FAIRCHILD CORP
Form 10-K
September 25, 2003

UNITED STATES

SECURITIES AND EXCHANGE COMMISSION

WASHINGTON, D.C. 20549

FORM 10-K

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

For the Year Ended June 30, 2003 Commission File Number 1-6560

THE FAIRCHILD CORPORATION

(Exact name of Registrant as specified in its charter)

Delaware 34-0728587

(State or other jurisdiction of (I.R.S. Employer Identification No.)

Incorporation or organization)

45025 Aviation Drive, Suite 400, Dulles, VA 20166

(Address of principal executive offices)

(703) 478-5800

(Registrant's telephone number, including area code)

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

Title of each class   Name of exchange on which registered

Class A Common Stock, par value $.10 per share New York and Pacific Stock Exchange

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

Indicate by check mark whether the Registrant (1) has filed all reports required to be filed by Section 13 or 15(d) of the Securities Exchange Act of 1934 during the preceding 12 months (or for such shorter period that the Registrant was required to file such reports), and (2) has been subject to such filing requirements for the past ninety (90) days [X] Yes [ ] No.

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Act) [X] Yes [ ] No

On December 27, 2002, the aggregate market value of the common shares held by nonaffiliates of the Registrant (based upon the closing price of these shares on the New York Stock exchange) was approximately $85.6 million (excluding shares deemed beneficially owned by affiliates of the Registrant under Commission Rules).

On August 29, 2003, the number of shares outstanding of each of the Registrant's classes of common stock were as follows:

Class A Common Stock, $0.10 Par Value	22,562,614
Class B Common Stock, $0.10 Par Value	2,621,502

DOCUMENTS INCORPORATED BY REFERENCE:

Portions of the registrant's definitive proxy statement for the 2003 Annual Meeting of Stockholders' to be held on November 7, 2003, which the Registrant intends to file within 120 days after June 30, 2003, are incorporated by reference into Part III of this Form 10-K.

THE FAIRCHILD CORPORATION

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ANNUAL REPORT ON FORM 10-K

FOR FISCAL YEAR ENDED JUNE 30, 2003

FORWARD-LOOKING STATEMENTS

Certain statements in this financial discussion and analysis by management contain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 with respect to our financial condition, results of operation and business. These statements relate to analyses and other information, which are based on forecasts of future results and estimates of amounts not yet determinable. These statements also relate to our future prospects, developments and business strategies. These forward-looking statements are identified by their use of terms and phrases such as "anticipate," "believe," "could," "estimate," "expect," "intend," "may," "plan," "predict," "project," "will" and similar terms and phrases, including references to assumptions. These forward-looking statements involve risks and uncertainties, including current trend information, projections for deliveries, backlog and other trend estimates, that may cause our actual future activitie s and results of operations to be materially different from those suggested or described in this financial discussion and analysis by management. These risks include: our ability to find, acquire and successfully operate one or more new businesses; product demand; our dependence on the aerospace industry; customer satisfaction and quality issues; labor disputes; competition; our ability to achieve and execute internal business plans; worldwide political instability and economic growth; military conflicts; reduced airline revenues as a result of the September 11, 2001 terrorist attacks on the United States, and their aftermath; reduced airline revenues due to SARS; and the impact of any economic downturns and inflation.

If one or more of these risks or uncertainties materializes, or if underlying assumptions prove incorrect, our actual results may vary materially from those expected, estimated or projected. Given these uncertainties, users of the information included in this financial discussion and analysis by management, including investors and prospective investors are cautioned not to place undue reliance on such forward-looking statements. We do not intend to update the forward-looking statements included in this Annual Report, even if new information, future events or other circumstances have made them incorrect or misleading.

PART I

All references in this Annual Report on Form 10-K to the terms "we," "our," "us," the "Company" and "Fairchild" refer to The Fairchild Corporation and its subsidiaries. All references to "fiscal" in connection with a year shall mean the 12 months ended June 30.

Item 1. BUSINESS

General

Our business consists of three segments: aerospace distribution, aerospace manufacturing and real estate operations. Our aerospace distribution segment stocks and distributes a wide variety of aircraft parts to commercial airlines and air cargo carriers, fixed-base operators, corporate aircraft operators and other aerospace companies worldwide. Our aerospace manufacturing segment primarily manufactures airframe components. Our real estate operations segment owns and leases a shopping center located in Farmingdale, New York, and owns and rents a building in Chatsworth, California and a manufacturing facility located in Fullerton, California.

On December 3, 2002, we completed the sale of our fastener business to Alcoa Inc. for approximately $657 million in cash and the assumption of certain liabilities. The cash received from Alcoa is subject to a post-closing adjustment based upon the net working capital of the fastener business on December 3, 2002, compared with its net working capital as of March 31, 2002 (See Item 8, Note 16, for further discussion). We may also receive additional cash proceeds up to $12.5 million per year over the four-year period from 2003 to 2006, if the number of commercial aircraft delivered by Boeing and Airbus exceeds specified annual levels.

We are continuing to investigate how best to redeploy our cash in opportunities which will enable us to build for the long term. Accordingly, we are actively pursuing worldwide acquisition opportunities in diverse business segments.

Financial Information about Business Segments

Our business segment information is incorporated herein by reference from Note 17 of our Consolidated Financial Statements included in Item 8, "Financial Statements and Supplementary Data".

Narrative Description of Business Segments

Aerospace Distribution Segment

Through our subsidiary Banner Aerospace Holding Company I, Inc., we offer a wide variety of aircraft parts and component repair and overhaul services. The aircraft parts, which we distribute are either purchased on the open market or acquired from OEMs as an authorized distributor. No single distributor arrangement is material to our financial condition. The aerospace distribution segment accounted for 77% of our revenues in fiscal 2003.

Products

Products of the aerospace distribution segment include rotable parts such as flight data recorders, radar and navigation systems, instruments, hydraulic and electrical components, space components and certain defense related items.

Rotable parts are sometimes purchased as new parts, but are generally purchased in the aftermarket and are then overhauled by us or for us by outside contractors, including OEMs or FAA-licensed facilities. Rotables are sold in a variety of conditions such as new, overhauled, serviceable and "as is". Rotables may also be exchanged instead of sold. An exchange occurs when an item in inventory is exchanged for a customer's part and the customer is charged an exchange fee.

An extensive inventory of products and a quick response time are essential in providing support to our customers. Another key factor in selling to our customers is our ability to maintain a system that traces a part back to the manufacturer or repair facility. We also offer immediate shipment of parts in aircraft-on-ground situations.

Through our FAA-licensed repair station, we provide a number of services such as component repair and overhaul services. Component repair and overhaul capabilities include pressurization, instrumentation, avionics, aircraft accessories and airframe components.

Sales and Markets

Our aerospace distribution segment sells its products in the United States and abroad to commercial airlines and air cargo carriers, fixed-base operators, corporate aircraft operators, distributors and other aerospace companies. Approximately 68% of our sales are to domestic purchasers, some of which may represent offshore users.

Our aerospace distribution segment conducts marketing efforts through its direct sales force, outside representatives and, for some product lines, overseas sales offices. Sales in the aviation aftermarket depend on price, service, quality and reputation. Our aerospace distribution segment's business does not experience significant seasonal fluctuations nor depend on a single customer.

Competition

Our aerospace distribution segment competes with Air Ground Equipment Services, Duncan Aviation, Stevens Aviation; OEMs such as Honeywell, Rockwell Collins, Raytheon, and Litton; other repair and overhaul organizations; and many smaller companies.

Aerospace Manufacturing Segment

Through our aerospace manufacturing segment, we primarily manufacture airframe components used in the construction and maintenance of commercial and military aircraft. Our products provide our customers with structural solutions by offering precision machined structural components in accordance with our customers' needs. Our aerospace manufacturing segment accounted for approximately 12% of our revenues in fiscal 2003.

Products

The principal product line of our aerospace manufacturing segment is precision machined structural components and assemblies. These precision machined structural components and assemblies are used on aircraft as pylons, flap hinges, struts, wing fittings, landing gear parts, spares and many other items.

Sales and Markets

The products of our aerospace manufacturing segment are sold primarily to domestic and foreign OEMs of airframes, as well as to subcontractors of OEMs. Approximately 94% of the sales of our aerospace manufacturing segment are to customers located in the United States. We have a small number of customers, which include Boeing, Lockheed

Martin, and other OEMs. Accordingly, our aerospace manufacturing segment is dependent on the business of these manufacturers.

Revenues in our aerospace manufacturing segment are closely related to aircraft production, which, in turn, is related in part to air miles flown. We are a small player in a fragmented industry and at times, during the recent aerospace industry recession, have accepted lower-priced orders at reduced profit margin to maintain market share.

Manufacturing and Production

Our aerospace manufacturing segment has two manufacturing facilities located in Huntington Beach, California. The facilities have complete production capability and are designed to produce a specified product or group of products, determined by production process and certification requirements. Our aerospace manufacturing segment's largest customers have recognized our quality and operational controls by conferring their advanced quality systems certifications at our facilities (e.g. Boeing's D1-9000A). We have received all necessary quality and product approvals from OEMs.

We have information systems in our facilities. The systems perform detailed and timely cost analysis of production by product and facility. Updated IT systems also help us to better service our customers. OEMs require each product to be produced in an OEM-qualified/OEM-approved facility.

Competition

We face intense competition in the industry, as we are one of many companies competing for business. Quality, performance, service and price are generally the prime competitive factors in the aerospace manufacturing segment. We seek to maintain our high level of quality and performance by maintaining a technological edge and competitive advantage over our competitors, and have demonstrated superior production methods to meet our customer demands. We seek to work closely with OEMs and involve ourselves early in the design process so that our products may be readily incorporated into the design of their products.

Real Estate Operations Segment

Our real estate operations segment owns and operates a 451,000 square foot shopping center located in Farmingdale, New York and also owns and leases a 102,000 square foot building in Chatsworth, California and a 208,000 square foot manufacturing facility located in Fullerton, California. We have two tenants that each occupy more than 10% of the rentable space of the shopping center. As of June 30, 2003, approximately 91% of the shopping center was leased. The Chatsworth property is leased through July 2008. The Fullerton property is leased to Alcoa through October 2007.

Tenants leasing space at our shopping center include: Staples; Modell's; Jillian's; Borders Books; Comp USA; Radio Shack; Hallmark; and others. In addition, Home Depot leases a portion of the shopping center real estate. Rental revenue from our real estate operations segment represents approximately 11% of our consolidated revenues. Our real estate operations segment represents approximately 31% of our total assets.

Backlog of Orders

Backlog is important for our aerospace manufacturing operation, due to the long-term production requirements of our customers. Our backlog of orders as of June 30, 2003 in the aerospace manufacturing segment amounted to approximately $9.0 million. We anticipate that in excess of 88% of the aggregate backlog at June 30, 2003 will be delivered by June 30, 2004. Often we are awarded long-term agreements by our customers who want us to provide our precision machined structural components and assemblies products over periods ranging generally from two-to-four years. However, amounts related to such agreements are not included in our backlog until our customers specify delivery dates for the products ordered.

Suppliers

In 2003, we purchased approximately $10 million of products from Universal Avionics. We are not materially dependent upon any other single supplier, but we are dependent upon a wide range of subcontractors, vendors and suppliers of materials to meet our commitments to our customers. From time to time, we enter into exclusive supply contracts in return for logistics and price advantages. We do not believe that any one of these contracts would impair our operations if a supplier failed to perform.

Research and Patents

We own patents relating to the design and manufacture of certain of our products and have licenses of technology covered by the patents of other companies. We do not believe that any of our business segments are dependent upon any single patent.

Personnel

As of June 30, 2003, we had approximately 250 employees, almost all of whom are based in the United States. None of our employees were covered by collective bargaining agreements. Overall, we believe that relations with our employees are good.

Environmental Matters

A discussion of our environmental matters is included in Note 16, "Contingencies", to our Consolidated Financial Statements, included in Part II, Item 8, "Financial Statements and Supplementary Data" and is incorporated herein by reference.

Available Information

Our Internet address is www.fairchild.com. We make available free of charge, on our Internet website, our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, and amendments to those reports filed or furnished pursuant to Section 13(a) or 15(d) of the Exchange Act as soon as reasonably practicable after we electronically file such material with, or furnish it to, the SEC.

ITEM 2. PROPERTIES

As of June 30, 2003, we owned or leased buildings totaling approximately 1,032,000 square feet, of which approximately 830,000 square feet were owned and 202,000 square feet were leased. Our aerospace manufacturing segment's properties consisted of approximately 116,000 square feet, with principal operating facilities concentrated in Southern California. The aerospace distribution segment's properties consisted of approximately 93,000 square feet, with principal operating facilities located in Florida, Georgia, Kansas, Texas, and California. Our real estate operations segment owns a shopping center consisting of approximately 451,000 square feet and also owns and leases a 102,000 square foot building in Chatsworth, California and a 208,000 square foot manufacturing facility located in Fullerton, California. We lease our corporate headquarters building at Washington-Dulles International Airport.

The following table sets forth the location of the larger properties used in our continuing operations, their square footage, the business segment or groups they serve and their primary use. Each of the properties owned or leased by us is, in our opinion, generally well maintained. All of our occupied properties are maintained and updated on a regular basis.

	Owned or	Square

Location	Leased	Footage	Business Segment/Group	Primary Use
Farmingdale, New York	Owned	451,000	Real Estate Operations	Rental
Fullerton, California	Owned	208,000	Real Estate Operations	Rental
Chatsworth, California	Owned	102,000	Real Estate Operations	Rental
Huntington Beach, California	Owned	58,000	Aerospace Manufacturing	Manufacturing
Huntington Beach, California	Leased	58,000	Aerospace Manufacturing	Manufacturing/Warehousing
Titusville, Florida	Leased	37,000	Aerospace Distribution	Distribution
Dulles, Virginia	Leased	34,000	Corporate	Office
Atlanta, Georgia	Leased	29,000	Aerospace Distribution	Distribution
Wichita, Kansas	Owned	11,000	Aerospace Distribution	Distribution
Austin, Texas	Leased	7,000	Aerospace Distribution	Distribution
San Francisco, California	Leased	5,000	Aerospace Distribution	Distribution

We have additional property located in Farmingdale, New York, which we are attempting to market, lease and/or develop.

Information concerning our long-term rental obligations at June 30, 2003, is set forth in Note 15 to our Consolidated Financial Statements, included in Part II, Item 8, "Financial Statements and Supplementary Data", of this Annual Report, and is incorporated herein by reference.

ITEM 3. LEGAL PROCEEDINGS

A discussion of our legal proceedings is included in Note 16, "Contingencies", to our Consolidated Financial Statements, included in Part II, Item 8, "Financial Statements and Supplementary Data", of this annual report and is incorporated herein by reference.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF STOCKHOLDERS

There were no matters submitted to a vote of security holders during the fourth quarter of the fiscal year covered by this report.

PART II

ITEM 5. MARKET FOR COMMON STOCK AND RELATED STOCKHOLDER MATTERS

Market Information

Our Class A common stock is traded on the New York Stock Exchange and Pacific Stock Exchange under the symbol "FA". Our Class B common stock is not listed on any exchange and is not publicly traded. Class B common stock can be converted to Class A common stock at any time at the option of the holder.

Information regarding the quarterly price range of our Class A common stock is incorporated herein by reference from Note 19 of our Consolidated Financial Statements included in Part II, Item 8, "Financial Statements and Supplementary Data".

We are authorized to issue 5,141,000 shares of our Class A common stock under our 1986 non-qualified stock option plan, and 250,000 shares of our Class A common stock under our 1996 non-employee directors stock option plan. At the beginning of the fiscal year, we had 181,859 shares available to grant under the 1986 non-qualified stock option plan and 188,000 shares available to grant under the 1996 non-employee directors stock option plan. At the end of the fiscal year, we had 378,698 shares available to grant under the 1986 non-qualified stock option plan and 226,750 shares available to grant under the 1996 non-employee directors stock option plan. Information regarding our stock option plans is incorporated herein by referenced from Note 12 of our Consolidated Financial Statements included in Part II, Item 8, "Financial Statements and Supplementary Data".

Holders of Record

We had approximately 1,114 and 37 record holders of our Class A and Class B common stock, respectively, at August 30, 2003.

Dividends

The agreement between us and Alcoa, under which we sold our Fairchild Fasteners business on December 3, 2003, provides that, for a period of five years after the closing, we will maintain our corporate existence, take no action to cause our own liquidation or dissolution and take no action to declare or pay any dividends on our common stock; provided, however, that we may engage in a merger or sale of substantially all of our assets to a third party that assumes our obligations under the acquisition agreement and that such provision of the agreement shall not prevent us from exercising our fiduciary duties to our stockholders. See Note 2 of our Consolidated Financial Statements included in Part II, Item 8, "Financial Statements and Supplementary Data".

Sale of Unregistered Securities

There were no sales or issuance of unregistered securities in the last fiscal quarter for the 2003 fiscal year. Sales or issuance of unregistered securities in previous fiscal quarters were reported on Form 10-Q for each such quarter.

Securities Authorized for Issuance under Equity Compensation Plans

The following table provides information as of June 30, 2003, with respect to compensation plans under which our equity securities are authorized for issuance.

	Number of securities to be issued upon exercise of outstanding options	Weighted average exercise price of outstanding options	Number of securities remaining available for future issuance
Equity compensation plans approved by shareholders	1,262,470	$ 6.40	605,448
Equity compensation plans not approved by shareholders (a)	382,018	$ 10.73	-
Total	1,644,488	$ 7.40	605,448

1. Upon our April 8, 1999 merger with Banner Aerospace, all of Banner Aerospace's stock options then issued and outstanding were converted into the right to receive 870,315 shares of our common stock. Since April 8, 1999, 30,984 shares were issued upon the exercise of stock options and 457,313 shares expired. All of the remaining stock options converted from the Banner Aerospace stock option plan are fully vested and expire at

various intervals between September 2003 and June 2005.

ITEM 6. SELECTED FINANCIAL DATA

Five-Year Financial Summary

(In thousands, except per share data)

	For the years ended June 30,				
Summary of Operations:	2003	2002	2001	2000	1999
Net sales	$ 68,820	$ 76,531	$ 94,192	$ 111,669	$ 177,567
Rental revenue	8,699	7,159	7,498	4,051	-
Gross profit	17,062	17,714	25,038	27,735	2,888
Operating loss	(48,427)	(21,022)	(17,145)	(11,184)	(78,877)
Net interest expense	28,491	45,346	53,921	42,578	28,879
Loss from continuing operations	(86,084)	(56,018)	(39,523)	(2,895)	(53,756)
Loss per share from continuing operations:					
Basic and Diluted	$ (3.42)	$ (2.23)	$ (1.57)	$ (0.12)	$ (2.36)
Other Data:					
Capital expenditures	9,861	2,450	3,832	20,836	43,094
	(122,521)	19,388	(40,156)	(71,303)	23,268

Cash provided by (used for) operating activities					
Cash provided by (used for) investing activities	605,516	(9,632)	18,233	95,649	(99,157)
Cash provided by (used for) financing activities	(485,842)	(9,655)	15,438	(41,373)	81,218
Balance Sheet Data:					
Total assets	390,549	992,118	1,164,030	1,270,880	1,332,530
Long-term debt, less current maturities	2,815	437,917	470,530	453,719	495,283
Stockholders' equity	137,816	230,222	363,767	404,212	410,201
Per outstanding common share	$ 5.47	$ 9.15	$ 14.47	$ 16.13	$ 16.49

The table above does not include the operating results of our fasteners business in the "Summary of Operations" section, which was sold on December 3, 2002 to Alcoa and is classified as a discontinued operation.

Effective July 1, 2001, we adopted Statement of Financial Accounting Standards No. 142, "Accounting for Goodwill and Other Intangible Assets." The comparable loss from continuing operations, as adjusted for the effects to eliminate goodwill amortization in each of the three years prior to 2002, would be: $38,426, or $1.52 per share, in 2001; $1,792, or $0.07 per share, in 2000; and $53,039, or $2.13 per share in 1999.

Fiscal 2000 includes a $28.6 million pre-tax gain from the disposition of our equity investment in Nacanco Paketleme, our Camloc Gas Springs Division and a smaller equity investment. Fiscal 1999 includes a $41.4 million pre-tax loss on the dispositions of Solair and Dallas Aerospace. The results of Solair are included until its disposition in December 1998. The results of Dallas Aerospace are included until its disposition in November 1999.

These transactions materially affect the comparability of the information reflected in the selected financial data.

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

FINANCIAL CONDITION

The Fairchild Corporation was incorporated in October 1969, under the laws of the State of Delaware. Banner Aerospace Holding Company I, Inc. is a 100% owned subsidiary. Fairchild Holding Corp. is our indirect 100% owned subsidiary. Fairchild Holding Corp. is the owner of Fairchild Aerostructures, Inc., and the indirect owner of 100% of Warthog Inc. Our principal operations are conducted through Banner Aerospace Holding Company I, Fairchild Aerostructures, and Warthog. Our consolidated financial statements present the results of our former fastener business, and APS, a small subsidiary being sold, as discontinued operations.

The following discussion and analysis provide information which management believes is relevant to the assessment and understanding of our consolidated results of operations and financial condition. The discussion should be read in conjunction with the consolidated financial statements and notes thereto.

GENERAL

Our business consists of three segments: aerospace distribution, aerospace manufacturing, and real estate operations. Our aerospace distribution segment stocks and distributes a wide variety of aircraft parts to commercial airlines and air cargo carriers, fixed-base operators, corporate aircraft operators and other aerospace companies worldwide. Our aerospace manufacturing segment primarily manufactures airframe components. Our real estate operations segment owns and leases a shopping center located in Farmingdale, New York, and owns and rents two improved parcels located in Southern California.

On December 3, 2002, we completed the sale of our fastener business to Alcoa Inc. for approximately $657 million in cash and the assumption of certain liabilities. The cash received from Alcoa is subject to a post-closing adjustment based upon the net working capital of the fastener business on December 3, 2002, compared with its net working capital as of March 31, 2002 (See Item 8, Note 16, for further discussion). We may also receive additional cash proceeds up to $12.5 million per year over the four-year period from 2003 to 2006, if the number of commercial aircraft delivered by Boeing and Airbus exceeds specified annual levels.

We are continuing to investigate how best to redeploy our cash in opportunities which will enable us to build for the long term. Accordingly, we are actively pursuing worldwide acquisition opportunities in diverse business segments.

CAUTIONARY STATEMENT

Certain statements in this financial discussion and analysis by management contain "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995 with respect to our financial condition, results of operation and business. These statements relate to analyses and other information, which are based on forecasts of future results and estimates of amounts not yet determinable. These statements also relate to our future prospects, developments and business strategies. These forward-looking statements are identified by their use of terms and phrases such as "anticipate," "believe," "could," "estimate," "expect," "intend," "may," "plan," "predict," "project," "will" and similar terms and phrases, including references to assumptions. These forward-looking statements involve risks and uncertainties, including current trend information, projections for deliveries, backlog and other trend estimates that may cause our actual future activities and results of operations to be materially different from those suggested or described in this financial discussion and analysis by management. These risks include: our ability to find, acquire and successfully operate one or more new businesses; product demand; our dependence on the aerospace industry; customer satisfaction and quality issues; labor disputes; competition; our ability to achieve and execute internal business plans; worldwide political instability and economic growth; military conflicts; reduced airline revenues as a result of the September 11, 2001 terrorist attacks on the United States, and their aftermath; reduced airline revenues due to SARS; and the impact of any economic downturns and inflation.

If one or more of these risks or uncertainties materializes, or if underlying assumptions prove incorrect, our actual results may vary materially from those expected, estimated or projected. Given these uncertainties, users of the information included in this financial discussion and analysis by management, including investors and prospective investors are cautioned not to place undue reliance on such forward-looking statements. We do not intend to update the forward-looking statements included in this Annual Report, even if new information, future events or other circumstances have made them incorrect or misleading.

CRITICAL ACCOUNTING POLICIES

On December 12, 2001, the Securities and Exchange Commission issued Release No. 33-8040, "Cautionary Advice Regarding Disclosure About Critical Accounting Policies." Critical accounting policies are those that involve subjective or complex judgments, often as a result of the need to make estimates. In response to Release No. 33-8040, we reviewed our accounting policies. The following areas require the use of judgments and estimates: the valuation of long-lived assets, impairment of goodwill, pension and postretirement benefits, income taxes, environmental and litigation accruals and revenue recognition. Estimates in each of these areas are based on historical experience and a variety of assumptions that we believe are appropriate. Actual results may differ from these estimates.

Valuation of Long-Lived Assets: We review our long-lived assets for impairment, including property, plant and equipment, and identifiable intangibles with definite lives, whenever events or changes in circumstances indicate that the carrying amount of the assets may not be fully recoverable. To determine recoverability of our long-lived assets, we evaluate the probability that future undiscounted net cash flows will be greater than the carrying amount of our assets. Impairment is measured based on the difference between the carrying amount of our assets and their estimated fair value.

Impairment of Goodwill: On July 1, 2001, we adopted Statement of Financial Accounting Standards No. 142, "Accounting for Goodwill and Other Intangible Assets." Since the adoption of SFAS No. 142, goodwill and intangible assets deemed to have an indefinite life are not amortized. Instead of amortizing goodwill and intangible assets deemed to have an indefinite life, goodwill is tested for impairment annually, or immediately if conditions indicate that such an impairment could exist. All of our goodwill is deemed to have an indefinite life and as a result of adopting SFAS No. 142, we ceased amortizing goodwill.

Pension and Postretirement Benefits: We have defined benefit pension plans covering certain of our employees. Our funding policy is to make the minimum annual contribution required by the Employee Retirement Income Security Act of 1974 or local statutory law. The accumulated benefit obligation for pensions and postretirement benefits was determined using a discount rate of 6.0% at June 30, 2003 and 7.125% at June 30, 2002 and a return on plan assets of 8.5% at June 30, 2003 and 9.0% at June 30, 2002. The effect of such change resulted in an increase to the accumulated benefit obligation in 2003. Assumed health care cost trend rates have a significant effect on the amounts reported for health care plans. For measurement purposes in 2003, we assumed a 10.0% annual rate of increase in the cost per capita of claims covered under health care benefits. Beginning in 2004, the trend rate is assumed to decrease each year by 0.5% to a rate of 5% in 2013 and remain at that level thereafter.

Deferred and Noncurrent Income Taxes: Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for income tax purposes. In assessing the realizability of deferred tax assets, we consider whether it is more likely than not that some portion or all of the deferred tax assets will not be realized. We consider the scheduled reversal of deferred tax liabilities, projected future taxable income, and tax planning strategies in making this assessment.

Environmental Matters: Our current and prior operations are subject to stringent government imposed environmental laws and regulations concerning, among other things, the discharge of materials into the environment and the generation, handling, storage, transportation and disposal of waste and hazardous materials. To date, such laws and regulations have not had a material effect on our financial condition, results of operations, or net cash flows, although we have expended, and can be expected to expend in the future, significant amounts for the investigation of environmental conditions and installation of environmental control facilities, remediation of environmental conditions and other similar matters.

In connection with our plans to dispose of certain real estate, we must investigate environmental conditions and we may be required to take certain corrective action prior or pursuant to any such disposition. In addition, we have identified several areas of potential contamination related to other facilities owned, or previously owned, by us, that may require us either to take corrective action or to contribute to a clean-up. We are also a defendant in several lawsuits and proceedings seeking to require us to pay for investigation or remediation of environmental matters, and we have been alleged to be a potentially responsible party at various "superfund" sites. We believe that we have recorded adequate accruals in our consolidated financial statements to complete such investigation and take any necessary corrective actions or make any necessary contributions. No amounts have been recorded as due from third parties, including insurers, or set off against, any environmental liability, unless such parties are contractually obligated to contribute and are not disputing such liability.

Legal Matters: We are involved in various other claims and lawsuits incidental to our business. We, either on our own or through our insurance carriers, are contesting these matters. In the opinion of management, the ultimate resolution of the legal proceedings will not have a material adverse effect on our financial condition, future results of operations, or net cash flows.

Revenue Recognition: Sales and related costs are recognized upon shipment of products and/or performance of services, when collection is probable. Sales and related cost of sales on long-term contracts are recognized as products are delivered and services performed, as determined by the percentage of completion method. Lease and rental revenue are recognized on a straight-line basis over the life of the lease. Shipping and handling amounts billed to customers are classified as revenues.

RESULTS OF OPERATIONS

The following summarizes certain business combinations and transactions we completed which significantly affect the comparability of the period to period results presented in this Management's Discussion and Analysis of Results of Operations and Financial Condition.

Business Transactions

On December 3, 2002, we completed the sale of our fastener business to Alcoa Inc. for approximately $657 million in cash and the assumption of certain liabilities. The cash received from Alcoa is subject to a post-closing adjustment based upon the net working capital of the fastener business on December 3, 2002, compared with its net working capital as of March 31, 2002 (See Item 8, Note 16, for further discussion). We may also receive additional cash proceeds up to $12.5 million per year over the four-year period from 2003 to 2006, if the number of commercial aircraft delivered by Boeing and Airbus exceeds specified annual levels.

In connection with the sale, we have deposited with an escrow agent $25 million to secure indemnification obligations we may have to Alcoa. The escrow period is five years, but funds may be held longer if claims are asserted and unresolved. In addition, for a period of five years after the closing, we are required to maintain our corporate existence, take no action to cause our own liquidation or dissolution, and take no action to declare or pay any dividends on our common stock.

The sale of the fastener business has reduced our dependence upon the aerospace industry. Additionally, the sale has allowed us to eliminate substantially all of our debt. We used a portion of the proceeds from the sale to repay our bank debt and to acquire by tender all of our outstanding $225 million 10.75% senior subordinated notes due in April 2009, leaving us with $6.7 million of debt outstanding on June 30, 2003. We plan to use the remaining proceeds from the sale to fund acquisitions.

Recent Developments

In February 2003, our Board of Directors adopted a formal plan for the sale of APS, a small operation in our aerospace manufacturing segment, which has been unprofitable. Based on our formal plan, APS is available for sale immediately, and we believe that it is probable that we can consummate a sale of APS by December 2003. Accordingly, the results of APS are being reported as a discontinued operation.

The results of the fastener business and APS are recorded as earnings from discontinued operations, the components of which are as follows:

(In thousands)	2003	2002	2001
Earnings from discontinued operations before taxes	$ 3,013	$ 46,935	$ 36,344
Income tax provision	95	(865)	(12,007)
Net earnings from discontinued operations	$ 3,108	$ 46,070	$ 24,337

Consolidated Results

We currently report in three principal business segments: aerospace distribution, aerospace manufacturing and real estate operations. The results of C-Line Automation, Ltd., a small start-up operation acquired in March 2003, is included in the Corporate and Other classification. The following table provides the historical sales and operating income of our operations for fiscal 2003, 2002 and 2001.

(In thousands)			
	2003	2002	2001
Revenues by Segment:			
Aerospace Distribution Segment	$ 59,608	$ 63,298	$ 85,908
Aerospace Manufacturing Segment	9,187	13,233	8,284
Real Estate Operations Segment	8,699	7,159	7,498
Corporate and Other	25	-	-
Total Revenues	$ 77,519	$ 83,690	$ 101,690
Operating Income (Loss) by Segment:			
Aerospace Distribution Segment	$ (4,143)	$ 2,579	$ 2,259
Aerospace Manufacturing Segment	(2,494)	(6,276)	(2,093)
Real Estate Operations Segment	2,735	1,550	307
Corporate and Other	(44,525)	(18,875)	(17,618)
Total Operating Loss (a)	$ (48,427)	$ (21,022)	$ (17,145)

1. The fiscal 2003 operating results include impairment expenses of $6.6 million to write down goodwill at our aerospace distribution segment and $0.1 million write down of intangible assets of a start-up company in our corporate and other segment. Operating results in fiscal 2002 includes impairment expenses of $3.0 million in the aerospace manufacturing segment and $0.4 million in the real estate operations segment. Operating results in Fiscal 2001 includes impairment charges of $2.4 million in the aerospace distribution segment, and $2.4 million in the real estate operations segment.

Revenues of $77.5 million in 2003 decreased by $6.2 million, or 7.4%, compared to revenues of $83.7 million in 2002. Revenues in 2003 were adversely affected by the overall conditions in the aerospace industry. The aerospace industry is still sluggish following the attacks of September 11, 2001, and weakness in the overall economy. The recent, well publicized, financial difficulties of major commercial airlines, and reduction in travel have affected the demand for products we sell at our remaining aerospace businesses. Revenues of $83.7 million in 2002 decreased by $18.0 million, or 17.7%, as compared to revenues of $101.7 million in 2001. The results for 2001 included revenue of $8.4 million from an operation in our aerospace distribution segment, which was shut down in June 2001. Excluding the results of the shut down operation, net revenues would have decreased by $9.6 million, or 10.3%, in 2002, as compared to 2001. Revenues in 2002 reflected the condition of the aerospace industry in th e aftermath of September 11, 2001.

Gross margin as a percentage of sales was 20.4%, 20.2% and 23.5% in 2003, 2002, and 2001, respectively. The improvement in 2003, reflects a slight increase in gross margin at our aerospace distribution segment, partially offset by declining margins at our remaining aerospace manufacturing locations, due to highly competitive pricing pressures.

Gross margins have declined following the aftermath of September 11, 2001.

Gross margin as a percentage of rental revenue at our real estate segment was 34.9 %, 31.3%, and 38.4% in 2003, 2002, and 2001, respectively. The improved margin in 2003 reflects a 21.5% increase in rental revenue, as compared to 2002. The change in margin in 2002 reflected a 4.5% decrease in rental revenue, as compared to 2001.

Selling, general and administrative expense for 2003, includes $13.7 million of one-time change of control payments required under contracts with our top four executives as a result of the sale of our fastener business, and $10.4 million of bonuses awarded to our top four executives as a result of the sale of our fasteners business. The top four executives have also relinquished their right to any other future change of control payments. In addition, selling, general and administrative expense for 2003 includes $1.1 million of severance expense. Excluding these items, selling, general & administrative expense as a percentage of revenues were 46.6%, 47.3%, and 39.8% in 2003, 2002, and 2001, respectively.

Other income decreased $1.7 million in 2003, as compared to 2002. This change primarily reflects income recognized in 2002 from the disposition of future royalty revenues to an unaffiliated third party in exchange for $12.8 million of promissory notes, offset partially by $0.8 million of income recognized in 2003 from the sale of non-core property. Other income increased $0.1 million in 2002, as compared to 2001.

Impairment charges of $6.7 million, $3.4 million and $4.8 million were recognized in 2003, 2002 and 2001, respectively. The fiscal 2003 impairment charges included $6.6 million to write down goodwill at our aerospace distribution segment and a $0.1 million write down of intangible assets of a start-up company in our corporate and other segment. The fiscal 2002 impairment charges included $3.0 million to write down the long-lived assets of the ongoing operation at our aerospace manufacturing segment and $0.4 million to write-off a former tenant's improvements at our shopping center. The fiscal 2001 impairment charges included $2.4 million due to the closing of a small subsidiary at our aerospace distribution segment, of which $1.7 million represented the write-off of goodwill, and $0.4 million represented severance payments. Additionally, the fiscal 2001 impairment charge also included a write-off of approximately $2.4 million of a former tenant's improvements at our shopping center.

Operating loss for 2003, includes the $13.7 million of one-time change of control payments required under contracts with our top four executives as a result of the sale of the fastener business, and $10.4 million of bonuses awarded to our top four executives as a result of the sale of the fasteners business. The top four executives have also relinquished their right to any other future change of control payments. In addition, the operating loss for 2003 includes the $6.6 million goodwill impairment at our aerospace distribution segment and $1.1 million of severance expense. With the sale of the fasteners business, we have become a much smaller company and are currently seeking acquisition opportunities. Costs at all locations are being strictly monitored, and reduced wherever possible. In January 2003, we announced a staff reduction of 24% at our corporate headquarters. The operating loss of $21.0 million in 2002 was larger by $3.9 million, or 22.6%, compared to the operating loss of $17.1 m illion in 2001. The 2001 results included goodwill amortization of $1.1 million, prior to the implementation of an accounting pronouncement that eliminates goodwill amortization beginning in 2002.

Net interest expense decreased by $16.9 million, or 37.2%, and cash interest expense decreased by $20.4 million in fiscal 2003, as compared to fiscal 2002. Interest expense was $38.5 million and $49.7 million for fiscal 2003 and fiscal 2002, respectively. The results for 2003 included an expense of $9.9 million to write-off deferred loan fees due to the repayment of all our outstanding senior subordinated notes and our term loan and revolving credit facilities, offset partially by $7.5 million of interest income recognized from the acceleration of principal on the repayment of notes due to us from an unaffiliated third party. As a result of the sale of the fastener business, our debt has been reduced by $485.1 million since June 30, 2002, to $6.7 million at June 30, 2003. As a result of our debt reduction, cash interest expense was significantly lower in 2003. Net interest expense decreased by $8.6 million, or 15.9%, and cash interest expense decreased by $5.3 million in fiscal 2002, as comp ared to fiscal 2001, due primarily to lower interest rates on our variable rate debt.

We recorded a nominal investment loss in 2003, an investment loss of $1.0 million in 2002, and investment income of $8.4 million in 2001. The investment results of 2003 included $1.2 million of dividend income, $0.6 million of realized gains on investments liquidated, and $0.5 million of fair market value increases to our trading securities, offset by a $2.4 million write down for impaired investments. The investment results in fiscal 2002 included a $2.3 million write down for impaired investments and a $0.8 million loss on investments sold, offset partially by $1.6 million of dividend income and a $0.5 million increase in the fair market value of trading securities. Investment income in 2001 was due primarily to recognition of gains on investments liquidated.

The fair market value adjustment of our position in a ten-year $100 million interest rate contract decreased by $7.7 million in fiscal 2003 and $4.6 million in 2002. The fair market value adjustment of this agreement will generally fluctuate, based on the implied forward interest rate curve for 3-month LIBOR. If the implied forward interest rate curve decreases, the fair market value of the interest rate contract will increase and we will record an additional charge. If the implied forward interest rate curve increases, the fair market value of the interest rate contract will decrease, and we will record income. Declining interest rates have caused the recorded change in fair market value of the contract.

We recorded an income tax provision of $0.4 million in fiscal 2003 on pre-tax losses from continuing operations. A tax provision was recorded due primarily from state income taxes. We recorded an income tax benefit of $16.0 million in fiscal 2002, representing a 22.3% effective tax rate benefit on pre-tax losses from continuing operations. The tax benefit resulted primarily from the reversal of tax accruals no longer required, and was lower than the statutory rate due primarily to federal income tax net operating loss carryforwards, which we had at June 30, 2002. We recorded an income tax benefit of $28.7 million in fiscal 2001, representing a 42.0% effective tax rate on pre-tax losses from continuing operations. The tax benefit was higher than the statutory rate due primarily to the reversal of $3.5 million of tax accruals no longer required.

Equity in earnings of affiliates decreased by $0.9 million in 2003, as compared to 2002 and decreased by $0.2 million in 2002, as compared to 2001. The decrease in 2003 reflected equity investments written down by $0.9 million for impairment. The decrease in 2002 reflected $0.1 million of equity losses in 2002 as compared to equity income of $0.1 million in 2001.

Earnings from discontinued operations include the results of the fasteners business prior to its sale, and APS. The current period reductions in earnings reflect our ownership of the fastener business for only five months in 2003, as compared to the full year in 2002.

In 2003, we recorded a $29.8 million gain on the disposal of discontinued operations, net of $20.5 million of taxes, as a result of the sale of the fastener business.

In 2002, we recorded a goodwill impairment charge of $144.6 million from the implementation of SFAS No. 142, presented as a cumulative effect of change in accounting, as of the beginning of our fiscal year. Of this amount, $19.3 million relates to our Fairchild Aerostructures operating unit in our aerospace manufacturing segment and $125.3 million relates to our fastener business sold to Alcoa on December 3, 2002. No tax effect was recognized on the change in accounting for goodwill. Instead of amortizing goodwill and intangible assets deemed to have an indefinite life, goodwill will be tested for impairment annually, or immediately if conditions indicate that such an impairment could exist. All of our goodwill has been deemed to have an indefinite life; and as a result of adopting SFAS No. 142, we ceased amortizing goodwill. Included in our operating results was $6.6 million of goodwill impairment at our aerospace distribution segment in 2003 and, prior to the implementation of SFAS No. 142 , we recognized amortization expense for goodwill of $12.5 million in 2001.

Other comprehensive income includes foreign currency translation adjustments, unrecognized actuarial loss on pensions, and unrealized periodic holding changes in the fair market value of available-for-sale investment securities. In 2003, other comprehensive income included a decrease of $60.8 million due to the recognition of an additional minimum pension liability due primarily to unrecognized actuarial losses, offset partially by an increase of $19.6 million in foreign currency translation adjustments which were realized as part of the sale of our fasteners business and a $1.8 million increase in the fair market value of unrealized holding gains on investment securities. The fair market value of available-for-sale securities, on an after-tax basis, declined by $0.6 million and $1.0 million in 2002 and 2001, respectively. The changes in 2001 reflect primarily gains realized from the liquidation of investments. Foreign currency translation adjustments improved by $21.6 million in 2002, which reflected the strengthening of the EURO to the U.S. Dollar. Foreign currency translation adjustments decreased by $24.5 million in 2001 due to the strengthening of the U.S. Dollar against the EURO.

Segment Results

Aerospace Distribution Segment

Our aerospace distribution business is an international supplier to the airlines, corporate aviation, and the military. The business operates from five locations in the United States and specializes in the distribution of avionics, airframe accessories, and other components. Products include: navigation and radar systems, instruments, and communication systems, flat panel technologies and rotables. The company also overhauls and repairs, landing gear, pressurization components, instruments, and avionics. Customers include commuter and regional airlines, corporate aircraft and fixed-base operators, air cargo carriers, general aviation suppliers and the military. Sales in our aerospace distribution segment decreased by $3.7 million, or 5.8%, in 2003, as compared to 2002. Sales in 2003 were adversely affected by the overall conditions in the aerospace industry, resulting primarily from the events of September 11, 2001, and the general weakness in the overall economy. Sales in our aerospace dist ribution segment decreased by $22.6 million in 2002, compared to 2001. Results in 2001, included revenue of $8.4 million from an operation which was shut down in June 2001. Sales in 2002 were also adversely affected due to the events of September 11, 2001.

The operating loss of $4.1 million in 2003, included $6.6 million of goodwill impairment charges. Excluding the goodwill impairment charges recognized in 2003, operating income decreased by $0.1 million as compared 2002 reflecting the decrease in sales and a 0.5% decrease in gross margin as a percentage of sales, offset partially by a 0.6% reduction in selling, general and administrative costs as a percentage of sales. Operating income increased by $0.3 million in 2002, as compared to 2001. The results in 2002 were affected by the reduction in revenue. Operating income in 2001 included asset impairment charges of $3.1 million due to the closing of Banner Aircraft Services, which also reported operating losses of $3.9 million in 2001.

Aerospace Manufacturing Segment

Sales in our aerospace manufacturing segment decreased by $4.0 million in 2003, as compared to 2002. The change reflected a reduction in shipments in the current period due to an overall lower level of demand in the aerospace industry resulting from the September 11, 2001 terrorist attacks and the recent financial difficulties of major commercial airlines. Sales in our aerospace manufacturing segment increased by $4.9 million, or 59.7%, in 2002, as compared 2001. The improvement reflected internal growth. However, sales decreased in the third and fourth quarters of fiscal 2002, due to a reduction in shipments resulting from an overall lower level of demand in the aerospace industry following the September 11, 2001 terrorist attacks.

Operating results improved by $3.8 million in 2003, as compared to 2002. The improvement reflects primarily impairment charges of $3.0 million to write down long-lived assets, and $1.3 million to write down inventory through cost of goods sold recognized in 2002, offset partially by a 2.0% increase in selling, general and administrative costs as a percentage of sales. Operating results in our aerospace manufacturing segment decreased by $4.2 million in 2002, as compared to 2001. The decrease was due primarily to impairment charges of $3.0 million to write down long-lived assets, and $1.3 million to write down inventory through cost of goods sold. Goodwill amortization of $0.5 million was recorded in 2001.

On December 3, 2002, we sold our fastener business for approximately $657 million in cash to Alcoa Inc. Additionally, in February 2003, we adopted a formal plan to sell APS. The company expects to sell APS by December 2003. Accordingly, the results of our fastener business and APS have been restated to report them as discontinued operations.

Real Estate Operations Segment

Our real estate operations segment owns and operates a 451,000 square foot shopping center located in Farmingdale, New York and also owns and leases a 102,000 square foot building in Chatsworth, California and a 208,000 square foot manufacturing facility located in Fullerton, California. We have two tenants that each occupy more than 10% of the rentable space of the shopping center. Rental revenue was $8.7 million in 2003, $7.2 million in 2002, and $7.5 million in 2001. Rental revenue increased by 21.5% in 2003, as compared to 2002, reflecting the lease of the Fullerton property and tenants occupying an additional 66,000 square feet of the shopping center. Rental revenue decreased by 4.5% in 2002, as compared to 2001, due to a decrease in the average per square foot amount charged to tenants in 2002. The weighted average occupancy rate of the shopping center was 87.1%, 76.9% and 74.4% in 2003, 2002, and 2001, respectively. The average effective annual rental rate per square foot of the shopp ing center was $20.27, $19.22, and $20.91 in 2003, 2002, and 2001, respectively. As of June 30, 2003, approximately 91% of the shopping center was leased. We anticipate that rental income will increase during 2004, as a result of a new lease for approximately 30,000 square feet, entered into shortly after the end of 2003. The Chatsworth property is leased through July 2008, and is expected to generate revenues and operating income of approximately $0.5 million per year. The Fullerton property is leased to Alcoa through October 2007, and is expected to generate revenues and operating income in excess of $0.5 million per year.

Operating income increased by $1.2 million to $2.7 million in 2003, as compared to $1.5 million in 2002. In 2003, repairs and maintenance expense and depreciation expense increased by $0.3 million and $0.2 million, respectively, as a result of an increased weighted-average portion of the shopping center being placed into service in 2003. Operating income increased by $1.2 million to $1.5 million in 2002, as compared to $0.3 million in 2001. In 2002, depreciation expense and real estate taxes increased by $0.5 million and $0.2 million, respectively, as a result of an increased weighted-average portion of the shopping center being placed into service in 2002. The results for 2001 were adversely affected by a charge of $2.5 million to write-off improvements at the shopping center.

Corporate Segment

The operating results at corporate in 2003 includes $13.7 million of one-time change of control payments required under contracts with our top four executives as a result of the sale of the fastener business, and $10.4 million of bonuses awarded to our top four executives as a result of the sale of the fastener business. The top four executives also have relinquished their right to any other future change of control payments. Other income at corporate decreased by $4.3 million in 2003, as compared to 2002, due primarily to income recognized in 2002 from the disposition of future royalty revenues to an unaffiliated third party in exchange for promissory notes. In January 2003, we reduced our corporate staff by approximately 24%. Severance expense associated with the reduction was $1.1 million in 2003.

The corporate segment operating loss in 2002 decreased by $1.3 million, or 7.1%, as compared to 2001. Results from 2001 included $3.1 million of gains recognized on the disposition of non-core assets. Results in each of 2002 and 2001, included consulting income of $1.5 million from a consulting agreement that expired on June 30, 2002.

FINANCIAL CONDITION, LIQUIDITY AND CAPITAL RESOURCES

Our combined cash and investment balances increased by $100.8 million to $121.9 million on June 30, 2003, as compared to $21.1 million on June 30, 2002. Our debt was reduced by $485.1 million, to $6.7 million on June 30, 2003, as compared to $491.8 million on June 30, 2002. Total capitalization was $144.5 million and $722.0 million as of June 30, 2003 and June 30, 2002, respectively. The change in capitalization included the $485.1 million decrease in debt reflecting repayment with the proceeds received from the sale of the fasteners business, and a decrease in equity of $92.4 million. The change in equity was due primarily to our reported net loss and changes in other comprehensive income, which included a decrease of $60.8 million, due to the recognition of the additional minimum pension liability, offset partially by a $19.6 million reversal of prior decreases in foreign currency translation adjustments, which were realized as part of the sale of our fasteners business.

Net cash used for operating activities for 2003, was $122.5 million. The working capital uses of cash in 2003 included $47.4 million of cash used for investments in trading securities, $7.4 million contributed to fund our pension plan, $13.7 million of one-time change of control payments required under contracts with our top four executives as a result of the sale of the fastener business, $10.4 million of bonuses awarded to our top four executives as a result of the sale of the fasteners business, and $30.4 of non-cash charges and working capital changes provided to discontinued operations. Net cash provided by operating activities for 2002 was $19.4 million. The working capital uses of cash in 2002 included a $5.2 million decrease in accounts payable and other accrued liabilities and a $19.6 million increase in other non-current assets, offset partially by a $4.8 million decrease in accounts receivable, a $7.1 million decrease in other current assets, and a $4.5 million decrease in invento ry. The working capital uses of cash were offset by $20.0 million of non-cash charges and working capital changes provided from discontinued operations, and $5.3 million of earnings, after deducting non-cash expenses of $5.2 million for depreciation, $2.1 million from the amortization of deferred loan fees, $144.6 million for the cumulative effect of the change in accounting for goodwill, $3.4 million loss from impairments, and $4.6 million from the reduction in the fair market value of an interest rate contract. Net cash used for operating activities for fiscal 2001 was $40.2 million. The primary use of cash for operating activities in 2001 was a $104.9 million decrease in accounts payable and other accrued liabilities, offset partially by a $3.2 million decrease in accounts receivable, a $33.5 million increase in other current assets, a $2.7 million increase in inventories, and $32.5 million of non-cash charges and working capital changes provided from discontinued operations.

Net cash provided by investing activities for 2003, was $605.6 million. In 2003, the primary source of cash was $657.1 million of proceeds from the sale of our fastener business, $13.4 million of net cash proceeds received from notes receivable, and $2.5 million cash proceeds received from net assets held for sale. Net cash provided by investing activities was offset partially by $54.7 million of new investments, $9.9 million of capital expenditures, including the purchase of a manufacturing facility located in Fullerton, California, and $2.8 million of investing activities used for discontinued operations. Net cash used for investing activities was $9.6 million in 2002. The primary source of cash in 2002 was $4.0 million provided from the dispositions of non-core real estate and net assets held for sale, offset by $2.5 million of capital expenditures and a $5.8 increase in notes receivable and $6.6 million of investing activities used for discontinued operations. Net cash provided from inve sting activities for 2001 was $18.2 million, and included $28.0 million in proceeds received from the dispositions of investments, and $1.5 million in proceeds received from the disposition of property, offset by $3.8 million of capital expenditures, and by $9.7 million of investing activities used for discontinued operations.

Net cash used by financing activities was $485.8 million for 2003, which reflected the repayment of essentially all of our debt, except for a $3.4 million margin loan and $3.2 million of debt at Fairchild Aerostructures. Net cash used for financing activities in 2002 included a $9.6 million decrease in debt. Net cash provided by financing activities in 2001 was $15.4 million, and included a $14.7 million net issuance of additional debt used to fund operations.

At June 30, 2002, $5.6 million of promissory notes were due to us from an unaffiliated third party, which are included in notes receivable. The promissory notes earn $1.4 million of annual cash interest and were being accreted to a face value of $12.8 million through May 2006. The promissory notes are secured by $12.8 million face value of our outstanding 10.75% senior subordinated debentures due 2009 acquired by the third party. As a result of the sale of the fastener business on December 3, 2002, we redeemed for cash the debentures held by the third party, and the third party then satisfied its obligation under its promissory notes.

Our principal cash requirements include acquisitions, capital expenditures, and the payment of other liabilities including postretirement benefits, environmental investigation and remediation obligations, and litigation settlements and related costs. We expect that cash on hand, cash generated from operations, cash available from borrowings, and proceeds received from dispositions of assets, including investments, will be adequate to satisfy our cash requirements during the next twelve months. In the second quarter of 2004, we may convert a large portion of our investments into cash or cash equivalents. Cash and cash equivalents, including investments in government securities, currently have much lower yields than the short-term bonds and other items we are currently invested in. We may also buy back up to 10% of our current outstanding Class A common stock, subject to market conditions, during the six months following the filing of this document.

We have entered into discussions with a lender to receive a 10-year, non-recourse, fixed rate, term-loan financing on our shopping center at interest rates currently approximating 6.1%.

Prior to the sale of our fastener business, the Pension Benefit Guaranty Corporation had contacted us to understand the impact of the sale of our fasteners business on our ability to fund our long-term pension obligations. The PBGC expressed concern that our retirement plan would be underfunded by $86 million after the sale of our fasteners business. We provided the PBGC with information, which represented the underfunding to be $42 million, using the PBGC plan termination assumptions. During 2003, we contributed $7.4 million of cash to fund this pension plan. Based upon our actuary's assumptions and projections, we do not expect additional cash contributions to this pension plan to be required until 2008.

At June 30, 2003, we had contractual commitments to repay debt (including capital lease obligations), and to make payments under operating leases. Payments due under these long-term obligations are as follows:

	2004	2005	2006	2007	2008	Thereafter	Total
Long-term debt and capital lease obligations	$ 468	$ 219	$ 92	$ 88	$ 83	$ 2,333	$ 3,283
Operating lease commitments	2,338	1,698	1,418	806	384	1,207	7,851
Total contractual cash obligations	$ 2,806	$ 1,917	$ 1,510	$ 894	$ 467	$ 3,540	$ 11,134

We have entered into standby letter of credit arrangements with insurance companies and others, issued primarily to guarantee our future performance of contracts. At June 30, 2003, we had contingent liabilities of $2.3 million on commitments related to outstanding letters of credit.

In addition, we have $13.1 million classified as other long-term liabilities at June 30, 2003, including environmental and other liabilities, which do not have specific payment terms or other similar contractual arrangements.

At June 30, 2003, we have $130.3 million of federal income tax loss carryforwards expiring 2019 through 2022, and $4.9 million of unused alternative minimum tax credit carryforwards that do not expire. These federal income tax loss carryforwards may be reduced by adjustments during the income tax audits of 1995 through 2003, which have not been completed. As the periods of assessment for 1995 to 1998 have expired, additional tax may be collected from us only for 1999 to 2003. Nonetheless, the tax losses of $68.3 million arising in 1995, 1997, and 1998 may still be reduced for determining the proper amount of net operating loss available to be carried forward to years after 1998. The gain we reported between 1995 to 2003, for federal income tax, may be significantly increased if our tax positions are not sustained with respect to the sales of several businesses; and the repayment with property, of debt under a bank credit agreement in which both we and our subsidiaries were liable, is not tre ated as tax free under Section 361 of the Internal Revenue Code of 1986, as amended. If all of these adjustments were made for 1995 to 2003, the federal income tax loss carryforwards would be substantially reduced, and we may be required to pay additional tax and interest of up to $69 million, which has already been provided. The amount of additional tax and interest to be paid by the Company depends on the amount of income tax audit adjustments, which are made and sustained for 1995 to 2003. These adjustments, if any, would be made at a future date, which is presently uncertain, and therefore we cannot predict the timing of cash outflows. To the extent a favorable final determination of the recorded tax liabilities occurs, appropriate adjustments will be made to decrease the recorded tax liability in the year such favorable determination will occur. It is presently uncertain when a final determination will occur since no Internal Revenue Service audits of 1995 to 2002 have been completed.

RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In July 2002, the FASB issued Statement of Financial Accounting Standards No. 146, "Accounting for Costs Associated with Exit or Disposal Activities". This standard requires costs associated with exit or disposal activities to be recognized when they are incurred and applies prospectively to such activities initiated after December 31, 2002. This standard has no impact on our financial statements.

Effective June 30, 2003, we adopted SFAS No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." This statement amends and clarifies financial accounting and reporting for derivatives and for hedging activities under SFAS No. 133, "Accounting for Derivative Instruments and Hedging Activities." This standard has no impact on our financial statements.

In May 2003, the Financial Accounting Standards Board issued SFAS No. 150, "Accounting for Certain Instruments with Characteristics of Both Liabilities and Equity." This standard requires that certain financial instruments embodying an obligation to transfer assets or to issue equity securities be classified as liabilities. It is effective for financial instruments entered into or modified after May 31, 2003, and otherwise is effective July 1, 2003. This standard has no impact on our financial statements.

Financial Interpretation 45 "Guarantor's Accounting and Disclosure Requirements for Guarantees of Indebtedness of Others" was issued in November 2002. FIN 45 was effective for periods ending after December 15, 2002. FIN 45 has no impact on our financial statements.

Financial Interpretation 46 "Consolidation of Variable Interest Entities" was issued in January 2003. FIN 46 requires that variable interest entities created before February 1, 2003 be consolidated during the first interim period after June 15, 2003. We have determined that, for our first quarter ending on September 30, 2003, we will consolidate our limited partner interest in a landfill development partnership in which we are the source of funds.

ITEM 7A. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

In fiscal 1998, we entered into a ten-year interest rate swap agreement to reduce our cash flow exposure to increases in interest rates on variable rate debt. The ten-year interest rate swap agreement provides us with interest rate protection on $100 million of variable rate debt, with interest being calculated based on a fixed LIBOR rate of 6.24% to February 17, 2003. On February 17, 2003, the bank, with which we entered into the interest rate swap agreement, did not exercise a one-time option to cancel the agreement, and accordingly the transaction will proceed, based on a fixed LIBOR rate of 6.745% from February 17, 2003 to February 19, 2008.

The interest rate swap agreement was executed to provide an economic hedge against cash flow variability on the floating rate note. When evaluating the impact of SFAS No. 133 on this hedge relationship, we assessed the key characteristics of the interest rate swap agreement and the note. Based on this assessment, we determined that the hedging relationship would not be highly effective. The ineffectiveness is caused by the existence of the embedded written call option in the interest rate swap agreement, and the absence of a mirror option in the hedged item. As such, pursuant to SFAS No. 133, we designated the interest rate swap agreement in the no hedging designation category. Accordingly, we do not use hedge accounting. We have recognized a non-cash decrease in the fair market value of interest rate derivatives, of $7.7 million, $4.6 million and $5.6 million in 2003, 2002, and 2001, respectively, as a result of the fair market value adjustment for our interest rate swap agreement.

The fair market value adjustment of these agreements will generally fluctuate based on the implied forward interest rate curve for 3-month LIBOR. If the implied forward interest rate curve decreases, the fair market value of the interest hedge contract will increase and we will record an additional charge. If the implied forward interest rate curve increases, the fair market value of the interest hedge contract will decrease, and we will record income.

The table below provides information about our financial instruments that are sensitive to changes in interest rates. Notional amounts are used to calculate the contractual payments to be exchanged under the contract. Weighted average variable rates are based on implied forward rates in the yield curve at the reporting date.

(In thousands)

Expected maturity date	February 19, 2008
Type of interest rate contract	Variable to Fixed
Variable to fixed contract amount	$100,000
Fixed LIBOR rate	6.745%
Weighted average forward LIBOR rate	2.48%
Fair market value at June 30, 2003	$(18,662)

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

The following consolidated financial statements of the Company and the report of our independent auditors, are set forth below.

Supplementary information regarding "Quarterly Financial Data (Unaudited)" is set forth under Item 8 in Note 19 to Consolidated Financial Statements.

Report of KPMG LLP, Independent Auditors

To the Board of Directors of The Fairchild Corporation:

We have audited the accompanying consolidated balance sheet of The Fairchild Corporation and subsidiaries (the "Company") as of June 30, 2003, and the related consolidated statements of operations and other comprehensive income (loss), stockholders' equity and cash flows for the year then ended. These consolidated financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audit. The consolidated balance sheet of the Company as of June 30, 2002, and the related consolidated statements of operations and other comprehensive income (loss), stockholders' equity, and cash flows for each of the two years in the period ended June 30, 2002 were audited by other auditors whose report dated March 28, 2003 expressed an unqualified opinion on those consolidated financial statements.

We conducted our audit in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. 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 audit provides a reasonable basis for our opinion.

In our opinion, the 2003 consolidated financial statements referred to above present fairly, in all material respects, the financial position of The Fairchild Corporation and subsidiaries at June 30, 2003, and the results of their operations and their cash flows for the year then ended, in conformity with accounting principles generally accepted in the United States.

/s/ KPMG LLP

McLean, Virginia

September 12, 2003

Report of Ernst & Young LLP, Independent Auditors

To the Board of Directors of The Fairchild Corporation:

We have audited the accompanying consolidated balance sheet of The Fairchild Corporation and subsidiaries (the "Company") as of June 30, 2002, and the related consolidated statements of operations and other comprehensive income (loss), stockholders' equity, and cash flows for each of the two years in the period ended June 30, 2002. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. 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 financial statements referred to above present fairly, in all material respects, the consolidated financial position of The Fairchild Corporation and subsidiaries at June 30, 2002, and the consolidated results of their operations and their cash flows for each of the two years in the period ended June 30, 2002, in conformity with accounting principles generally accepted in the United States.

As discussed in Note 3 to the consolidated financial statements, effective July 1, 2001, the Company adopted Statement of Financial Accounting Standard No. 142, "Accounting for Goodwill and Other Intangible Assets."

As discussed in Note 1 to the consolidated financial statements, effective July 1, 2001, the Company adopted Statement of Financial Accounting Standard No. 144, "Accounting or Disposal of Long-Lived Assets."

/s/ Ernst & Young LLP

McLean, Virginia

March 28, 2003

THE FAIRCHILD CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In thousands)

ASSETS	June 30, 2003	June 30, 2002
CURRENT ASSETS:		
Cash and cash equivalents	$ 12,017	$ 14,810
Short-term investments	48,403	966

Accounts receivable-trade, less allowances of $1,598 and $2,577	16,327	12,232
Inventories:		
Finished goods	24,708	20,382
Work-in-process	723	1,555
Raw materials	308	1,311
	25,739	23,248
Current assets of discontinued operations	728	286,769
Prepaid expenses and other current assets	3,590	3,891
Total Current Assets	106,804	341,916
Property, plant and equipment, net of accumulated		
depreciation of $26,081 and $22,228	126,574	119,757
Net noncurrent assets held for sale	312	9,928
Noncurrent assets of discontinued operations	125	384,145
Goodwill	10,821	17,438
Investments and advances, affiliated companies	7,136	3,261
Prepaid pension assets	59,892	64,693
Deferred loan costs	1,071	10,925
Long-term investments	61,486	5,360
Notes receivable	7,801	11,275
Deferred income tax assets	-	16,611
Other assets	8,527	6,809
TOTAL ASSETS	$ 390,549	$ 992,118

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

THE FAIRCHILD CORPORATION AND SUBSIDIARIES

CONSOLIDATED BALANCE SHEETS

(In thousands)

LIABILITIES AND STOCKHOLDERS' EQUITY	June 30,	June 30,
	2003	2002
CURRENT LIABILITIES:		
Bank notes payable and current maturities of long-term debt	$ 3,879	$ 53,879
Accounts payable	11,262	9,456
Accrued liabilities:		
Salaries, wages and commissions	10,408	4,625
Employee benefit plan costs	2,531	2,025
Insurance	13,460	10,465
Interest	704	6,365
Other accrued liabilities	12,231	21,294
Income taxes	1,703	702
Current liabilities of discontinued operations	859	69,059
Total Current Liabilities	57,037	177,870
LONG-TERM LIABILITIES:		
Long-term debt, less current maturities	2,815	437,917
Fair value of interest rate contract	18,662	10,989
Other long-term liabilities	13,101	13,569
Pension liabilities	63,829	-
Retiree health care liabilities	27,894	28,011
Noncurrent income taxes	69,395	53,791
Noncurrent liabilities of discontinued operations	-	39,749
TOTAL LIABILITIES	252,733	761,896
STOCKHOLDERS' EQUITY:		
Class A common stock, $0.10 par value; 40,000 shares authorized,		
30,377 (30,354 in 2002) shares issued and 22,563 (22,540 in 2002);		
shares outstanding; entitled to one vote per share	3,037	3,035
Class B common stock, $0.10 par value; 20,000 shares authorized,		
2,622 shares issued and outstanding; entitled to ten votes per share	262	262

Paid-in capital	232,741	232,797
Treasury stock, at cost, 7,814 shares of Class A common stock	(76,459)	(76,532)
Retained earnings	40,961	94,153
Notes due from stockholders	(1,508)	(1,831)
Cumulative other comprehensive loss	(61,218)	(21,662)
TOTAL STOCKHOLDERS' EQUITY	137,816	230,222
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$ 390,549	$ 992,118

The accompanying Notes to Consolidated Financial Statements are an integral part of these statements.

THE FAIRCHILD CORPORATION AND SUBSIDIARIES

CONSOLIDATED STATEMENTS OF OPERATIONS AND OTHER COMPREHENSIVE INCOME (LOSS)

(In thousands, except per share data)

	For the years ended June 30,		
REVENUE:	2003	2002	2001
Net sales	$ 68,820	$ 76,531	$ 94,192
Rental revenue	8,699	7,159	7,498
	77,519	83,690	101,690
COSTS AND EXPENSES:			
Cost of goods sold	54,792	61,059	72,030
Cost of rental revenue	5,665	4,917	4,622
Selling, general & administrative	61,344	39,594	40,517
Other (income) expense, net	(2,581)	(4,293)	(4,181)
Amortization of intangibles	-	-	1,097
Impairment charges			