as more of its fixed costs are covered.

## Selling and Administrative Expenses

Fiscal years ended April 30,  
(in thousands)

	<u>2013</u>	<u>2012</u>	<u>Change</u>	
			<u>\$</u>	<u>%</u>
	\$14,704	\$14,055	\$649	5%

In the fiscal years ended April 30, 2013 and 2012, selling and administrative costs were 21% and 22%, respectively, of consolidated revenues. Fiscal year 2013 expenses include a full year of selling and administrative expenses incurred by FEI-Elcom. For the years ended April 30, 2013 and 2012, selling and administrative expenses include stock compensation expense of \$538,000 and \$359,000, respectively. Fiscal year 2012 expenses also include approximately \$230,000 of transaction costs related to the FEI-Elcom acquisition as well as approximately \$140,000 related to a stock award to the Company's employees in celebration of its 50th anniversary. The Company expects fiscal year 2014 selling and administrative expenses to be incurred at approximately the same rate relative to revenues.

## Research and Development Expenses

Fiscal years ended April 30,  
(in thousands)

	<u>2013</u>	<u>2012</u>	<u>Change</u>	
			<u>\$</u>	<u>%</u>
	\$5,727	\$3,860	\$1,867	48%

Research and development ("R&D") expenditures represent investments intended to keep the Company's products at the leading edge of time and frequency technology and enhance competitiveness for future revenues. R&D spending for the year ended April 30, 2013 was approximately 8% of revenues compared to approximately 6% of revenues for fiscal year 2012. Approximately half of the increased

R&D spending in fiscal year 2013 was due to product development expenditures at recently acquired FEI-Elcom on its own product line. Additionally, the FEI-NY segment, including engineering resources at FEI-Elcom, accelerated development of new satellite payload microwave receivers/converters from DC to Ka band, development and improvement of miniaturized rubidium atomic clocks, development of new GPS-based synchronization products and further enhancement of the capabilities of its line of low g-sensitivity and ruggedized rubidium oscillators. The lower rate and lower R&D expenditures in fiscal year 2012 were due primarily to the dedication of resources to customer-funded programs rather than to internal R&D programs. Some customer-funded development activity continued into fiscal year 2013 but with the added resources from FEI-Elcom, the Company spent more on internal R&D. The costs of customer-funded development efforts appear in cost of revenues, thus reducing the level of internal R&D spending. Although funding is obtained from customers, the Company retains the rights to any products developed. The Company will continue to devote significant resources to develop new products, enhance existing products and implement efficient manufacturing processes. For fiscal year 2014, the Company anticipates that internal research and development spending will be less than 10% of revenues. The Company believes that internally generated cash and cash reserves are adequate to fund these development efforts.

### **Operating Profit**

Fiscal years ended April 30,  
(in thousands)

			<u>Change</u>	
<u>2013</u>	<u>2012</u>	<u>\$</u>	<u>%</u>	
\$4,679	\$6,703	(\$2,024)	(30%)	

For the year ended April 30, 2013, operating profit was reduced by the \$1.4 million inventory write down in the Gillam-FEI segment, higher selling and administrative costs and increased R&D spending. All of the fiscal year 2013 operating profit was generated by the FEI-NY segment which enjoyed the benefit of rising satellite payload revenues. The Company's other segments, FEI-Zyfer and Gillam-FEI, both incurred operating losses on reduced revenues, higher costs and the inventory write down.

For the year ended April 30, 2012, higher revenues, improved gross margin rates and operating expenses in line with expectations enabled the Company to record an operating profit that was nearly twice the operating profit recorded in the preceding fiscal year. On a segment basis, the operating profit of FEI-NY increased as a result of a 35% increase in revenues and improved gross margin rates. The fiscal year 2012 operating profit at Gillam-FEI was favorably impacted by an improved product mix despite lower revenues than for fiscal year 2011. FEI-Zyfer realized an operating loss due to lower gross margins partially due to increased warranty reserves as well as product mix.

On anticipated increased revenues and favorable product mix, the Company expects to realize an improved gross margin while maintaining other operating expenses within their targeted amounts. Thus, the Company expects to report higher operating profits in fiscal year 2014.

### **Other Income (Expense)**

Fiscal years ended April 30,  
(in thousands)

			<u>Change</u>	
<u>2013</u>	<u>2012</u>	<u>\$</u>	<u>%</u>	
Investment income	\$ 671	\$ 646	\$ 25	4%
Gain on investment in affiliate	-	730	(730)	NM
Equity loss	-	(650)	650	NM
Impairment charge	-	(350)	350	NM
Interest expense	(195)	(121)	(74)	(61%)
Other expense, net	<u>(69)</u>	<u>(144)</u>	<u>75</u>	52%
	\$407	\$111	\$ 296	267%

Investment income includes interest and dividend income on marketable securities. Earnings on these securities may vary based on fluctuating dividends and interest rates and the timing of purchases or sales of securities. During the year ended April 30, 2012, the Company broadened its investment

portfolio to include higher yielding marketable securities thus generating greater investment income than in fiscal year 2011. During fiscal years 2013 and 2012, investment income included gains upon the sale or redemption of marketable securities of approximately \$46,000 and \$20,000, respectively. During fiscal year 2014, the Company anticipates that investment income will be approximately the same as that earned in fiscal year 2013, depending on the yield of its investment portfolio.

The fiscal year 2012 step acquisition of FEI-Elcom resulted in the recognition of a gain of approximately \$730,000. Equity losses of \$650,000 represent the Company's share of the losses recorded by FEI-Elcom prior to the Company's fiscal year 2012 fourth quarter acquisition of that company. See "NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - 11. Acquisition of Elcom Technologies, Inc. In addition, during the second quarter of fiscal year 2012, based on comparisons to comparable companies as well as FEI-Elcom's forecasts of future financial results, the Company recorded an impairment charge in the amount of \$350,000. Since FEI-Elcom is a wholly-owned subsidiary of the Company for all of fiscal year 2013, there is no comparable income or expense items for the year ended April 30, 2013.

In fiscal years 2013 and 2012, interest expense was incurred on borrowings under short-term credit obligations, on deferred compensation payments and capital leases for equipment. During the year ended April 30, 2012, to complete the acquisition of FEI-Elcom, the Company decided to draw on its bank line of credit rather than liquidate any of its investment in marketable securities. In addition, subsequent to April 30, 2013, the Company established a five-year, \$25 million credit facility with a bank, replacing the previous \$9.3 million credit line. As a result of the new credit facility, the Company expects to maintain a higher level of debt and anticipates that interest expense in fiscal year 2014 will be higher than that incurred in fiscal year 2013.

Other expenses for the year ended April 30, 2013, consists primarily of an uninsured loss sustained by the Company's Gillam-FEI segment. For the year ended April 30, 2012, other expenses consisted primarily of amortization of certain non-operating assets that was partially offset by gains of approximately \$137,000 derived from the excess of proceeds over the cash values of life insurance policies covering a former employee. The Company anticipates that in future years items in this category will not be significant to pretax earnings.

**Income Tax Provision (Benefit)**

Fiscal years ended April 30, (in thousands)			
		<u>Change</u>	
<u>2013</u>	<u>2012</u>	<u>\$</u>	<u>%</u>
\$1,400	(\$560)	\$1,960	NM

During the year ended April 30, 2013, certain tax law changes were enacted which enabled the Company to obtain larger federal tax credits. The changes reduced the Company's effective tax rate on pre-tax income to 27.5%.

During the fourth quarter of fiscal year 2012, the Company reduced its valuation allowance against deferred tax assets in the amount of \$3.1 million. This reduction was based on a review of all available evidence, both positive and negative, and management's assessment that it is more likely than not that it will be able to realize the tax benefits from the future deductibility of most items included in its deferred tax assets. Excluding the valuation allowance reduction, for the year ended April 30, 2012, the Company recorded a net tax provision of \$2.5 million or an effective tax rate of 37%. The Company is subject to taxation in several countries. The statutory federal rates are 34% in the U.S., 33% in Europe and 25% in China. The Company utilizes the availability of research and development tax credits in the U.S. to lower its tax rate. The actual rate incurred may be impacted by the non-deductibility of losses incurred in overseas operations. (See Note 13 to the Consolidated Financial Statements for a reconciliation of the actual tax benefit to the expected tax provision at the federal statutory rate.)

The Company's European subsidiaries have available net operating loss ("NOL") carryforwards of approximately \$2.7 million to offset future taxable income. The associated deferred tax asset for the foreign subsidiary NOL is fully reserved by the deferred tax valuation allowance. These loss carryforwards have no expiration date. As a result of the acquisition of FEI-Elcom, the Company has a

federal NOL carryforward of \$6.6 million which may be applied in annually limited amounts to offset future U.S.-sourced taxable income over the next 19 years.

## **LIQUIDITY AND CAPITAL RESOURCES**

The Company's balance sheet continues to reflect a highly liquid position with working capital of \$71.7 million at April 30, 2013. Included in working capital at April 30, 2013 is \$21.7 million consisting of cash, cash equivalents and short-term investments. The Company's current ratio at April 30, 2013 is 8.7 to 1 compared to 4.9 to 1 at the end of the prior fiscal year.

Net cash provided by operating activities for the year ended April 30, 2013, was \$2.8 million compared to \$2.1 million for the prior fiscal year. During fiscal years 2013 and 2012, the Company incurred \$6.5 million and \$5.8 million, respectively, in non-cash charges to earnings, including depreciation and amortization expense, inventory write downs, warranty and accounts receivable reserves, certain employee benefit plan expenses, including accounting for stock-based compensation and, in fiscal year 2012, the equity loss on its Elcom investment net of the gain on that investment. In fiscal year 2012, such non-cash charges were partially offset by the non-cash benefit of \$3.1 million resulting from the Company's reduction of a portion of the valuation allowance on its deferred tax assets. For fiscal year 2013, operating cash was reduced by increases to inventories and payment of estimated income taxes. For fiscal year 2012, operating cash was reduced by increases to accounts receivable and inventory. In fiscal year 2014, the Company anticipates that it will maintain positive cash flow from operations by continuing to generate operating profits.

Net cash used in investing activities was \$2.0 million and \$8.0 million, respectively, for the fiscal years ended April 30, 2013 and 2012. The fiscal year 2013 activities consisted of net proceeds from marketable securities transactions of \$170,000 and acquisitions of capital equipment for \$2.2 million. In fiscal year 2012, investing activities included the additional investment in FEI-Elcom for \$4.5 million, net of acquired cash of \$763,000, net purchase of marketable securities for \$2.1 million and the acquisition of capital equipment for \$1.4 million. The Company may continue to invest cash equivalents in longer-term securities or to convert short-term investments to cash equivalents as dictated by its investment and acquisition strategies. The Company will continue to acquire more efficient equipment to automate its production process. The Company intends to spend between \$2.0 million and \$3.0 million on capital equipment during fiscal year 2014. Internally generated cash is expected to be adequate to acquire this property, plant and equipment.

Through April 30, 2013, the Company had a \$9.3 million line of credit with the financial institution that also managed a substantial portion of its investment in marketable securities. Rather than liquidate some of these investments to meet short-term working capital requirements, the Company borrowed against the line of credit at variable interest rates which averaged approximately 1.75%, which is less than the return on the Company's portfolio of marketable securities that secured the line. To fund the acquisition of FEI-Elcom during fiscal year 2012, the Company borrowed \$6.0 million. During the year ended April 30, 2013, the Company borrowed additional money for working capital purposes and subsequently repaid such borrowing such that by April 30, 2013, the outstanding principal balance was \$6.0 million. During fiscal year 2013, the highest level of borrowing under this line was \$8.5 million. Following the end of fiscal year 2013, the Company obtained a five-year, \$25 million credit facility from a bank and repaid the credit line from the previous financial institution. The Company thus converted the short-term debt obligation into a longer-term loan. The Company will draw on this new credit facility to provide additional working capital and to fund acquisitions. The interest rate on the new facility is based on LIBOR plus either 75 basis points or 175 basis points depending on under which of the two tranches the Company chooses to borrow. For a more complete description of the new credit facility, see "NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - 7. Debt Obligations and Subsequent Event. In addition, the Company's European subsidiaries have available approximately \$650,000 in bank credit lines to meet short-term cash flow requirements. The rate of interest on these borrowings is based on the one month EURO Interbank Offered Rate (EURIBOR). The European subsidiaries borrowed against these lines of credit during fiscal years 2013 and 2012 but repaid the obligations during each year.

During the year ended April 30, 2013, cash used in financing activities was \$1.9 million. The Company borrowed and repaid \$5.0 million under the previous credit line and made payments on capital lease obligations in the amount of \$357,000. In addition, during the third quarter of fiscal year 2013, the Company paid a special cash dividend of \$1.7 million. Partially offsetting these financing cash outflows,

the Company also received \$172,000 upon the exercise of stock-based awards and the tax benefit arising from such exercises. During fiscal year 2012, cash provided by financing activities was \$5.7 million consisting of borrowings under its lines of credit of \$6.3 million and reduced by repayment of short-term borrowings and capital lease obligations in the amount of \$660,000. The Company will continue to use treasury shares to satisfy the future exercise of stock options and stock appreciation rights granted to officers and employees. The Company has been authorized by its Board of Directors to repurchase up to \$5 million worth of shares of its common stock for treasury whenever appropriate opportunities arise but it has neither a formal repurchase plan nor commitments to purchase additional shares in the future. As of the end of fiscal year 2013, the Company has repurchased approximately \$4 million of its common stock out of the \$5 million authorization.

The Company will continue to expend resources to develop, improve and acquire products for space applications, guidance and targeting systems, and communication systems which management believes will result in future growth and continued profitability. During fiscal year 2014, the Company intends to make a substantial investment of capital and technical resources to develop and acquire new products to meet the needs of the U.S. Government, commercial space and network infrastructure marketplaces and to invest in more efficient product designs and manufacturing procedures. Where possible, the Company will secure partial customer funding for such development efforts but is targeting to spend its own funds at a rate of approximately 10% of revenues to achieve its development goals. Internally generated cash will be adequate to fund these development efforts. The Company may also pursue acquisitions to expand its range of products and may use internally generated cash and external funding in connection with such acquisitions.

#### **Off-Balance Sheet Arrangements**

The Company does not have any off-balance sheet arrangements, other than operating leases, that have or are reasonably likely to have a current or future effect on the Company's financial condition, changes in financial condition, revenues or expenses, results of operations, liquidity, capital expenditures or capital resources that is material to investors.

As of April 30, 2013, the Company's consolidated backlog amounted to approximately \$51 million as compared to approximately \$57 million at the beginning of the fiscal year. (See Item 1). Approximately 70% of this backlog is expected to be filled during the Company's fiscal year ending April 30, 2014. Included in the backlog at April 30, 2013 is approximately \$700,000 under cost-plus-fee contracts which the Company believes represent firm commitments from its customers for which the Company has not received full funding to date. The Company excludes from backlog any contracts or awards for which it has not received authorization to proceed. On fixed price contracts, the Company excludes any unfunded portion which, as of April 30, 2013, was approximately \$3 million. The Company expects these contracts to become fully funded over time and will be added to its backlog at that time. The backlog is subject to change by reason of several factors including possible cancellation of orders, change orders, terms of the contracts and other factors beyond the Company's control. Accordingly, the backlog is not necessarily indicative of the revenues or profits (losses) which may be realized when the results of such contracts are reported.

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The Company's liquidity is adequate to meet its operating and investment needs through at least April 30, 2014.

#### **RECENT ACCOUNTING PRONOUNCEMENTS**

In June 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2011-05 "Comprehensive Income (Topic 220): Presentation of Comprehensive Income" ("ASU No. 2011-05"). Under ASU No. 2011-5, an entity has the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. Regardless of which option is selected, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. ASU No. 2011-5 eliminates the option (previously utilized by the Company) to present the components of other

comprehensive income as part of the statement of changes in stockholders' equity. ASU No. 2011-5 was adopted by the Company at the beginning of the current fiscal year, and affects only the presentation of financial statements and has no financial impact on the Company's Consolidated Financial Statements.

In September 2011, the FASB issued ASU No. 2011-08, *Testing Goodwill for Impairment*" ("ASU No. 2011-08"), which is intended to reduce the complexity and costs to test goodwill for impairment. The amendment allows an entity the option to make a qualitative evaluation about the likelihood of goodwill impairment to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. An entity will no longer be required to calculate the fair value of a reporting unit unless the entity determines, based on its qualitative assessment, that it is more likely than not that the fair value of the reporting unit is less than its carrying amount. ASU No. 2011-08 also expands upon the examples of events and circumstances that an entity should consider between annual impairment tests in determining whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. The amendment became effective for annual and interim goodwill impairment tests performed by the Company in the fourth quarter of the fiscal year ended April 30, 2012. The adoption of ASU 2011-08 did not have a material impact on its consolidated financial statements.

In February 2013, the FASB issued Accounting Standard Update No. 2013-02, *Other Comprehensive Income*. The amendments require an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under U.S. GAAP that provide additional detail about those amounts. This ASU is effective for periods beginning after December 15, 2012. The Company does not expect adoption of ASU 2013-02 to have a material effect on its financial statements.

In July 2012, the FASB issued ASU No. 2012-02, *Intangibles – Goodwill and Other (Topic 350): Test Indefinite-Lived Intangible Assets for Impairment*. Under the requirements of ASU 2012-02 an entity has the option to assess qualitative factors when testing indefinite-lived intangible assets annually to determine whether it is more likely than not that the asset is not impaired. An entity also has the option to bypass the qualitative assessment for any indefinite-lived intangible asset in any period and proceed directly to performing the quantitative impairment test or resume performing the qualitative assessment in any subsequent period. If, after assessing the totality of events and circumstances, an entity concludes that it is more likely than not that the indefinite-lived intangible asset is impaired, then it is required to determine the fair value of the indefinite-lived intangible asset and perform the quantitative impairment test by comparing the fair value with the carrying amount in accordance with *Subtopic 350-30*. ASU 2012-02 is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. The Company will adopt ASU 2012-02 for its fiscal year 2014 which begins on May 1, 2013. The Company is unable to determine the impact of such adoption until it performs the annual test for impairment in the next fiscal year.

## **OTHER MATTERS**

The financial information reported herein is not necessarily indicative of future operating results or of the future financial condition of the Company. Except as noted, management is unaware of any impending transactions or internal events that are likely to have a material adverse effect on results from operations.

## **INFLATION**

During fiscal year 2013, as in fiscal year 2012, the impact of inflation on the Company's business has not been materially significant.

Item 8. Financial Statements and Supplementary Data

**REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM**

Board of Directors and Shareholders  
Frequency Electronics, Inc.

We have audited the accompanying consolidated balance sheets of Frequency Electronics, Inc. and subsidiaries (the "Company") as of April 30, 2013 and 2012, and the related consolidated statements of income and comprehensive income, cash flows and changes in stockholders' equity for each of the years in the two-year period ended April 30, 2013. The financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the 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 audits 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 financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the consolidated financial position of Frequency Electronics, Inc. and subsidiaries as of April 30, 2013 and 2012, and the consolidated results of their operations and their cash flows for each of the years in the two-year period ended April 30, 2013, in conformity with accounting principles generally accepted in the United States.

/s/ EisnerAmper LLP  
EisnerAmper LLP

New York, New York  
July 29, 2013

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

Consolidated Balance Sheets

April 30, 2013 and 2012

(In thousands, except par value)

<b>ASSETS:</b>	<u>2013</u>	<u>2012</u>
Current assets:		
Cash and cash equivalents	\$ 3,460	\$ 4,782
Marketable securities	18,270	17,658
Accounts receivable, net of allowance for doubtful accounts of \$288 in 2013 and \$400 in 2012	7,781	10,866
Costs and estimated earnings in excess of billings, net	8,617	7,207
Inventories, net	37,521	34,299
Deferred income taxes	3,170	3,152
Prepaid income taxes	680	-
Prepaid expenses and other	1,517	1,398
Total current assets	<u>81,016</u>	<u>79,362</u>
Property, plant and equipment, at cost, net of accumulated depreciation and amortization	8,316	8,374
Deferred income taxes	6,320	5,692
Goodwill and other intangible assets	781	873
Cash surrender value of life insurance and cash held in trust	10,763	10,133
Other assets	1,713	1,793
<b>Total assets</b>	<b><u>\$108,909</u></b>	<b><u>\$106,227</u></b>
<b>LIABILITIES AND STOCKHOLDERS' EQUITY:</b>		
Current liabilities:		
Short-term credit obligations	\$ 158	\$ 6,383
Accounts payable - trade	1,205	2,644
Accrued liabilities	7,964	6,986
Income taxes payable	-	96
Total current liabilities	<u>9,327</u>	<u>16,109</u>
Credit obligations- noncurrent	6,000	15
Deferred compensation	10,374	10,179
Deferred rent and other liabilities	756	792
Total liabilities	<u>26,457</u>	<u>27,095</u>
Commitments and contingencies		
Stockholders' equity:		
Preferred stock, \$1.00 par value authorized 600 shares, no shares issued	-	-
Common stock, \$1.00 par value; authorized 20,000 shares, 9,164 shares issued and 8,463 outstanding in 2013; 8,363 outstanding in 2012	9,164	9,164
Additional paid-in capital	51,913	50,797
Retained earnings	20,662	18,660
	<u>81,739</u>	<u>78,621</u>
Common stock reacquired and held in treasury - at cost (701 shares in 2013 and 801 shares in 2012)	(3,200)	(3,659)
Accumulated other comprehensive income	3,913	4,170
Total stockholders' equity	<u>82,452</u>	<u>79,132</u>
<b>Total liabilities and stockholders' equity</b>	<b><u>\$108,909</u></b>	<b><u>\$106,227</u></b>

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

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES  
Consolidated Statements of Income and Comprehensive Income  
Years ended April 30, 2013 and 2012

	<u>2013</u>	<u>2012</u>
	(In thousands, except share data)	
Revenues	\$ 68,932	\$ 63,595
Cost of revenues	<u>43,822</u>	<u>38,977</u>
Gross margin	25,110	24,618
Selling and administrative expenses	14,704	14,055
Research and development expenses	<u>5,727</u>	<u>3,860</u>
Operating profit	4,679	6,703
Other income (expense):		
Investment income	671	646
Gain on investment in affiliate	-	730
Equity loss	-	(650)
Impairment of investment in affiliate	-	(350)
Interest expense	(195)	(121)
Other expense, net	<u>(69)</u>	<u>(144)</u>
Income before provision (benefit) for income taxes	5,086	6,814
Provision (Benefit) for income taxes	<u>1,400</u>	<u>(560)</u>
Net income	<u>\$ 3,686</u>	<u>\$ 7,374</u>
Net income per common share:		
Basic	<u>\$ 0.44</u>	<u>\$ 0.89</u>
Diluted	<u>\$ 0.43</u>	<u>\$ 0.86</u>
Average shares outstanding:		
Basic	<u>8,412,633</u>	<u>8,329,081</u>
Diluted	<u>8,604,651</u>	<u>8,540,955</u>

**Statements of Comprehensive Income**

Net Income	\$ 3,686	\$ 7,374
Other comprehensive income (loss):		
Foreign currency translation adjustment	(782)	(1,070)
Change in market value of marketable securities	821	74
Deferred tax effect of change in marketable securities	<u>(296)</u>	<u>(26)</u>
Total other comprehensive income (loss)	<u>(257)</u>	<u>(1,022)</u>
Comprehensive income	<u>\$ 3,429</u>	<u>\$ 6,352</u>

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

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES  
Consolidated Statements of Cash Flows  
Years ended April 30, 2013 and 2012

	<u>2013</u>	<u>2012</u>
	(In thousands)	
Cash flows from operating activities:		
Net income	\$ 3,686	\$ 7,374
Adjustments to reconcile net income to net cash provided in operating activities:		
Deferred income tax benefit	(320)	(3,100)
Depreciation and amortization	2,413	2,241
Deferred lease obligation	(68)	(69)
Provision for losses on accounts receivable, inventories and warranty reserve	2,146	1,463
(Gain) Loss on marketable securities and other assets, net	(2)	(69)
Gain on investment in affiliate	-	(730)
Equity loss	-	650
Impairment of investment in affiliate	-	350
Employee benefit plans expense	1,072	1,156
Stock-based compensation expense	947	862
Tax benefit from exercise of stock-based compensation	(152)	(9)
Changes in operating assets and liabilities:		
Accounts receivable	465	(4,522)
Inventories	(6,017)	(4,242)
Prepaid expenses and other	(133)	(102)
Other assets	(614)	(567)
Accounts payable - trade	(502)	880
Accrued liabilities	895	(29)
Income taxes refundable/payable	(1,071)	1,114
Other liabilities	88	(507)
Net cash provided by operating activities	<u>2,833</u>	<u>2,144</u>
Cash flows from investing activities:		
Acquisition of FEI-Elcom, net of \$763 cash acquired	-	(4,483)
Purchase of marketable securities	(2,836)	(8,782)
Proceeds from sale or redemption of marketable securities	3,006	6,636
Proceeds from sale of fixed assets	67	24
Capital expenditures	<u>(2,250)</u>	<u>(1,396)</u>
Net cash used in investing activities	<u>(2,013)</u>	<u>(8,001)</u>

Continued

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES  
Consolidated Statements of Cash Flows  
Years ended April 30, 2013 and 2012  
(Continued)

	<u>2013</u>	<u>2012</u>
	(In thousands)	
Cash flows from financing activities:		
Proceeds from credit line borrowing	\$ 5,000	\$ 6,344
Payment of short-term credit and lease obligations	(5,357)	(660)
Proceeds from exercise of stock options	20	13
Dividends	(1,684)	-
Tax benefit from exercise of stock-based compensation	<u>152</u>	<u>9</u>
Net cash provided by (used in) financing activities	<u>(1,869)</u>	<u>5,706</u>
Net decrease in cash and cash equivalents before effect of exchange rate changes	(1,049)	(151)
Effect of exchange rate changes on cash and cash equivalents	<u>(273)</u>	<u>(342)</u>
Net decrease in cash and cash equivalents	(1,322)	(493)
Cash and cash equivalents at beginning of year	<u>4,782</u>	<u>5,275</u>
Cash and cash equivalents at end of year	<u>\$ 3,460</u>	<u>\$ 4,782</u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest	<u>\$ 186</u>	<u>\$ 119</u>
Income taxes	<u>\$ 2,993</u>	<u>\$ 1,475</u>

Allocation of fair value to net assets acquired on fiscal year 2012 purchase of FEI-Elcom Tech, Inc.

Cash	\$ -	\$ 763
Accounts receivable	-	342
Inventory	-	3,233
Other current assets	-	61
Fixed assets	-	2,100
Goodwill and other intangible assets	-	673
Deferred tax assets	-	2,573
Other assets	-	180
Accounts payable	-	(350)
Accrued expenses	-	(1,461)
Capital lease obligations	<u>-</u>	<u>(234)</u>
	<u>-</u>	<u>\$7,880</u>

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

FREQUENCY ELECTRONICS, INC. AND SUBSIDIARIES  
Consolidated Statements of Changes in Stockholders' Equity  
Years ended April 30, 2013 and 2012  
(In thousands, except share data)

	Common Stock		Additional paid in capital	Retained earnings	Treasury stock (at cost)		Accumulated other comprehensive income (loss)	Total
	Shares	Amount			Shares	Amount		
<u>Balance at April 30, 2011</u>	9,163,940	\$9,164	\$49,868	\$11,286	865,734	(\$3,975)	\$5,192	\$71,535
Contribution of stock to 401(k) plan			154		(42,370)	206		360
Stock-based compensation expense			775		(17,900)	87		862
Tax benefit from stock option exercise			9					9
Exercise of stock options and stock appreciation rights - net of shares tendered for exercise price			(9)		(4,677)	23		14
Change in unrealized gains and losses on marketable securities - net							48	48
Foreign currency translation adjustment							(1,070)	(1,070)
Net Income				7,374				7,374
<u>Balance at April 30, 2012</u>	<u>9,163,940</u>	<u>9,164</u>	<u>50,797</u>	<u>18,660</u>	<u>800,787</u>	<u>(3,659)</u>	<u>4,170</u>	<u>79,132</u>
Contribution of stock to 401(k) plan			214		(52,715)	242		456
Stock-based compensation expense			947		100			947
Tax benefit from stock option exercise			152					152
Exercise of stock options and stock appreciation rights - net of shares tendered for exercise price			(197)		(47,582)	217		20
Cash dividend \$0.20 per share				(1,684)				(1,684)
Change in unrealized gains and losses on marketable securities - net							525	525
Foreign currency translation adjustment							(782)	(782)
Net Income				3,686				3,686
<u>Balance at April 30, 2013</u>	<u>9,163,940</u>	<u>\$9,164</u>	<u>\$51,913</u>	<u>\$20,662</u>	<u>700,590</u>	<u>(\$3,200)</u>	<u>\$3,913</u>	<u>\$82,452</u>

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

# FREQUENCY ELECTRONICS, INC. AND SUBSIDIARIES

## NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

### 1. Summary of Accounting Policies

#### **Principles of Consolidation:**

The consolidated financial statements include the accounts of Frequency Electronics, Inc. and its wholly-owned subsidiaries (the "Company" or "Registrant"). References to "FEI" are to the parent company alone and do not refer to any of its subsidiaries. The Company is principally engaged in the design, development and manufacture of precision time and frequency control products and components for microwave integrated circuit applications. See Note 15 for information regarding the Company's FEI-NY (which includes the subsidiaries FEI Government Systems, Inc., FEI Communications, Inc., Frequency Electronics, Inc. Asia ("FEI-Asia") and FEI-Elcom Tech, Inc. ("FEI-Elcom")), Gillam-FEI, and FEI-Zyfer business segments. Intercompany accounts and significant intercompany transactions are eliminated in consolidation. To accommodate the different fiscal periods of Gillam-FEI, the Company recognizes its share of net income or loss on a one month lag. Any material events which may occur during the intervening month at Gillam-FEI will be accounted for in the consolidated financial statements.

These financial statements have been prepared in conformity with United States generally accepted accounting principles ("U.S. GAAP") and require management to make estimates and assumptions that affect amounts reported and disclosed in the financial statements and related notes. Actual results could differ from these estimates.

#### **Cash Equivalents:**

The Company considers certificates of deposit and other highly liquid investments with maturities of three months or less when purchased to be cash equivalents. The Company places its temporary cash investments with high credit quality financial institutions. Such investments may be in excess of the FDIC insurance limit. No losses have been experienced on such investments.

#### **Marketable Securities:**

Marketable securities consist of investments in common stocks, including exchange-traded funds, corporate debt securities and debt securities of U.S. government agencies. All marketable securities were held in the custody of financial institutions; five institutions at April 30, 2013 and 2012. Investments in debt and equity securities are categorized as available for sale and are carried at fair value, with unrealized gains and losses excluded from income and recorded directly to stockholders' equity. The Company recognizes gains or losses when securities are sold using the specific identification method.

#### **Allowance for Doubtful Accounts:**

Losses from uncollectible accounts receivable are provided for by utilizing the allowance for doubtful accounts method based upon management's estimate of uncollectible accounts. Management analyzes accounts receivable and the potential for bad debts, customer concentrations, credit worthiness, current economic trends and changes in customer payment terms when evaluating the amount recorded for the allowance for doubtful accounts.

#### **Inventories:**

Inventories, which consist of finished goods, work-in-process, raw materials and components, are accounted for at the lower of cost (specific and average) or market.

#### **Property, Plant and Equipment:**

Property, plant and equipment are recorded at cost and include interest on funds borrowed to finance construction. Expenditures for renewals and betterments are capitalized; maintenance and repairs are charged to income when incurred. When fixed assets are sold or retired, the cost and related accumulated depreciation and amortization are eliminated from the respective accounts and any gain or loss is credited or charged to income.

If events or changes in circumstances indicate that the carrying amount of a long-lived asset may not be recoverable, the Company estimates the future cash flows expected to result from the use of the asset and its eventual disposition. If the sum of the expected future cash flows (undiscounted and without interest charges) is less than the carrying amount of the long-lived asset, an impairment loss is recognized. To date, no impairment losses have been recognized.

FREQUENCY ELECTRONICS, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued

**Depreciation and Amortization:**

Depreciation of fixed assets is computed on the straight-line method based upon the estimated useful lives of the assets (40 years for buildings and 3 to 10 years for other depreciable assets). Leasehold improvements and equipment acquired under capital leases are amortized on the straight-line method over the shorter of the term of the lease or the useful life of the related asset.

Amortization of identifiable intangible assets is based upon the expected lives of the assets and is recorded at a rate which approximates the Company's utilization of the assets.

**Intangible Assets:**

Intangible assets consist of the ISO 9000 certification arising from the acquisition of FEI-Elcom in the assignment of fair value to its acquired assets including intangibles. The certification is valued at fair value and amortized over the estimated useful life of 3 years from the date of acquisition.

**Goodwill:**

The Company records goodwill as the excess of purchase price over the fair value of identifiable net assets acquired. Goodwill is tested for impairment on at least an annual basis at year end. When it is determined that the carrying value of goodwill may not be recoverable, the Company writes down the goodwill to an amount commensurate with the revised value of the acquired assets. The Company measures impairment based on revenue projections, recent transactions involving similar businesses and price/revenue multiples at which they were bought and sold, price/revenue multiples of competitors, and the present market value of publicly-traded companies in the Company's industry.

**Revenue and Cost Recognition:**

Revenues under larger, long-term contracts, which generally require billings based on achievement of milestones rather than delivery of product, are reported in operating results using the percentage of completion method. For U.S. Government and other fixed-price contracts that require initial design and development of the product, revenue is recognized on the cost-to-cost method. Under this method, revenue is recorded based upon the ratio that incurred costs bear to total estimated contract costs with related cost of sales recorded as the costs are incurred. Costs and estimated earnings in excess of billings on uncompleted contracts, net of billings on uncompleted contracts in excess of costs and estimated earnings, are included in current assets.

On production-type orders, revenue is recorded as units are delivered with the related cost of sales recognized on each shipment based upon a percentage of estimated final program costs.

Changes in job performance on long-term and production-type orders may result in revisions to costs and revenue and are recognized in the period in which revisions are determined to be required. Provisions for anticipated losses are made in the period in which they become determinable.

For customer orders in the Company's subsidiaries, and smaller contracts or orders in the other business segments, sales of products and services to customers are reported in operating results upon shipment of the product or performance of the services pursuant to terms of the customer order.

Contract costs include all direct material, direct labor costs, manufacturing overhead and other direct costs related to contract performance. Selling, general and administrative costs are charged to expense as incurred.

In accordance with industry practice, inventoried costs contain amounts relating to contracts and programs with long production cycles, a portion of which will not be realized within one year. Program costs for which production-level orders cannot be determined as probable are written down in the period in which that assessment is made.

**Comprehensive Income:**

Comprehensive income consists of net income and other comprehensive income. Other comprehensive income includes changes in unrealized gains or losses, net of tax, on securities available for sale during the year and the effects of foreign currency translation adjustments.

FREQUENCY ELECTRONICS, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued

**Research and Development expenses:**

The Company engages in research and development activities to identify new applications for its core technologies, to improve existing products and to improve manufacturing processes to achieve cost reductions and manufacturing efficiencies. Research and development costs include direct labor, manufacturing overhead, direct materials and contracted services. Such costs are expensed as incurred.

**Income Taxes:**

The Company recognizes deferred tax liabilities and assets based on the expected future tax consequences of events that have been included in the financial statements or tax returns. Under this method, deferred tax liabilities and assets are determined based on the difference between the financial statement and tax bases of assets and liabilities using enacted tax rates in effect for the year in which the differences are expected to reverse. Valuation allowances are established and adjusted when necessary to increase or reduce deferred tax assets to the amount expected to be realized.

The Company analyzes its tax positions under accounting standards which prescribe recognition thresholds that must be met before a tax benefit is recognized in the financial statements and provides guidance on de-recognition, classification, interest and penalties, accounting in interim periods, disclosure, and transition. An entity may only recognize or continue to recognize tax positions that meet a "more likely than not" threshold. When and if the Company were to recognize interest or penalties related to unrecognized tax benefits, it would be reported net of the federal tax benefit in the tax provision.

**Earnings Per Share:**

Basic earnings per share are computed by dividing net earnings by the weighted average number of shares of common stock outstanding. Diluted earnings per share are computed by dividing net earnings by the sum of the weighted average number of shares of common stock and the if-converted effect of unexercised stock options.

**Fair Values of Financial Instruments:**

Cash and cash equivalents and short-term credit obligations are reflected in the accompanying consolidated balance sheets at amounts considered by management to reasonably approximate fair value based upon the nature of the instrument and current market conditions. Management is not aware of any factors that would significantly affect the value of these amounts. The Company also has an investment in a privately-held company, Morion, Inc. ("Morion"). The Company is unable to reasonably estimate a fair value for this investment. Additionally, the Company had a non-controlling interest in Elcom Technologies, Inc. ("Elcom" and, after the acquisition, "FEI-Elcom") in 2012 (through the date of acquisition). See Note 11 - Acquisition of Elcom Technologies, Inc.

**Foreign Operations and Foreign Currency Adjustments:**

The Company maintains manufacturing operations in Belgium and the People's Republic of China. The Company is vulnerable to currency risks in these countries. The local currency is the functional currency of each of the Company's non-U.S. subsidiaries. No foreign currency gains or losses are recorded on intercompany transactions since they are effected at current rates of exchange. The results of operations of foreign subsidiaries, when translated into U.S. dollars, reflect the average rates of exchange for the periods presented. The balance sheets of foreign subsidiaries, except for equity accounts which are translated at historical rates, are translated into U.S. dollars at the rates of exchange in effect on the date of the balance sheet. As a result, similar results in local currency can vary upon translation into U.S. dollars if exchange rates fluctuate significantly from one period to the next.

**Equity-based Compensation:**

The Company values its share-based payment transactions using the Black-Scholes valuation model. Such value is recognized as expense on a straight-line basis over the service period of the awards, which is generally the vesting period, net of estimated forfeitures.

FREQUENCY ELECTRONICS, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued

The weighted average fair value of each option or stock appreciation right has been estimated on the date of grant using the Black-Scholes option pricing model with the following range of weighted average assumptions used for grants:

	<u>Years ended April 30</u>	
	<u>2013</u>	<u>2012</u>
Expected volatility	40%	40%
Dividend yield	0.0%	0.0%
Risk-free interest rate	1.31% to 1.35%	1.30% to 1.34%
Expected lives	8.5 years	10 years

The expected life assumption was determined based on the Company's historical experience. The expected volatility assumption was based on the historical volatility of the Company's common stock. The dividend yield assumption was determined based upon the Company's past history of dividend payments and the Company's current decision to suspend payment of dividends. On December 21, 2012, the Company's Board of Directors declared a special cash dividend of \$0.20 per share, payable on December 31, 2012 to shareholders of record on December 24, 2012. Due to the one-time nature of the special dividend it was not factored into the Black Scholes fair value calculations. The risk-free interest rate assumption was determined using the implied yield currently available for zero-coupon U.S. government issues with a remaining term equal to the expected life of the stock options.

**Concentration of Credit Risk**

Financial instruments, which potentially subject the Company to concentration of credit risk, consist principally of cash and cash equivalents and trade receivables. The Company maintains accounts at several commercial banks at which the balances exceed Federal Deposit Insurance Corporation limits. The Company has not experienced any losses on such amounts. Concentration of credit risk with respect to trade receivables is generally diversified due to the large number of entities comprising the Company's customer base and their dispersion across geographic areas principally within the United States. The Company routinely addresses the financial strength of its customers and, as a consequence, believes that its receivable credit risk exposure is limited. The Company does not require customers to post collateral.

**New Accounting Pronouncements:**

In June 2011, the Financial Accounting Standards Board ("FASB") issued Accounting Standards Update ("ASU") No. 2011-05 *Comprehensive Income (Topic 220): Presentation of Comprehensive Income* ("ASU No. 2011-05"). Under ASU No. 2011-05, an entity has the option to present the total of comprehensive income, the components of net income, and the components of other comprehensive income either in a single continuous statement of comprehensive income or in two separate but consecutive statements. Regardless of which option is selected, an entity is required to present each component of net income along with total net income, each component of other comprehensive income along with a total for other comprehensive income, and a total amount for comprehensive income. ASU No. 2011-05 eliminates the option (previously utilized by the Company) to present the components of other comprehensive income as part of the statement of changes in stockholders' equity. ASU No. 2011-05 was adopted by the Company at the beginning of the current fiscal year, and affects only the presentation of financial statements and has no financial impact on the Company's Consolidated Financial Statements.

In September 2011, the FASB issued ASU No. 2011-08, *Testing Goodwill for Impairment* ("ASU No. 2011-08"), which is intended to reduce the complexity and costs to test goodwill for impairment. The amendment allows an entity the option to make a qualitative evaluation about the likelihood of goodwill impairment to determine whether it is necessary to perform the two-step quantitative goodwill impairment test. An entity will no longer be required to calculate the fair value of a reporting unit unless the entity determines, based on its qualitative assessment, that it is more likely than not that the fair value of the reporting unit is less than its carrying amount. ASU No. 2011-08 also expands upon the examples of events and circumstances that an entity should consider between annual impairment tests in determining whether it is more likely than not that the fair value of a reporting unit is less than its carrying amount. The amendment became effective for annual and interim goodwill impairment tests performed by the Company in the fourth quarter of the fiscal year ended April 30, 2012. The adoption of ASU 2011-08 did not have a material impact on its consolidated financial statements.

FREQUENCY ELECTRONICS, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued

In February 2013, the FASB issued Accounting Standard Update No. 2013-02, *Other Comprehensive Income*. The amendments require an entity to provide information about the amounts reclassified out of accumulated other comprehensive income by component. In addition, an entity is required to present, either on the face of the statement where net income is presented or in the notes, significant amounts reclassified out of accumulated other comprehensive income by the respective line items of net income but only if the amount reclassified is required under U.S. GAAP to be reclassified to net income in its entirety in the same reporting period. For other amounts that are not required under U.S. GAAP to be reclassified in their entirety to net income, an entity is required to cross-reference to other disclosures required under U.S. GAAP that provide additional detail about those amounts. This ASU is effective for periods beginning after December 15, 2012. The Company does not expect adoption of ASU 2013-02 to have a material effect on its financial statements.

In July 2012, the FASB issued ASU No. 2012-02, *Intangibles – Goodwill and Other (Topic 350): Test Indefinite-Lived Intangible Assets for Impairment*. Under the requirements of ASU 2012-02 an entity has the option to assess qualitative factors when testing indefinite-lived intangible assets annually to determine whether it is more likely than not that the asset is not impaired. An entity also has the option to bypass the qualitative assessment for any indefinite-lived intangible asset in any period and proceed directly to performing the quantitative impairment test or resume performing the qualitative assessment in any subsequent period. If, after assessing the totality of events and circumstances, an entity concludes that it is more likely than not that the indefinite-lived intangible asset is impaired, then it is required to determine the fair value of the indefinite-lived intangible asset and perform the quantitative impairment test by comparing the fair value with the carrying amount in accordance with *Subtopic 350-30*. ASU 2012-02 is effective for annual and interim impairment tests performed for fiscal years beginning after September 15, 2012. The Company will adopt ASU 2012-02 for its fiscal year 2014 which begins on May 1, 2013. The Company is unable to determine the impact of such adoption until it performs the annual test for impairment in the next fiscal year.

2. Earnings Per Share

Reconciliations of the weighted average shares outstanding for basic and diluted Earnings Per Share are as follows:

	<u>Years ended April 30,</u>	
	<u>2013</u>	<u>2012</u>
Basic EPS Shares outstanding (weighted average)	8,412,633	8,329,081
Effect of Dilutive Securities	<u>192,018</u>	<u>211,874</u>
Diluted EPS Shares outstanding	<u>8,604,651</u>	<u>8,540,955</u>

Dilutive securities consist of unexercised stock options and stock appreciation rights (“SARS”). The computation of diluted shares outstanding excludes those options and SARS with an exercise price in excess of the average market price of the Company’s common shares during the periods presented. The inclusion of such options and SARS in the computation of earnings per share would have been antidilutive. For the years ended April 30, 2013 and 2012, the number of excluded options and SARS were 939,375 and 733,375, respectively.

3. Costs and Estimated Earnings in Excess of Billings

At April 30, 2013 and 2012, costs and estimated earnings in excess of billings, net, consist of the following:

	<u>2013</u>	<u>2012</u>
	(in thousands)	
Costs and estimated earnings in excess of billings	\$10,228	\$ 9,552
Billings in excess of costs and estimated earnings	<u>(1,611)</u>	<u>(2,345)</u>
Net asset	<u>\$ 8,617</u>	<u>\$ 7,207</u>

Such amounts represent revenue recognized on long-term contracts that had not been billed at the balance sheet dates or represent a liability for amounts billed in excess of the revenue recognized. Amounts are billed to customers pursuant to contract terms. In general, the recorded amounts will be billed and collected or revenue recognized within twelve months of the balance sheet date. Revenue on

FREQUENCY ELECTRONICS, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued

these long-term contracts is accounted for on the percentage of completion basis. During the years ended April 30, 2013 and 2012, revenue recognized under percentage of completion contracts was approximately \$35.6 million and \$36.1 million, respectively.

4. Inventories

Inventories at April 30, 2013 and 2012, respectively, consisted of the following (in thousands):

	<u>2013</u>	<u>2012</u>
Raw Materials and Component Parts	\$ 21,066	\$ 15,813
Work in Progress	13,665	15,762
Finished Goods	<u>2,790</u>	<u>2,724</u>
	<u>\$ 37,521</u>	<u>\$ 34,299</u>

As of April 30, 2013 and 2012, approximately \$29.9 million and \$25.5 million, respectively, of total inventory is located in the United States, approximately \$6.9 million and \$8.2 million, respectively, is located in Belgium and approximately \$0.7 million and \$0.6 million, respectively, is located in China.

5. Marketable Securities

The cost, gross unrealized gains, gross unrealized losses and fair market value of available-for-sale securities at April 30, 2013 and 2012 are as follows (in thousands):

<u>April 30, 2013</u>				
	<u>Cost</u>	Gross Unrealized <u>Gains</u>	Gross Unrealized <u>Losses</u>	Fair Market <u>Value</u>
Fixed income securities	\$10,285	\$ 297	\$ 0	\$10,582
Equity securities	<u>6,490</u>	<u>1,266</u>	<u>(68)</u>	<u>7,688</u>
	<u>\$16,775</u>	<u>\$ 1,563</u>	<u>\$ (68)</u>	<u>\$18,270</u>
<u>April 30, 2012</u>				
	<u>Cost</u>	Gross Unrealized <u>Gains</u>	Gross Unrealized <u>Losses</u>	Fair Market <u>Value</u>
Fixed income securities	\$11,573	\$ 297	\$ (6)	\$11,864
Equity securities	<u>5,411</u>	<u>552</u>	<u>(169)</u>	<u>5,794</u>
	<u>\$16,984</u>	<u>\$ 849</u>	<u>\$ (175)</u>	<u>\$17,658</u>

The following table presents the fair value and unrealized losses, aggregated by investment type and length of time that individual securities have been in a continuous unrealized loss position:

	<u>Less than 12 months</u>		<u>12 Months or more</u>		<u>Total</u>	
	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>	<u>Fair Value</u>	<u>Unrealized Losses</u>
<u>April 30, 2013</u>						
Fixed Income Securities	\$ -	\$ -	\$ -	\$ -	\$ -	\$ -
Equity Securities	<u>-</u>	<u>-</u>	<u>512</u>	<u>(68)</u>	<u>512</u>	<u>(68)</u>
	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 512</u>	<u>\$ (68)</u>	<u>\$ 512</u>	<u>\$ (68)</u>
<u>April 30, 2012</u>						
Fixed Income Securities	\$ 301	\$ (6)	\$ -	\$ -	\$ 301	\$ (6)
Equity Securities	<u>539</u>	<u>(169)</u>	<u>-</u>	<u>-</u>	<u>539</u>	<u>(169)</u>
	<u>\$ 840</u>	<u>\$ (175)</u>	<u>\$ -</u>	<u>\$ -</u>	<u>\$ 840</u>	<u>\$ (175)</u>

The Company regularly reviews its investment portfolio to identify and evaluate investments that have indications of possible impairment. The Company does not believe that its investments in marketable securities with unrealized losses at April 30, 2013 are other-than-temporary due to market volatility of the security's fair value, analysts' expectations and the Company's ability to hold the securities for a period of time sufficient to allow for any anticipated recoveries in market value.

FREQUENCY ELECTRONICS, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued

Proceeds from the sale or redemption of available-for-sale securities and the resulting gross realized gains and losses included in the determination of net income (loss) are as follows (in thousands):

	For the years ended April 30,	
	<u>2013</u>	<u>2012</u>
Proceeds	<u>\$3,006</u>	<u>\$6,636</u>
Gross realized gains	<u>\$ 47</u>	<u>\$ 20</u>
Gross realized losses	<u>\$ -</u>	<u>\$ -</u>

Maturities of fixed income securities classified as available-for-sale at April 30, 2013 are as follows (at cost, in thousands):

Current	\$ 2,003
Due after one year through five years	7,478
Due after five years through ten years	<u>804</u>
	<u>\$10,285</u>

The fair value accounting framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements).

The three levels of the fair value hierarchy are described below:

- Level 1 Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Company has the ability to access.
- Level 2 Inputs to the valuation methodology include:
  - Quoted prices for similar assets or liabilities in active markets;
  - Quoted prices for identical or similar assets or liabilities in inactive markets
  - Inputs other than quoted prices that are observable for the asset or liability;
  - Inputs that are derived principally from or corroborated by observable market data by correlation or other means.
- Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs. All of the Company's investments in marketable securities are Level 1 assets.

6. Property, Plant and Equipment and Leases

Property, plant and equipment at April 30, 2013 and 2012, consists of the following (in thousands):

	<u>2013</u>	<u>2012</u>
Buildings and building improvements	\$ 5,477	\$ 5,500
Machinery, equipment and furniture	<u>44,758</u>	<u>42,850</u>
	50,235	48,350
Less, accumulated depreciation	<u>41,919</u>	<u>39,976</u>
	<u>\$ 8,316</u>	<u>\$ 8,374</u>

Depreciation and amortization expense for the years ended April 30, 2013 and 2012 was \$2,250,000 and \$2,222,000, respectively.

Maintenance and repairs charged to operations for the years ended April 30, 2013 and 2012 was approximately \$993,000 and \$807,000, respectively.

The Company leases its Long Island, New York headquarters building at an annual rental of \$600,000. During fiscal year 2013, the Company exercised its option to renew the lease for a second 5-year period at an annual rental of \$800,000 beginning February 2014. The lease will end in January 2019

FREQUENCY ELECTRONICS, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued

Under the terms of the lease, the Company is required to pay its proportionate share of real estate taxes, insurance and other charges.

In addition, the Company's subsidiaries in New Jersey, China, France and California lease their office and manufacturing facilities. FEI-Elcom leases 32,000 square feet of office and manufacturing space at current monthly rental of approximately \$27,000, increasing to \$28,000 in the last two years of the lease which expires in March 2016. The lease for the FEI-Asia facility is for a one-year term with monthly rent of \$6,800 through February 2014. FEI-Zyfer leases office and manufacturing space encompassing 27,850 square feet. Monthly rental payments are currently \$28,700 and increase each year over the remaining 52 months of the lease term. Satel-FEI, a wholly-owned subsidiary of Gillam-FEI, occupies office space under a 9-year lease, cancelable after three years, at an approximate rate of \$1,100 per month.

Rent expense under operating leases was approximately \$1.3 million and \$1.0 million for the fiscal years ended April 30, 2013 and 2012. The Company records rent expense on its New York building and FEI-Zyfer facility on the straightline method over the lives of the respective leases. As a result, as of April 30, 2013 and 2012, the Company's balance sheet includes deferred rent payable of approximately \$310,000 and \$338,000, respectively, which will be amortized over the respective rental periods.

Included in the assets of FEI-Elcom is machinery and equipment with a value of approximately \$300,000 obtained under capital leases prior to the Company's acquisition of FEI-Elcom. (See Note 11. Acquisition of Elcom Technologies, Inc.) FEI-Elcom's remaining capital lease obligation at the date of acquisition was approximately \$234,000.

Future minimum lease payments required by the leases are as follows (in thousands):

Years ending <u>April 30,</u>	<u>Operating Leases</u>	<u>Capital Lease</u>
2014	\$1,397	\$16
2015	1,503	-
2016	1,473	-
2017	1,174	-
2018	925	-
Thereafter	600	-
Less amounts representing interest	<u>-</u>	<u>(1)</u>
Present value of future minimum lease payments	<u>\$7,072</u>	<u>\$ 15</u>

7. Debt Obligations and Subsequent Event

On June 6, 2013, the Company obtained a credit facility (the "Facility") from JPMorgan Chase Bank, N.A. ("JPMorgan") pursuant to a credit agreement (the "Credit Agreement") between the Company and JPMorgan. The maximum aggregate amount of the Facility is \$25.0 million, of which the Company immediately borrowed \$7.2 million, using the proceeds to repay the outstanding balance under the \$9.3 million line of credit with another financial institution which formerly managed a substantial portion of the Company's investment portfolio. As a result of this refinancing of short-term credit with a long-term obligation, as of April 30, 2013, the Company reclassified the \$6.0 million balance payable under the replaced line of credit to long-term debt. Proceeds from the Facility will be used for working capital and to finance acquisitions.

The Company may make borrowings under the Facility from either Tranche A or Tranche B or a combination of both, not to exceed \$25.0 million. Pursuant to the Credit Agreement, the amount of Tranche A borrowings may not exceed the value of the Pledged Investments (as defined in the Credit Agreement). The amount of Tranche B borrowings may not exceed the lesser of (i) \$15.0 million and (ii) the Borrowing Base (as defined in the Credit Agreement). The Facility is fully guaranteed by certain of the Company's subsidiaries and is secured by, among other things, a pledge of substantially all personal property of the Company and certain of the Company's subsidiaries.

Borrowings under the Facility are evidenced by a line of credit note (the "Note") and bear interest, payable monthly, at a rate equal to the LIBOR Rate, as determined from time to time by JPMorgan pursuant to the terms of the Note, plus a margin of 0.75% for Tranche A borrowings and 1.75% for

FREQUENCY ELECTRONICS, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued

Tranche B borrowings. The principal balance on the Note, along with any accrued and unpaid interest, is due and payable no later than June 5, 2018, which is the maturity date of the Facility. In addition, the Company is required to pay JPMorgan fees equal to 0.1% per annum on any unused portion of the Facility.

The Credit Agreement contains a number of affirmative and negative covenants, including limitations on the incurrence of additional debt, liens on property, acquisitions, loans and guarantees, mergers, consolidations, liquidations and dissolutions, asset sales, and distributions and other payments in respect of the Company's capital stock. The Credit Agreement also contains certain events of default customary for credit facilities of this type, including nonpayment of principal or interest when due, material incorrectness of representations and warranties when made, breach of covenants, bankruptcy and insolvency, unstayed material judgment beyond specified periods, and acceleration or payment default of other material indebtedness. The Credit Agreement requires the Company to maintain, as of the end of each fiscal quarter, a funded debt to EBITDA (Earnings Before Interest, Taxes, Depreciation and Amortization) ratio and an interest charge coverage ratio. The calculation of both ratios is defined in the Credit Agreement.

Under the Company's subsequently replaced \$9.3 million line of credit with the financial institution which formerly managed a substantial portion of its investment in marketable securities, during the fiscal year ended April 30, 2013, the Company borrowed \$5.0 million and repaid the same amount. The highest borrowings under this line of credit during fiscal year 2013 was \$8.5 million. The line was secured by the investments and had no maturity date so long as the Company maintained its investments with the financial institution. During fiscal years 2013 and 2012, advances against the line of credit bore interest at variable interest rates between 1.70% and 1.80%.

The Company's European subsidiaries have available 500,000 Euros (approximately \$650,000 based on current rates of exchange between the dollar and the Euro) in bank credit lines to meet short-term cash flow requirements. As of April 30, 2013 and 2012, no amounts were outstanding under such lines of credit. Borrowings under the bank credit lines, if any, must be repaid within one year of receipt of funds. Interest on these credit lines varies from 0.5% to 1.5% over the EURO Interbank Offered rate (EURIBOR). At April 30, 2013 and 2012, the rate was 1.117% and 1.244%, respectively, based on the one-month EURIBOR.

8. Accrued Liabilities

Accrued liabilities at April 30, 2013 and 2012 consist of the following (in thousands):

	<u>2013</u>	<u>2012</u>
Vacation and other compensation	\$1,794	\$1,712
Incentive compensation	1,634	1,799
Payroll taxes	1,323	1,485
Deferred revenue	1,620	137
Warranty reserve	598	778
Other	<u>995</u>	<u>1,075</u>
	<u>\$7,964</u>	<u>\$6,986</u>

9. Investment in Morion, Inc.

The Company has an investment in Morion, Inc., a privately-held Russian company, which manufactures high precision quartz resonators and crystal oscillators. The Company's investment consists of 4.6% of Morion's outstanding shares, accordingly, the Company accounts for its investment in Morion on the cost basis. This investment is included in investment in and loans receivable from affiliates in the accompanying balance sheets.

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During the fiscal years ended April 30, 2013 and 2012, the Company acquired product from Morion in the aggregate amount of approximately \$54,000 and \$224,000, respectively, and the Company sold product to Morion in the aggregate amount of approximately \$355,000 and \$1,162,000, respectively. At April 30, 2013, accounts receivable included \$144,000 due from Morion and \$8,000 were payable to Morion.

On October 22, 2012, the Company entered into an agreement to license its rubidium oscillator production technology to Morion. The agreement requires the Company to sell certain fully-depreciated production equipment currently owned by the Company and to provide training to Morion employees to enable Morion to produce a minimum of 5,000 rubidium oscillators per year. Morion will pay the Company approximately \$2.7 million for the license and the equipment plus 5% royalties on third party sales for a 5-year period following an initial production run. During the same 5-year period, the Company commits to purchase from Morion a minimum of approximately \$400,000 worth of rubidium oscillators per year although Morion is not obligated to sell that amount to the Company. In November 2012, Morion paid the Company a \$925,000 deposit under this agreement. This amount is considered deferred revenue and is included in accrued liabilities on the accompanying consolidated balance sheet. The United States Department of State has approved the technology transfer which is expected to be completed within a year from the date of the agreement.

10. Goodwill and Other Intangible Assets

During fiscal year 2004, the Company acquired FEI-Zyfer, Inc. ("FEI-Zyfer"). This acquisition resulted in the recording of \$218,000 in goodwill. In February 2012, the Company acquired FEI-Elcom (see Note 11 Acquisition of Elcom Technologies, Inc.) resulting in the recording of goodwill in the amount of \$398,000 plus other intangible assets with a value of \$275,000. Management has determined that goodwill is not impaired as of April 30, 2013 and 2012. The other intangible asset will be amortized over a three-year period from the date of acquisition. Amortization expense for the years ended April 30, 2013 and 2012 was approximately \$91,000 and \$19,000, respectively.

11. Acquisition of Elcom Technologies, Inc.

On February 21, 2012, the Company purchased 74.88% of the capital stock of Elcom. Prior to the acquisition, the Company had a minority ownership interest of 25.12% of the capital stock of Elcom. After the acquisition, the Company owned 100% and changed the subsidiary's name to FEI-Elcom Tech, Inc. The Company acquired Elcom as, in addition to its own product line, Elcom provides design and technical support for the Company's satellite business, which accounts for a significant amount of the Company's consolidated revenue. For the acquisition, the Company paid approximately \$4.1 million to the shareholders for their shares of common stock and an additional \$910,000 to certain selling shareholders to settle their outstanding debt with Elcom. In addition the Company had notes due from Elcom with a book value of approximately \$1.7 million which was forgiven as an additional investment in Elcom. Based on the amounts paid to the Elcom shareholders, the Company determined that the fair value of Elcom at the date of acquisition was approximately \$7.9 million. The Company's determination of the fair value of Elcom at the date of acquisition included an adjustment for a control premium of 15% based on the total value at the date of acquisition.

The fair value of Elcom at the date of the transaction was allocated to \$4.6 million of net tangible assets, deferred taxes of \$2.6 million, and approximately \$700,000 of intangible assets, including goodwill of approximately \$400,000. None of the goodwill is expected to be deductible for income tax purposes.

The FEI-Elcom transaction is considered a "step acquisition" by generally accepted accounting principles. Such an acquisition required the Company to remeasure its previously held equity interest in Elcom and adjust it to fair value. The difference between the fair value of the Company's ownership in Elcom and the Company's carrying value of its investment resulted in the recognition of a gain of approximately \$730,000.

Prior to the acquisition of Elcom, the Company recorded its share of Elcom's income or loss on the equity method. In addition, periodically the Company measured the market value of Elcom based on comparisons to comparable companies as well as Elcom's forecasts of future financial results. For the

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year ended April 30, 2012, in addition to its equity share in the income or loss of Elcom during the year, the Company determined that its investment was impaired and recorded impairment charges in the amount \$350,000.

During the fiscal years ended April 30, 2012, prior to the acquisition of Elcom, the Company acquired technical services from Elcom in the aggregate amount of approximately \$16,000; sold product to Elcom in the amount of approximately \$5,000; and the Company recorded interest income on notes to Elcom in the amount of approximately \$87,000.

The estimated fair value of Elcom has been allocated as follows.

Cash	\$ 763
Accounts receivable	342
Inventory	3,233
Other current assets	61
Fixed assets	2,100
Goodwill and other intangible assets	673
Deferred tax assets	2,573
Other assets	180
Accounts payable	(350)
Accrued expenses	(1,461)
Capital lease obligations	<u>(234)</u>
	<u>\$7,880</u>

The Company incurred approximately \$230,000 in acquisition related costs applicable to the transaction during fiscal year 2012. These expenses are included in selling and administrative expenses in the Company's consolidated statements of income.

The accompanying consolidated statements of income for the years ended April 30, 2013 and 2012 include the results of operations of FEI-Elcom since the date of acquisition, February 21, 2012. For the period from the acquisition date to April 30, 2012, FEI-Elcom had revenue of \$840,000 and recorded an operating loss of \$700,000. The pro forma financial information set forth below is based upon the Company's historical consolidated statements of income for the year ended April 30, 2012, adjusted to give effect to the acquisition of FEI-Elcom as if it had occurred at the beginning of fiscal year 2012.

The pro forma financial information is presented for informational purposes only and may not be indicative of what actual results of operations would have been had the acquisition occurred on May 1, 2011, nor does it purport to represent the results of operations for future periods. The pro forma results of operations do not include the gain on the Company's original investment of \$730,000 or the impairment of the Company's investment in Elcom during fiscal year 2012.

	Pro forma (unaudited) Year ended April 30, <u>2012</u> (in thousands except per share data)
Revenues	<u>\$70,955</u>
Operating profit	<u>\$5,147</u>
Net income	<u>\$5,863</u>
Earnings per share- basic	<u>\$0.70</u>
Earnings per share- diluted	<u>\$0.69</u>

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12. Employee Benefit Plans

**Profit Sharing Plan:**

The Company provides its U.S.-based employees with a profit sharing plan and trust under section 401(k) of the Internal Revenue Code. This plan allows all eligible employees to defer a portion of their income through voluntary contributions to the plan. In accordance with the provisions of the plan, the Company can make discretionary matching contributions in the form of cash or common stock. For the years ended April 30, 2013 and 2012, the Company contributed 52,715 and 42,370 shares of common stock, respectively. The approximate value of these shares at the date of contribution was \$456,000 in fiscal year 2013 and \$360,000 in fiscal year 2012. Contributed shares are drawn from the Company's common stock held in treasury and are removed at the Company's original cost of acquisition of such shares on a specific identification basis. In addition to changes in the treasury stock accounts, during fiscal years 2013 and 2012, such transactions increased additional paid in capital by \$214,000 and \$154,000, respectively.

**Income Incentive Pool:**

The Company maintains incentive bonus programs for certain employees which are based on operating profits of the individual subsidiaries to which the employees are assigned. The Company also adopted a plan for the President and Chief Executive Officer of the Company, which formula is based on consolidated pre-tax profits. The Company charged approximately \$1.6 million and \$1.8 million to selling and administrative expenses under these plans for the fiscal years ended April 30, 2013 and 2012, respectively.

**Employee Stock Plans:**

The Company has various stock plans, some of which have been approved by the Company's stockholders, for key management employees, including officers and directors who are employees, certain consultants and independent members of the Board of Directors. The plans are Nonqualified Stock Options ("NQSO") plans, Incentive Stock Option ("ISO") plans and Stock Appreciation Rights ("SARS"). Under these plans, options or SARS are granted at the discretion of the Stock Option Committee at an exercise price not less than the fair market value of the Company's common stock on the date of grant.

Typically, options and SARS vest over a four-year period from the date of grant. The options and SARS expire ten years after the date of grant and are subject to certain restrictions on transferability of the shares obtained on exercise. As of April 30, 2012, a consultant, who is the son of the Company's president, had been granted options to purchase 56,625 shares of Company stock under NQSO plans at a weighted average exercise price of \$5.60. During the year ended April 30, 2013, the consultant elected a cashless exercise of 19,125 shares at an exercise price of \$3.50 per share (resulting in a net issuance of 11,011 shares) and the remaining 37,500 options are outstanding and exercisable at an exercise price of \$6.67. The options expire one year after the termination of the consulting agreement which has no expiration date. As of April 30, 2013, eligible employees had been granted options to purchase approximately 231,200 shares of Company stock under ISO plans, of which approximately 172,500 options with a weighted average exercise price of \$11.55 are both outstanding and exercisable. During the year ended April 30, 2013, employees exercised ISOs for 58,700 shares of Company stock. During fiscal year 2013, the Company gave option holders the opportunity to exercise stock options either by paying the exercise price for the shares or to do a cashless exercise whereby the individual receives the net number of shares of stock equal in value to the exercised number of shares times the difference between the current market value of the Company's stock and the exercise price. For the year ended April 30, 2013, the Company received approximately \$20,000 upon the exercise of options for 3,000 shares. The balance of stock option exercises under ISO and NQSO plans, including the consultant shares above, which aggregated 74,825 shares were conducted under the cashless option. Accordingly, the Company issued 25,897 shares for cashless exercises and returned 48,928 shares to the pool of available shares which may be used for future grants. As of April 30, 2013, eligible employees and

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directors have been granted SARS based on approximately 1,550,000 shares of Company stock, of which approximately 1,498,625 shares are outstanding and approximately 871,000 with a weighted average exercise price of \$7.93 are exercisable. When the SARS become exercisable, the Company will settle the SARS by issuing to exercising recipients the number of shares of stock equal to the appreciated value of the Company's stock between the grant date and exercise date. At the time of exercise, the quantity of shares under the SARS grant equal to the exercise value divided by the then market value of the shares will be returned to the pool of available shares for future grant under the Company's stock plan. During the year ended April 30, 2013, employees exercised SARS representing 35,250 shares of Company stock and received 18,685 shares of Company stock. The 16,565 share difference was returned to the pool of available shares and may be used for future grants.

The excess of the consideration received over the par value of the common stock or cost of treasury stock issued under both types of option plans is recognized as an increase in additional paid-in capital.

The following table summarizes information about stock option activity for the years ended April 30:

	<u>Stock Options and Stock Appreciation Rights</u>			
	<u>Shares</u>	<u>Weighted-Average Exercise Price</u>	<u>Weighted Average Remaining Contractual Term</u>	<u>Aggregate Intrinsic Value</u>
Outstanding – May 1, 2011	1,433,525	\$8.22	6.6 years	
Granted	253,000	7.36		
Exercised	(7,950)	5.35		
Expired or Canceled	<u>(48,875)</u>	11.10		
Outstanding – April 30, 2012	1,629,700	\$ 7.95	6.4 years	
Granted	209,000	8.82		
Exercised	(113,075)	5.63		
Expired or Canceled	<u>(17,000)</u>	5.16		
Outstanding – April 30, 2013	<u>1,708,625</u>	<u>\$ 8.23</u>	<u>6.1 years</u>	\$ 3,697,430
Exercisable	<u>1,081,000</u>	<u>\$ 8.46</u>	<u>4.8 years</u>	\$ 2,324,626
Available for future grants	<u>166,743</u>			

As of April 30, 2013, total unrecognized compensation cost related to nonvested options and stock appreciation rights under the plans was approximately \$2,149,000. These costs are expected to be recognized over a weighted average period of 3.0 years.

During the years ended April 30, 2013 and 2012, 254,813 and 221,969 shares, respectively, vested, the fair value of which was approximately \$847,000 and \$748,000, respectively. The weighted average grant date fair value of stock appreciation rights granted during the years ended April 30, 2013 and 2012, were approximately \$4.16 and \$3.73, respectively.

Stock-based compensation costs capitalized as part of work in process inventory or included in the cost of sales of programs on which the Company recognizes revenue under the percentage of completion method were approximately \$410,000 and \$363,000 for the years ended April 30, 2013 and 2012, respectively. Selling and administrative expenses include stock-based compensation expense of approximately \$537,000 and \$359,000 for the years ended April 30, 2013 and 2012, respectively.

The Company classifies cash flows resulting from the tax benefits from tax deductions recognized upon the exercise of stock options or SARS (tax benefits) as financing cash flows. For the years ended April 30, 2013 and 2012, the Company realized \$152,000 and \$9,000 respectively, of tax benefits from the exercise of stock options and SARS.

**Independent Contractor Stock Option Plan:**

The Company had an Independent Contractor Stock Option Plan under which up to 350,000 shares could be granted. This plan was terminated in fiscal year 2006. An Independent Contractor Stock Option Committee determined to whom options may be granted from among eligible participants, the timing and

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duration of option grants, the option price, and the number of shares of common stock subject to each option. Options were granted to certain independent contractors at a price equal to the then fair market value of the Company's common stock. The options were exercisable over specified periods per terms of the individual agreements. No compensation expense was recorded during the years ended April 30, 2013 and 2012 as no other grants were made in those years and previous grants have been fully expensed. As a result of the adoption by the stockholders of the 2005 Stock Award Plan, the Independent Contractor Stock Option Plan was discontinued. No additional grants will be made under this plan and the outstanding grant will expire in fiscal year 2015.

At April 30, 2013 and 2012, options for 30,000 shares, at a weighted average exercise price of \$14.76, were issued and outstanding under this plan. No other activities occurred during the two year period ended April 30, 2013.

**Restricted Stock Plan:**

During fiscal year 1990, the Company adopted a Restricted Stock Plan which provided that key management employees could be granted rights to purchase an aggregate of 375,000 shares of the Company's common stock. The grants, transferability restrictions and purchase price were determined at the discretion of a special committee of the board of directors. The purchase price could not be less than the par value of the common stock. Transferability of shares is restricted for a four-year period, except in the event of a change in control as defined. As a result of the adoption by the Company's stockholders of the 2005 Stock Award Plan, the Restricted Stock Plan was discontinued. No additional grants will be made under this plan. As of April 30, 2013 and 2012, grants for 7,500 shares are available to be purchased at a price of \$4.00 per share.

**Employee Stock Ownership Plan/Stock Bonus Plan:**

During 1990, the Company amended its Stock Bonus Plan to become an Employee Stock Ownership Plan ("ESOP"). By means of a bank note, subsequently repaid, the Company reacquired 561,652 shares of its common stock during fiscal year 1990. These shares plus approximately 510,000 additional shares issued by the Company from its authorized, unissued shares were sold to the ESOP in May 1990. Shares were released for allocation to participants based on a formula as specified in the ESOP document. By the end of fiscal year 2000, all shares (1,071,652) had been allocated to participant accounts of which 406,102 shares remain in the ESOP.

**Deferred Compensation Agreements:**

The Company has a series of agreements with key employees providing for the payment of benefits upon retirement or death. Under these agreements, each key employee receives specified retirement payments for the remainder of the employee's life with a minimum payment of ten years' benefits to either the employee or his beneficiaries. The agreements also provide for lump sum payments upon termination of employment without cause and reduced benefits upon early retirement. The Company pays the benefits out of its working capital, but has also purchased whole life or term life insurance policies on the lives of certain of the participants to cover the optional lump sum obligations of the agreements upon the death of the participant. Deferred compensation expense charged to selling and administrative expenses during the years ended April 30, 2013 and 2012 was approximately \$616,000 and \$796,000, respectively.

**Life Insurance Policies and Cash Held in Trust:**

The whole-life insurance policies on the lives of certain participants covered by deferred compensation agreements have been placed in a trust. Upon the death of any insured participant, cash received from life insurance policies in excess of the Company's deferred compensation obligations to the estate or beneficiaries of the deceased, are also placed in the trust. These assets belong to the Company until a change of control event, as defined in the trust agreement, should occur. At that time, the Company is required to add sufficient cash to the trust so as to match the deferred compensation liability described above. Such funds will be used to continue the deferred compensation arrangements following a change of control.

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13. Income Taxes

The income before benefit for income taxes consisted of (in thousands):

	<u>Year Ended April 30,</u>	
	<u>2013</u>	<u>2012</u>
U.S.	\$ 7,028	\$7,426
Foreign	(1,942)	(612)
	<u>\$ 5,086</u>	<u>\$6,814</u>

The benefit for income taxes consists of the following (in thousands):

	<u>2013</u>	<u>2012</u>
Current:		
Federal	\$ 1,680	\$ 2,534
Foreign	-	-
State	40	6
Current provision	<u>1,720</u>	<u>2,540</u>
Deferred:		
Federal	(145)	16
Foreign	(585)	(49)
State	(80)	(10)
Deferred benefit	<u>(810)</u>	<u>(43)</u>
Change in valuation allowance	490	(3,057)
Total benefit	<u>\$ 1,400</u>	<u>\$ (560)</u>

The following table reconciles the reported income tax (benefit) expense with the amount computed using the federal statutory income tax rate (in thousands):

	<u>2013</u>	<u>2012</u>
Computed "expected" tax expense	\$ 1,729	\$ 2,316
State and local tax, net of federal benefit	(81)	(3)
Valuation allowance on deferred tax assets	490	(3,057)
Nontaxable income from foreign subsidiaries	29	72
Nondeductible expenses	178	143
Nontaxable life insurance cash value increase	(168)	(150)
Write off benefit from equity investment losses	-	466
Tax credits	(299)	(350)
Other items, net, none of which individually exceeds 5% of federal taxes at statutory rates	<u>(478)</u>	<u>3</u>
	<u>\$ 1,400</u>	<u>\$ (560)</u>

The components of deferred taxes are as follows (in thousands):

	<u>2013</u>	<u>2012</u>
Deferred tax assets:		
Employee benefits	\$ 6,490	\$ 5,320
Inventory	1,980	2,055
Accounts receivable	470	525
Tax credits	990	1,140
Other liabilities	270	332
Net operating loss carryforwards	<u>3,040</u>	<u>2,800</u>
Total deferred tax asset	<u>13,240</u>	<u>12,172</u>
Deferred tax liabilities:		
Marketable securities	540	243
Property, plant and equipment	<u>1,310</u>	<u>1,630</u>
Net deferred tax asset	11,390	10,299
Valuation allowance	<u>(1,900)</u>	<u>(1,455)</u>
Net deferred tax assets	<u>\$ 9,490</u>	<u>\$ 8,844</u>

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Net deferred tax assets are comprised of the following (in thousands):

	<u>2013</u>	<u>2012</u>
Gross current assets	\$ 3,890	\$ 4,092
Valuation allowance	-	(697)
Current liabilities	<u>(720)</u>	<u>(243)</u>
Net current deferred tax assets	3,170	3,152
Gross noncurrent assets	9,600	8,080
Valuation allowance	(1,900)	(758)
Noncurrent liabilities	<u>(1,380)</u>	<u>(1,630)</u>
Net noncurrent deferred tax assets	<u>6,320</u>	<u>5,692</u>
Net deferred tax assets	<u>\$ 9,490</u>	<u>\$ 8,844</u>

The total valuation allowance relates to deferred tax assets of both domestic and foreign subsidiaries. For the year ended April 30, 2013, the change in valuation allowance was an increase of \$445,000 which consists of the \$490,000 deferred tax provision less a foreign exchange adjustment of \$45,000. The change in valuation allowance during the year ended April 30, 2012 was a decrease of \$3.1 million, including foreign exchange adjustments of \$58,000 and the \$43,000 tax effect of unrealized gains on marketable securities.

During the fourth quarter of fiscal year 2012, the Company reduced its valuation allowance against deferred tax assets in the amounts of \$3.1 million. This recognition was the result of an evaluation of the Company's net operating losses incurred in prior years, its recent history of three consecutive years of increasing profitability and recent contract bookings which increased the Company's long-term backlog to a higher level. Company management believed such contracts would enable the Company to continue to generate operating profits in fiscal year 2013 and beyond. These adjustments were made in the fourth quarter of fiscal year 2012 as the Company waited until it had results for the full year to make final its determination, given the existence of a loss in recent years, that it met the accounting threshold for determination that the recovery of the deferred tax asset was more likely than not and to estimate the appropriate balance of the valuation allowance, based on all available information. The amount of the non-cash valuation allowance reduction was based on management's estimates of taxable income by reporting segment and taxing jurisdictions and the periods over which the Company believes deferred tax assets will be recoverable.

At April 30, 2013, the Company has available approximately \$2.7 million in net operating losses available to offset future income of certain of its foreign subsidiaries. These loss carryforwards have no expiration date. As a result of the acquisition of FEI-Elcom, the Company has a federal net operating loss carryforward of \$6.6 million which may be applied in annually limited amounts to offset future U.S.-sourced taxable income over the next 19 years.

The Company has evaluated its tax positions and has concluded that the tax positions meet the more-likely-than-not recognition threshold as specified under accounting standards. It is difficult to predict what would occur to change the Company's unrecognized tax benefits over the next twelve months. The Company believes, however, that there should be no change during the next twelve months. The Company's tax returns for April 30, 2006 and 2007 have been examined by the Internal Revenue Service, which resulted in no material adjustments. The Company's tax years from April 30, 2005 through April 30, 2013 remain open to examination by state tax authorities and tax years from April 30, 2008 through April 30, 2013 remain open for examination by the Internal Revenue Service.

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14. Product Warranties

The Company generally provides its customers with a one-year warranty regarding the manufactured quality and functionality of its products. For some limited products, the warranty period has been extended. The Company establishes warranty reserves based on its product history, current information on repair costs and annual sales levels. Changes in the carrying amount of accrued product warranty costs are as follows (in thousands):

	<u>Year Ended April 30,</u>	
	<u>2013</u>	<u>2012</u>
Balance at beginning of year	\$778	\$145
Acquired reserve of FEI-Elcom		370
Warranty costs incurred	(324)	(192)
Product warranty accrual	<u>144</u>	<u>455</u>
Balance at end of year	<u>\$598</u>	<u>\$778</u>

15. Segment Information

The Company operates under three reportable segments based on the geographic locations of its subsidiaries:

- (1) FEI-NY – operates out of New York and its operations consist principally of precision time and frequency control products used in three principal markets- communication satellites (both commercial and U.S. Government-funded); terrestrial cellular telephone or other ground-based telecommunication stations and other components and systems for the U.S. military.
- (2) Gillam-FEI - operates out of Belgium and France and primarily sells wireline synchronization and network management systems in non-U.S. markets. All sales from Gillam-FEI to the United States are to other segments of the Company.
- (3) FEI-Zyfer – operates out of California and its products incorporate Global Positioning System (GPS) technologies into systems and subsystems for secure communications, both government and commercial, and other locator applications. This segment also provides sales and support for the Company’s wireline telecommunications family of products, including US5G, which are sold in the United States market.

The FEI-NY segment also includes the operations of the Company’s wholly-owned subsidiaries, FEI-Elcom and FEI-Asia. FEI-Asia functions as a manufacturing facility for the FEI-NY segment with minimal sales to outside customers. FEI-Elcom, in addition to its own product line, provides design and technical support for the FEI-NY segment’s satellite business.

The Company’s Chief Executive Officer measures segment performance based on total revenues and profits generated by each geographic location rather than on the specific types of customers or end-users. Consequently, the Company determined that the segments indicated above most appropriately reflect the way the Company’s management views the business.

The accounting policies of the three segments are the same as those described in the “Summary of Significant Accounting Policies.” The Company evaluates the performance of its segments and allocates resources to them based on operating profit which is defined as income before investment income, interest expense and taxes. The European-based director of Gillam-FEI and the president of FEI-Zyfer manage the assets of these segments. All acquired assets, including intangible assets, are included in the assets of these two segments.

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The table below presents information about reported segments for each of the years ended April 30 with reconciliation of segment amounts to consolidated amounts as reported in the statement of operations or the balance sheet for each of the years (in thousands):

	<u>2013</u>	<u>2012</u>
Net revenues:		
FEI-NY	\$52,567	\$44,711
Gillam-FEI	11,825**	12,811**
FEI-Zyfer	10,523	11,494
less intersegment revenues	<u>(5,983)**</u>	<u>(5,421)**</u>
Consolidated revenues	<u>\$68,932</u>	<u>\$63,595</u>
Operating profit (loss):		
FEI-NY	\$ 7,334	\$ 7,938
Gillam-FEI	(1,643)**	138**
FEI-Zyfer	(552)	(511)
Corporate	<u>(460)</u>	<u>(862)</u>
Consolidated operating profit	<u>\$ 4,679</u>	<u>\$ 6,703</u>

\*\*For fiscal years ended April 30, 2013 and 2012, includes Gillam-FEI intersegment sales of \$4.1 million and \$3.9 million, respectively, to the FEI-NY and FEI-Zyfer segments. Such sales consist principally of manufacture of assemblies and units of a wireline synchronization product for ultimate production and sale in the U.S. plus the costs of ongoing research and development costs to support the product line. In the Gillam-FEI segment, these transactions increased the operating profit in each of the fiscal years. In addition, during the fourth quarter of fiscal year 2013, Gillam-FEI wrote down \$1.4 million of accumulated costs related to hardware and software design of a product in connection with the French government's smart electrical grid initiative. Based on slower than anticipated rollout of this project, the Company has less visibility regarding the probable schedule for obtaining production-level orders, which are now anticipated to occur no earlier than fiscal year 2015.

	<u>2013</u>	<u>2012</u>
Identifiable assets:		
FEI-NY (approximately \$3 million in China)	\$ 55,508	\$ 50,234
Gillam-FEI (all in Belgium or France)	18,071	20,407
FEI-Zyfer	10,418	9,685
less intersegment receivables	(18,903)	(16,424)
Corporate	<u>43,815</u>	<u>42,325</u>
Consolidated identifiable assets	<u>\$108,909</u>	<u>\$106,227</u>
Depreciation and amortization (allocated):		
FEI-NY	\$1,892	\$1,590
Gillam-FEI	304	425
FEI-Zyfer	202	207
Corporate	<u>15</u>	<u>19</u>
Consolidated depreciation and amortization expense	<u>\$2,413</u>	<u>\$2,241</u>

Major Customers

The Company's products are sold to both commercial and governmental customers. For the years ended April 30, 2013 and 2012, approximately 62% and 46% respectively, of the Company's sales were made under contracts to the U.S. Government or subcontracts for U.S. Government end-use.

In fiscal year 2013, sales to three customers of the FEI-NY segment aggregated \$34.1 million or 65% of that segment's total sales. Each of these customers also exceeded 10% of the Company's consolidated revenues. During the year ended April 30, 2013, in the Gillam-FEI segment, sales to one

FREQUENCY ELECTRONICS, INC. AND SUBSIDIARIES  
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS - Continued

customer exceeded 10% of that segment's revenues. In the FEI-Zyfer segment, two customers accounted for more than 10% of that segment's sales. None of the customers in the Gillam-FEI and FEI-Zyfer segments accounted for more than 10% of consolidated revenues.

In fiscal year 2012, sales to three customers of the FEI-NY segment aggregated \$29.3 million or 66% of that segment's total sales. Each of these customers also exceeded 10% of the Company's consolidated revenues. During the year ended April 30, 2012, in the Gillam-FEI segment, sales to one customer exceeded 10% of that segment's revenues. In the FEI-Zyfer segment, one customer accounted for more than 10% of that segment's sales. None of the customers in the Gillam-FEI and FEI-Zyfer segments accounted for more than 10% of consolidated revenues.

The loss by the Company of any one of these customers would have a material adverse effect on the Company's business. The Company believes its relationship with these customers to be mutually satisfactory. Sales to major customers above can include commercial and governmental end users.

Foreign Sales

Revenues in each of the Company's segments include sales to foreign governments or to companies located in foreign countries. Revenues, based on the location of the procurement entity and excluding intersegment sales, were derived from the following countries:

	(in thousands)	
	<u>2013</u>	<u>2012</u>
France	\$ 9,527	\$ 8,480
Belgium	4,240	4,254
China	565	899
Other	<u>3,390</u>	<u>7,533</u>
	<u>\$ 17,722</u>	<u>\$21,166</u>

## 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's management, with the participation of the Company's chief executive officer and chief financial officer, has evaluated the effectiveness of the Company's disclosure controls and procedures (as such term is defined in Rules 13a-15(e) and 15d-15(e) under the Securities Exchange Act of 1934, as amended (the "Exchange Act")) as of the end of the period covered by this report. There are inherent limitations to the effectiveness of any system of disclosure controls and procedures, including the possibility of human error and the circumvention or overriding of the controls and procedures. Accordingly, even effective disclosure controls and procedures can only provide reasonable assurance of achieving their control objectives. Based on their evaluation, the Company's chief executive officer and chief financial officer have concluded that, as of April 30, 2013, the Company's disclosure controls and procedures were effective.

#### Management's Annual Report on Internal Control Over Financial Reporting

Management of Frequency Electronics is responsible for establishing and maintaining adequate internal control over financial reporting as defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act. The Company's internal control system is designed 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. Because of 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.

Management has assessed the effectiveness of the Company's internal control over financial reporting as of April 30, 2013. In making this assessment, management used the criteria established in Internal Control—Integrated Framework issued by the Committee of Sponsoring Organizations of the Treadway Commission (COSO). Based on this evaluation, management has concluded that the Company's internal control over financial reporting were effective as of April 30, 2013.

A material weakness is a deficiency, or a combination of deficiencies, in internal control over financial reporting, such that there is a reasonable possibility that a material misstatement of the Company's annual or interim financial statements will not be prevented or detected on a timely basis.

#### Financial Reporting

In the prior fiscal year, the Company reported a material weakness in internal controls related to accounting for the acquisition of Elcom Technologies, Inc. in a "step-acquisition." No similar acquisitions occurred in fiscal year 2013. If and when another acquisition takes place, the Company intends to supplement its technical resources to provide for the appropriate accounting for such transactions. Consequently, the Company asserts that the previous material weakness in internal controls over financial reporting will be remediated.

This annual report does not include an attestation report of the Company's registered public accounting firm regarding internal control over financial reporting. Management's report was not subject to attestation by the Company's registered public accounting firm pursuant to rules of the Securities and Exchange Commission that permit the Company to provide only management's report in this annual report.

#### Changes in Internal Control Over Financial Reporting.

Other than the matters described in this Item 9A under "Financial Reporting," there were no changes in the Company's internal control over financial reporting (as such term is defined in Rules 13a-15(f) and 15d-15(f) under the Exchange Act) during the quarter ending April 30, 2013 to which this report relates that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

Item 9B Other Information

NONE

PART III

Item 10. Directors and Executive Officers of the Company

The information required to be furnished pursuant to this item with respect to Directors of the Company, in compliance with Section 16(a) of the Securities Exchange Act of 1934, as amended, and the Company's code of ethics is incorporated herein by reference from the Company's definitive proxy statement to be filed for the annual meeting of stockholders to be held on or about October 8, 2013. The information required to be furnished pursuant to this item with respect to Executive Officers is set forth, pursuant to General Instruction G of Form 10-K, under Part I of this Report.

Item 11. Executive Compensation

This item is incorporated herein by reference from the Company's definitive proxy statement to be filed for the annual meeting of stockholders to be held on or about October 8, 2013.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

This item is incorporated herein by reference from the Company's definitive proxy statement to be filed for the annual meeting of stockholders to be held on or about October 8, 2013.

Item 13. Certain Relationships and Related Transactions, and Director Independence

This item is incorporated herein by reference from the Company's definitive proxy statement to be filed for the annual meeting of stockholders to be held on or about October 8, 2013.

Item 14. Principal Accountant Fees and Services

This item is incorporated herein by reference from the Company's definitive proxy statement to be filed for the annual meeting of stockholders to be held on or about October 8, 2013.

## PART IV

### Item 15. Exhibits and Financial Statement Schedules

#### (a) Index to Financial Statements and Exhibits

The financial statements and exhibits are listed below and are filed as part of this report.

#### (1) FINANCIAL STATEMENTS

Included in Part II of this report:

	<u>Page(s)</u>
Report of Independent Registered Public Accounting Firm	22
Consolidated Balance Sheets April 30, 2013 and 2012	23
Consolidated Statements of Income and Comprehensive Income - years ended April 30, 2013 and 2012	24
Consolidated Statements of Cash Flows - years ended April 30, 2013 and 2012	25-26
Consolidated Statements of Changes in Stockholders' Equity - years ended April 30, 2013 and 2012	27
Notes to Consolidated Financial Statements	28-46

#### (2) EXHIBITS

Exhibit 21	List of Subsidiaries of Registrant
Exhibit 23.1	Consent of Independent Registered Public Accounting Firm
Exhibit 31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
Exhibit 31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
Exhibit 32	Certification of the Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
Exhibit 101	The following materials from the Frequency Electronics, Inc. Annual Report on Form 10-K for the year ended April 30, 2013 formatted in eXtensible Business Reporting Language (XBRL): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income and Comprehensive Income, (iii) Consolidated Statements of Cash Flows, (iv) Consolidated Statement of Changes in Stockholders' Equity and (v) Notes to Consolidated Financial Statements

The exhibits listed on the accompanying Index to Exhibits beginning on page 51 are filed as part of this annual report.

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.

FREQUENCY ELECTRONICS, INC.

By: /s/ Martin B. Bloch  
Martin B. Bloch  
President and CEO

By: /s/ Alan L. Miller  
Alan L. Miller  
Chief Financial Officer  
and Secretary/Treasurer

Dated: July 29, 2013

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:

<u>Signature</u>	<u>Title</u>	<u>Date</u>
<u>/s/ Joseph P. Franklin</u> Joseph P. Franklin	Chairman of the Board	7/29/13
<u>/s/ Joel Girsky</u> Joel Girsky	Director	7/29/13
<u>/s/ S. Robert Foley</u> S. Robert Foley	Director	7/29/13
<u>/s/ Richard Schwartz</u> Richard Schwartz	Director	7/29/13
<u>/s/ Martin B. Bloch</u> Martin B. Bloch	President and CEO (Principal Executive Officer)	7/29/13
<u>/s/ Alan L. Miller</u> Alan L. Miller	Chief Financial Officer and Secretary/Treasurer (Principal Financial and Accounting Officer)	7/29/13

## INDEX TO EXHIBITS

### ITEM 15(a)(3)

Certain of the following exhibits were filed with the Securities and Exchange Commission as exhibits, numbered as indicated below, to the Registration Statement or report specified below, which exhibits are incorporated herein by reference:

Exhibit No. in this Form 10-K	Description of Exhibit	NOTE
2.1	Stock Purchase Agreement, dated as of February 21, 2012, by and among the Registrant, Elcom Technologies Inc. and the stockholders of Elcom Technologies Inc. identified on the signature pages thereto	(12)
3.1	Copy of Certificate of Incorporation of the Registrant filed with the Secretary of State of Delaware	(1)
3.2	Amendment to Certificate of Incorporation of the Registrant filed with the Secretary of State of Delaware on March 27, 1981	(2)
3.3	Amendment to Certificate of Incorporation of the Registrant filed with Secretary of State of Delaware on October 26, 1984	(5)
3.4	Amendment to Certificate of Incorporation of the Registrant filed with the Secretary of State of Delaware on October 22, 1986	(7)
3.5	Amended and Restated Certificate of Incorporation of the Registrant filed with the Secretary of State of Delaware on October 26, 1987	(9)
3.6	Amended Certificate of Incorporation of the Company filed with the Secretary of State of Delaware on November 2, 1989	(9)
3.7	Copy of By-Laws of the Registrant, as amended to date	(3)
4.1	Specimen of Common Stock certificate	(1)
10.1	Registrant's 1997 Independent Contractor Stock Option Plan	(10)
10.8	Employment agreement between Registrant and Harry Newman	(4)
10.9	Employment agreement between Registrant and Marcus Hechler	(4)
10.10	Employment agreement between Registrant and Charles Stone	(8)
10.13	Lease agreement between Registrant and Reckson Operating Partnership, L.P. dated January 6, 1998	(11)
10.16	Registrant's Cash or Deferral Profit Sharing Plan and Trust under Internal Revenue Code Section 401, dated April 1, 1985	(6)
10.21	Form of Agreement concerning Executive Compensation	(2)
10.23	Registrant's Senior Executive Stock Option Plan	(8)

Exhibit No. in this Form 10-K	Description of Exhibit	NOTE
10.24	Amendment dated Jan. 1, 1988 to Registrant's Cash or Deferred Profit Sharing Plan and Trust under Section 401 of Internal Revenue Code	(8)
10.25	Executive Incentive Compensation Plan between Registrant and various employees	(8)
21	List of Subsidiaries of Registrant	Filed herewith
23.1	Consent of Independent Registered Public Accounting Firm to incorporation by reference of its 2012 audit report in Registrant's Form S-8 Registration Statements.	Filed herewith
31.1	Certification of the Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	Filed herewith
31.2	Certification of the Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002	Filed herewith
32	Certifications of the Chief Executive Officer and Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002	Filed herewith
101	The following materials from the Frequency Electronics, Inc. Annual Report on Form 10-K for the fiscal year ended April 30, 2013 formatted in eXtensible Business Reporting Language (XBRL): (i) Consolidated Balance Sheets, (ii) Consolidated Statements of Income and Comprehensive Income, (iii) Consolidated Statements of Cash Flows, (iv) Consolidated Statement of Changes in Stockholders' Equity and (v) Notes to Consolidated Financial Statements	

NOTES:

- (1) Filed with the SEC as an exhibit, numbered as indicated above, to the registration statement of Registrant on Form S-1, File No. 2-29609, which exhibit is incorporated herein by reference.
- (2) Filed with the SEC as an exhibit, numbered as indicated above, to the registration statement of Registrant on Form S-1, File No. 2-71727, which exhibit is incorporated herein by reference.
- (3) Filed with the SEC as an exhibit, numbered as indicated above, to the annual report of Registrant on Form 10-K, File No. 1-8061 for the year ended April 30, 1981, which exhibit is incorporated herein by reference.
- (4) Filed with the SEC as an exhibit, numbered as indicated above, to the registration statement of Registrant on Form S-1, File No. 2-69527, which exhibit is incorporated herein by reference.
- (5) Filed with the SEC as an exhibit, numbered as indicated above, to the annual report of Registrant on Form 10-K, File No. 1-8061, for the year ended April 30, 1985, which exhibit is incorporated herein by reference.
- (6) Filed with the SEC as exhibit, numbered as indicated above, to the annual report of Registrant on Form 10-K, File No. 1-8061, for the year ended April 30, 1986, which exhibit is incorporated herein by reference.
- (7) Filed with the SEC as an exhibit, numbered as indicated above, to the annual report of Registrant on Form 10-K, File No. 1-8061, for the year ended April 30, 1987, which exhibit is incorporated herein by reference.
- (8) Filed with the SEC as an exhibit, numbered as indicated above, to the annual report of Registrant on Form 10-K, File No. 1-8061, for the year ended April 30, 1989, which exhibit is incorporated herein by reference.
- (9) Filed with the SEC as an exhibit, numbered as indicated above, to the annual report of Registrant on Form 10-K, File No. 1-8061, for the year ended April 30, 1990, which exhibit is incorporated herein by reference.

- (10) Filed with the SEC as an exhibit, numbered as indicated above, to the registration statement of Registrant on Form S-8, File No. 333-42233, which exhibit is incorporated herein by reference.
- (11) Filed with the SEC as an exhibit, numbered as indicated above, to the annual report of Registrant on Form 10-K, File No. 1-8061, for the year ended April 30, 1998, which exhibit is incorporated herein by reference.
- (12) Filed with the SEC as an exhibit, numbered as indicated above, to the current report of Registrant on Form 8-K, File No. 1-8061, on February 27, 2012, which exhibit is incorporated herein by reference.

## FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

## List of Subsidiaries of Registrant

<u>Subsidiary &amp; Name under which business is performed</u>	<u>Jurisdiction of Incorporation</u>
Frequency Electronics, Inc.	Delaware
FEI Communications, Inc.	Delaware
FEI Government Systems, Inc.	Delaware
FEI Realty, Inc. (Inactive)	Delaware
Monitor Corp. (Inactive)	Delaware
FEI Zyfer, Inc.	Delaware
FEI-Elcom Tech, Inc.	Delaware
Gillam-FEI, s.a.	Belgium
Satel-FEI, s.a.	France
Frequency Electronics, Inc. Asia	People's Republic of China

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We consent to the incorporation by reference in the Registration Statements of Frequency Electronics, Inc. on Form S-8 (Nos. 333-08901, 333-40506, 333-140938, 333-156600, 333-42233 and 333-188952) of our report dated July 29, 2013 on our audits of the consolidated financial statements as of April 30, 2013 and 2012 and for each of the years in the two-year period ended April 30, 2013 which report is included in this Annual Report on Form 10-K to be filed on or about July 29, 2013.

/s/ EisnerAmper LLP  
EisnerAmper LLP

New York, New York  
July 29, 2013

## Certification

I, Martin B. Bloch, certify that:

1. I have reviewed this annual report on Form 10-K of Frequency Electronics, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: July 29, 2013

By: /s/ Martin B. Bloch  
Martin B. Bloch  
Chief Executive Officer

## Certification

I, Alan L. Miller, certify that:

1. I have reviewed this annual report on Form 10-K of Frequency Electronics, Inc.;
2. Based on my knowledge, this report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this report;
3. Based on my knowledge, the financial statements, and other financial information included in this report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this report;
4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e)) and internal control over financial reporting (as defined in Exchange Act Rules 13a-15(f) and 15d-15(f)) for the registrant and have:
  - (a) Designed such disclosure controls and procedures, or caused such disclosure controls and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this report is being prepared;
  - (b) Designed such internal control over financial reporting, or caused such internal control over financial reporting to be designed under our supervision, 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;
  - (c) Evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this report based on such evaluation; and
  - (d) Disclosed in this report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's fourth fiscal quarter in the case of an annual report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting;
5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of the registrant's board of directors (or persons performing the equivalent functions):
  - (a) All significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and
  - (b) Any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal control over financial reporting.

Date: July 29, 2013

By: /s/ Alan L. Miller  
Alan L. Miller  
Chief Financial Officer

**CERTIFICATION PURSUANT TO  
SECTION 906 OF  
THE SARBANES-OXLEY ACT OF 2002**

**Certification of CEO**

In connection with the Annual Report of Frequency Electronics, Inc. (the "Company") on Form 10-K for the year ended April 30, 2013 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Martin B. Bloch, Chief Executive Officer of the Company, certify, pursuant to Section 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) and 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Martin B. Bloch  
Martin B. Bloch  
Chief Executive Officer

July 29, 2013

**Certification of CFO**

In connection with the Annual Report of Frequency Electronics, Inc. (the "Company") on Form 10-K for the year ended April 30, 2013 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Alan L. Miller, Chief Financial Officer of the Company, certify, pursuant to Section 18 U.S.C. 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that:

- (1) The Report fully complies with the requirements of Section 13(a) and 15(d) of the Securities Exchange Act of 1934; and
- (2) The information contained in the Report fairly presents, in all material respects, the financial condition and results of operations of the Company.

/s/ Alan L. Miller  
Alan L. Miller  
Chief Financial Officer

July 29, 2013

A signed original of this written statement required by Section 906, or other document authenticating, acknowledging, or otherwise adopting the signature that appears in typed form within the electronic version of this written statement required by Section 906, has been provided to the Company and will be retained by the Company and furnished to the Securities and Exchange Commission or its staff upon request.

## CORPORATE INFORMATION

### Board of Directors

Joseph P. Franklin

*Chairman of the Board of Directors*

Martin B. Bloch

*President, Chief Executive Officer, Frequency Electronics, Inc.*

S. Robert Foley<sup>(1)</sup>

*Admiral, U.S. Navy (retired)*

Joel Girsky<sup>(2)</sup>

*President, Jaco Electronics, Inc.*

Richard Schwartz

*Former Chairman and CEO of ATK (retired)*

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<sup>(1)</sup>Chairman- Compensation Committee

<sup>(2)</sup>Chairman- Audit Committee

### Officers

Martin B. Bloch

*President, Chief Executive Officer and Director*

Joseph P. Franklin

*Chairman of the Board of Directors*

Markus Hechler

*Executive Vice President, President of FEI Government Systems, Inc. and Assistant Secretary*

Steven Strang

*President, FEI-Zyfer*

Oleandro Mancini

*Senior Vice President, Business Development*

Daniel Leonard

*Managing Director, Gillam-FEI*

Leonard Martire

*Vice President, Program Management*

Thomas McClelland

*Vice President, Advanced Development*

Adrian Lalicata

*Vice President, RF & Microwave Systems*

Alan Miller

*Secretary/Treasurer and Chief Financial Officer*

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### Counsel

Greenberg Traurig, LLP  
MetLife Building  
200 Park Avenue

*New York, NY 10166*

### Auditors

EisnerAmper LLP  
750 Third Avenue  
New York, NY 10017

### Website:

[www.frequencyelectronics.com](http://www.frequencyelectronics.com)

### Form 10-K

The Form 10-K report included in this annual report to Stockholders has been filed with the Securities and Exchange Commission ("SEC")

Additional copies of the Form 10-K as filed with the SEC may be obtained by request from the Company or through the Company's website.

### Transfer Agent and Registrar

American Stock Transfer & Trust Co.  
59 Maiden Lane  
New York, NY 10038

### Exchange Listing

NASDAQ Global Market  
Common Stock  
Stock Symbol: **FEIM**

### Annual Meeting

October 8, 2013, 10:00 AM  
Frequency Electronics, Inc.  
55 Charles Lindbergh Blvd.  
Mitchel Field, NY 11553



## **FREQUENCY ELECTRONICS, INC. & SUBSIDIARIES**

Corporate Headquarters  
55 Charles Lindbergh Blvd  
Mitchel Field, NY 11553

<u>Subsidiary</u>	<u>Location</u>	<u>Primary Function</u>
FEI Communications, Inc.	Mitchel Field, NY	Commercial communication systems and products
FEI Government Systems, Inc.	Mitchel Field, NY	U.S. Government systems and products
FEI-Elcom Tech, Inc.	Rockleigh, NJ	RF Microwave products
Frequency Electronics, Inc. Asia	Tianjin, China	Commercial communication products
FEI Realty, Inc.	Mitchel Field, NY	Corporate property holdings
Gillam-FEI	Liege, Belgium	Wireline synchronization and network management systems
Satel-FEI	Chalon-Sur-Saone, France	Network control products
FEI-Zyfer, Inc.	Garden Grove, CA	GPS time and frequency systems and products and U.S. wireline synchronization products
 <u>Affiliate</u>		
Morion, Inc.	St. Petersburg, Russia	Crystals and crystal oscillator products