

FREQUENCY ELECTRONICS INC

FORM 10-K (Annual Report)

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Telephone 5167944500
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Industry Electronic Instr. & Controls
Sector Technology
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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, 2016

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

Name of each exchange on which registered

Common Stock (par value \$1.00 per share)

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

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

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T (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 No

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

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See 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

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

The aggregate market value of voting stock held by non-affiliates of the Registrant as of October 31, 2015 - \$67,100,000

The number of shares outstanding of Registrant's Common Stock, par value \$1.00 as of July 22, 2016 – 8,729,682

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 November 1, 2016.

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 generation technology, which is employed in commercial, government, Command, Control, Communication, Computer, Intelligence, Security and Reconnaissance ("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.

Frequency Electronics was founded in 1961 as a research and development firm generating proprietary precision time and frequency technology primarily under contracts for end-use by the United States ("U.S.") Government. 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 end market is satellite payloads, a market in which 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 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. In addition, there are various mega-constellations being planned for the very near future that will operate in low and mid earth orbits.

The Company's products support multiple C4ISR counter measures and additional defense electronic applications for the U.S. Government on land, sea and air-borne platforms. Recently identified threats to the communication capabilities of U.S. Government facilities through jamming, multi-path or "spoofing" GPS signals may be mitigated by the Company's technologies. High precision, ruggedized clocks combined with specialized software are essential for communication and operational security.

Commercial markets include network infrastructure and other industrial uses. The Company's products support precise signal synchronization in mobile and wireline 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 ("RTUs") 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.

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, as well as products for certain terrestrial commercial communications and other industrial applications.

Frequency Electronics, Inc. Asia ("FEI-Asia") was established in fiscal year 2002 as a wholly-owned subsidiary, to be the Company's Asia-based low cost manufacturer of certain commercial communications products used primarily in the wireless and wireline markets as well as power grids. FEI-Asia is located in the Free-Trade Zone in Tianjin, China.

The Company's subsidiary, FEI-Elcom Tech, Inc. ("FEI-Elcom") designs and manufactures Radio Frequency ("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. FEI-Elcom's RF microwave technology has also been utilized to develop new products for application in the Company's satellite payload end market.

2. **Gillam-FEI** - The Company's Belgian subsidiary, Gillam-FEI, s.a. ("Gillam-FEI") develops and manufactures products for various network management and synchronization systems for different industries, utilities, railways 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"). 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.

For additional information about these reportable segments, see "Item 1. Business – Reportable Segments and Products."

In addition to its subsidiaries, the Company made a strategic investment in and licensed certain technology to 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. For more information regarding the Company's investment in Morion, see Note 9 to Consolidated Financial Statements.

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 historically minimal sales to outside customers. Beginning in late fiscal year 2014, FEI-Asia began shipping higher volumes of product to third parties as a contract manufacturer. FEI-Elcom, in addition to its own product line, provides design and technical support for the FEI-NY segment's satellite business. The products manufactured by 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 and rugged high-precision-clocks that are designed and manufactured at FEI-NY. 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 2016 and 2015, approximately 73% and 81%, respectively, of the Company's consolidated revenues were from products sold by the FEI-NY segment. Sales by Gillam-FEI were approximately 10% of consolidated revenues for fiscal years 2016 and 2015. In fiscal years 2016 and 2015, sales for the FEI-Zyfer segment were 20% and 12% 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, primarily in Europe and China. During fiscal years 2016 and 2015, foreign sales comprised 19% and 31%, respectively, of consolidated revenues. For segment information, see Note 13 to the Consolidated Financial Statements.

FEI-NY SEGMENT :

The Company provides precision time, frequency generation and synchronization products and subsystems that are found on-board satellites, in ground-based communication stations, 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 satellites, 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 Constellation, Intelsat EPIC, O3B, WAAS, MexSat, MSV, ICO, TerreStar, EchoStar, Inmarsat and numerous others. The Company is also positioned to participate in certain large constellations being planned for the very near future that will operate in low or mid earth orbits such as the O3B Next Generation Constellation and the LeoSat constellation that consists of up to 108 satellites.

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. Government'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.

The federal budget for U.S. military programs has been under intense scrutiny in recent years. The Budget Control Act of 2011, which went into effect in March 2013, was an example of U.S. Government efforts to reduce the federal deficit by a process known as sequestration. Due to continuing budgetary concerns, future annual budgets proposed by the federal administration and Congress may include lower spending for U.S. military programs. As indicated above, many of the programs and platforms for which the Company supplies products and systems, are used by the U.S. Government for maintaining secure communications world-wide, for obtaining vital intelligence and for 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 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. The Company's experience indicates that some programs or product sales have been 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.

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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. The last full DCAA audit was performed in 2008, however the Company is required annually to submit an incurred cost report at the end of October for the year that ended the preceding April. All reports have been submitted and approved except for the report for fiscal 2015, for which the Company has not received a rate approval letter yet.

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. There were no end-use contracts terminated for the year ended April 30, 2016.

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 towards telecommunication operators and network equipment manufacturers that utilize modular and flexible platforms to build reliable digital-network-systems worldwide. Telecommunications operators such as The Proximus Group, formerly known 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 markets variants of 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 85% 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. Recently identified threats to the communication capabilities of U.S. Government facilities through jamming, multi-path or "spoofing" GPS signals may be mitigated by FEI-Zyfer's technologies and products. High precision, ruggedized clocks combined with specialized software are essential for communication and operational security.

BACKLOG

As of April 30, 2016, the Company's consolidated backlog amounted to approximately \$32 million compared to approximately \$37 million at the end of the prior fiscal year. Approximately 75% of the current backlog is expected to be filled during the Company's fiscal year ending April 30, 2017. As of April 30, 2016, there are no amounts included in backlog under cost-plus fee contracts. 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. The Company expects any partially funded contracts to become fully funded over time and will add the additional funding 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, which includes the revenues of its overseas subsidiaries, totaled approximately 19% and 31%, respectively, of net revenues in fiscal years 2016 and 2015.

The Company's products are sold to both commercial and governmental customers. For the years ended April 30, 2016 and 2015, approximately 60% and 47%, 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 2016, Boeing Corporation ("Boeing"), Lockheed Martin Corporation ("Lockheed"), Northrop Grumman Corporation ("Northrop") and Space and Intelligence Systems/Harris Corporation ("Harris"), each accounted for more than 10% of FEI-NY segment revenues; additionally, Boeing and Lockheed also each accounted for more than 10% of consolidated revenues. During fiscal year 2015, Boeing, Northrop, and Thales Alenia Space ("Thales") each accounted for more than 10% of FEI-NY segment revenues; Boeing and Thales also each accounted for more than 10% of consolidated revenues.

During fiscal years 2016 and 2015, The Proximus Group, formerly known as Belgacom, was a major customer of the Gillam-FEI segment, accounting for more than 10% of that segment's revenues in each year.

During fiscal year 2016, Copper River Information Technology and Raytheon Company were major customers of the FEI-Zyfer segment, each accounting for more than 10% of the segment's revenues. During fiscal year 2015, L-3 Communications and Copper River Information Technology each 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 2016 and 2015, the Company expended \$5.9 million and \$5.7 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 2016 and 2015, some of the Company's development resources were applied to certain cost-plus-fee contracts and the design-stage of fixed-price satellite payload programs. For fiscal year 2017, the Company anticipates that internal research and development spending will not exceed the amount expended during fiscal year 2016 and will remain at less than 10% of revenues. The actual amount spent in fiscal year 2017 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, 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, such as in space or in other extremely hostile environments, and the Company's track record of 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. With respect to very high precision products, the Company encounters fewer competitors than it does 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 Boeing, Northrop, 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 Excelitas Technologies Corp. (a Veritas Capital portfolio company), Microsemi Corporation and Vectron, Inc., a division of Dover Corp. The Company also competes against multiple foreign entities including Korean and other Asian enterprises such as the Chinese company, Huawei. In Europe large competitors include Siemens, Schneider Electric and Oscilloquartz, a division of ADVA Optical Networking SE.

The Company has successfully outsourced certain manufacturing processes to third parties and to its wholly-owned subsidiary, FEI-Asia in Tianjin, China and to Russia-based Morion, 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 390 full-time persons worldwide. None of the U.S. or Chinese employees are 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:

Martin B. Bloch	- President, Chief Executive Officer and Director
Markus Hechler	- Executive Vice President, President of FEI Government Systems, Inc. and Secretary and Treasurer
Oleandro Mancini	- Senior Vice President, Business Development
Steven Strang	- President, FEI-Zyfer
James Davis	- President, FEI-Elcom Tech
Leonard Martire	- Vice President, Program Management
Thomas McClelland	- Vice President, Advanced Development
Adrian Lalicata	- Vice President, RF & Microwave Systems
Steven L. Bernstein	- Chief Financial Officer

None of the officers and directors is related.

Martin B. Bloch, age 80, 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 70, 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.

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Oleandro Mancini, age 67, 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 52, 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 20 years in various technical and management positions.

James Davis, age 63, is the President of FEI-Elcom Tech, Inc. which the Company acquired in February 2012. Mr. Davis was named an officer of the Company in October 2013. Mr. Davis became the president of Elcom Technologies, Inc., the pre-acquisition company, on September 20, 2007. Prior to joining FEI-Elcom, Mr. Davis held leadership positions at other technology companies including General Manager of Hewlett Packard's (Agilent) Semiconductor Systems Center, Vice President and General Manager of Schlumberger Technologies N.A. and Vice President and General Manager of Gretag Macbeth LLC. Mr. Davis also held the rank of Captain as a U.S. Army Special Forces Team Commander.

Leonard Martire, age 79, 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 61, 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 69, 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.

Steven L. Bernstein, age 51, joined the Company in April 2010 as its controller and was appointed to the position of Chief Financial Officer in April 2016. Prior to joining the Company, Mr. Bernstein worked in the North America accounting group of a Fortune 500 electronics distributor.

Item 1A. Risk Factors

This item is not required for smaller reporting companies.

Item 1B. Unresolved Staff Comments

This item is not required for smaller reporting companies.

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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:

Location	Size (sq. ft.)	Own or Lease
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 followed by two five-year renewal periods. The Company is currently in the second 5-year renewal period paying annual rent of \$800,000 per year plus its pro rata share of real estate taxes and the costs of utilities and insurance. 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 approximately \$31,200 and will remain constant over the remaining 16 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 under a 9-year lease, cancelable after three years, at an approximate rate of \$1,000 per month. 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 \$5,000 through February 2017. 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 2018, requires monthly payments of \$39,900.

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 21, 2016, the Company is not a party to any material, pending legal proceeding other than routine litigation incidental to its business.

Item 4. Mine Safety Disclosures

Not applicable.

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.

FISCAL QUARTER	HIGH SALE	LOW SALE
2016-		
FIRST QUARTER	\$ 13.42	\$ 10.33
SECOND QUARTER	11.46	9.95
THIRD QUARTER	11.28	8.51
FOURTH QUARTER	11.00	8.83
2015 -		
FIRST QUARTER	\$ 12.50	\$ 10.31
SECOND QUARTER	12.50	10.50
THIRD QUARTER	11.99	10.00
FOURTH QUARTER	14.80	11.35

As of July 22 2016, the approximate number of holders of record of common stock was 675. The closing share price of the Company's stock on April 30, 2016 was \$10.13. The closing share price of the Company's stock on July 22, 2016 was \$10.42.

DIVIDEND POLICY

The Board of Directors reviews the Company's dividend policy at each regular meeting. No dividends were declared or paid during fiscal years 2016 and 2015.

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 2016 or 2015.

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>
	(a)	(b)	(c)
Equity Compensation Plans			
Approved by Security Holders (1)	1,660,125	\$ 9.02	16,336

(1) The Company's equity compensation plans are described in Note 11 to the Consolidated Financial Statements.

Item 6. Selected Financial Data

This item is not required for smaller reporting companies.

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 the full amount of 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.

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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.

RESULTS OF OPERATIONS

The table below sets forth for the fiscal years ended April 30, 2016 and 2015, the percentage of consolidated net sales represented by certain items in the Company's consolidated statements of operations:

	<u>2016</u>	<u>2015</u>
Revenues		
FEI-NY	73.3%	80.9%
Gillam-FEI	9.8	10.5
FEI-Zyfer	20.3	12.0
Less intersegment revenues	(3.4)	(3.4)
	<u>100.0</u>	<u>100.0</u>
Cost of Revenues	<u>66.2</u>	<u>69.2</u>
Gross Margin	33.8	30.8
Selling and Administrative expenses	21.8	18.6
Research and Development expenses	9.8	7.4
Operating Profit	2.2	4.8
Other Income (Expenses), net	1.3	1.1
Provision for Income Taxes	(1.8)	(2.2)
Net Income	<u>1.7%</u>	<u>3.7%</u>

Revenues

Fiscal years ended April 30, (in thousands)					
			<u>Change</u>		
	<u>2016</u>	<u>2015</u>	<u>\$</u>	<u>%</u>	
FEI-NY	\$ 44,238	\$ 61,905	\$ (17,667)	(29%)	
Gillam-FEI	5,942	8,026	(2,084)	(26%)	
FEI-Zyfer	12,286	9,215	3,071	33%	
Intersegment sales	(2,072)	(2,582)	510		
	<u>\$ 60,394</u>	<u>\$ 76,564</u>	<u>\$ (16,170)</u>	<u>(21%)</u>	

Fiscal Year 2016 compared to fiscal year 2015:

For the year ended April 30, 2016, revenues from commercial and U.S. Government satellite programs accounted for approximately 55% of consolidated revenues, an approximately 6% decrease from the prior year. Fiscal year 2016 satellite revenues decreased by approximately 30% or \$13.8 million over the prior fiscal year, due to the postponement and rescheduling of certain satellite programs. Revenues on satellite program contracts, which are recorded in the FEI-NY segment, are recognized primarily under the percentage of completion method. Revenues from non-space U.S. Government/DOD customers, which are recorded in both the FEI-NY and FEI-Zyfer segments, accounted for approximately 25% and 20% of consolidated revenues for fiscal years 2016, and 2015, respectively. In actual sales dollars, revenues from this market area increased by approximately \$2.1 million or 16% compared to prior fiscal year, as increased U.S. Government revenues at FEI-Zyfer were offset by lower non-space U.S. Government revenues at FEI-NY. The decrease at FEI-NY was principally attributed to FEI-Elcom which was negatively impacted by orders that were delayed and is expected to book most of those delayed orders in the upcoming year. In both fiscal years 2016 and 2015 network infrastructure and other industrial revenues, which are recorded in all three segments, accounted for approximately 20% of consolidated revenues. In actual sales dollars, fiscal year 2016 decreased by approximately 27%, driven by the decrease in contract manufacturing revenues from third parties in the Company's FEI-Asia subsidiary which is part of the FEI-NY segment, and declining revenues at Gilliam-FEI.

Fiscal year 2015 compared to fiscal year 2014:

For the year ended April 30, 2015, revenues from commercial and U.S. Government satellite programs accounted for more than 60% of consolidated revenues, similar to the prior year. Fiscal year 2015 satellite revenues increased by approximately 8% over the prior fiscal year. Revenues on satellite program contracts, which are recorded in the FEI-NY segment, are recognized primarily under the percentage of completion method. Revenues from non-space U.S. Government/DOD customers, which are recorded in both the FEI-NY and FEI-Zyfer segments, accounted for less than 20% of consolidated revenues for both fiscal years 2015 and 2014. In actual sales dollars, revenues from this market area were approximately the same in both fiscal years 2015 and 2014 as increased U.S. Government revenues at FEI-Zyfer were offset by lower non-space U.S. Government revenues at FEI-NY. For the year ended April 30, 2015, total U.S. Government end-use sales (a combination of revenues from U.S. Government satellite contracts and non-space programs) were approximately 47% of consolidated revenues as compared to 54% of consolidated revenues for the year ended April 30, 2014. The reason for the percentage decrease in U.S. Government sourced revenue is due to increased revenues on commercial satellite programs. Based on the Company's current backlog and prospects for new contract orders, the Company expects to record a higher percentage of revenues from U.S. Government-related programs in fiscal year 2016. In fiscal year 2015, network infrastructure and other industrial revenues, which are recorded in all three segments, accounted for approximately 20% of consolidated revenues which is similar to their share of consolidated revenues in the prior year. In actual sales dollars, fiscal year 2015 commercial revenues increased by approximately 9% as compared to non-space commercial revenues for fiscal year 2014. The primary reason for growth in this industrial, non-space market area is due to increased contract manufacturing revenues from third parties in the Company's FEI-Asia subsidiary which is part of the FEI-NY segment. In prior periods, third party revenues for the FEI-Asia subsidiary were insignificant as most of its manufacturing capacity was applied to intersegment production. Increased revenues in FEI-Asia were partially offset by declining revenues at Gillam-FEI.

Gross Margin

	Fiscal years ended April 30, (in thousands)			
	2016	2015	Change	
			\$	%
GM Rate	\$ 20,436 33.8%	\$ 23,548 30.8%	\$ (3,112)	(13%)

For the year ended April 30, 2016, gross margin decreased as a result of lower revenues, however gross margin rate increased. The increase in gross margin rate was mainly a result of increase in efficiencies due to the completion of the implementation of automated test equipment as mentioned below, reduction in costs and product mix at FEI-NY. The other factor increasing gross margin rate is the increase in revenues at FEI-Zyfer, which had a larger impact in consolidated results. For the year ended April 30, 2015, gross margin and the gross margin rate decreased over the prior fiscal year due to product mix, higher than anticipated contract costs and inventory-related charges. Exceptional engineering costs incurred late in the fiscal year, related to delivery of state-of-the-art satellite systems as well as efforts to increase production capacity in the FEI-NY segment resulted in inefficiencies and higher costs. Higher contract costs were pronounced on one program with an aggregate contract value of approximately \$27 million. This program requires a relatively high quantity of units to be manufactured for which automated processes were implemented during fiscal year 2015. Higher than anticipated touch labor was incurred while those processes and related equipment were being installed, increasing the expected costs on the program's contracts by approximately \$2 million. The net gross margin on these contracts recognized during fiscal year 2015 was a loss of \$800,000. Over the life of the contracts through April 30, 2015, the Company recorded net gross margin of approximately \$2.5 million. In future years, the Company expects to realize improved margins from this investment in capacity improvements and to generate additional satellite business from its enhanced technological capabilities. Inventory write downs at several subsidiaries which aggregated approximately \$800,000 and increased costs of approximately \$450,000 recorded in the Gillam-FEI segment combined to reduce the gross margin rate by 1.6%. The Gillam-FEI costs are for the purpose of modifying certain network infrastructure inventory originally manufactured for the U.S. market to be able to sell the same units in non-U.S. markets.

Selling and Administrative Expenses

Fiscal years ended April 30, (in thousands)				
2016	2015	Change		
		\$	%	
\$ 13,205	\$ 14,207	\$ (1,002)	(7%)	

In the fiscal years ended April 30, 2016 and 2015, selling and administrative costs (“SG&A”) were 22% and 19%, respectively, of consolidated revenues. For fiscal year 2016, incentive compensation expense decreased from the prior year due to reduced operating profits. Selling and administrative expenses include stock compensation expense of \$548,000 and \$668,000, respectively. The Company expects fiscal year 2017 selling and administrative expenses to meet or approach our target of 20% of revenues.

Research and Development Expenses

Fiscal years ended April 30, (in thousands)				
2016	2015	Change		
		\$	%	
\$ 5,929	\$ 5,666	\$ 263	5%	

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. As a percentage of consolidated revenue, R&D spending for the years ended April 30, 2016 and 2015 was approximately 10% and 7%, respectively. During fiscal year 2016, the Company has continued the development of its frequency converter product line in particular (the following letters represent specific frequency bands) Ku to Ku band converters, Ka to Ka band converters and new Ka to L band and L to Ka band converters. Internal R&D spending will also include, additional work on Low noise CRO’s and low aging, and high stability Rb standard for secure communications.

The Company also continued to engage in customer-funded development activity, the cost of which appears 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 2017, the Company anticipates that internal research and development spending will be comparable to the amount expended during fiscal year 2016 but will remain at 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)				
2016	2015	Change		
		\$	%	
\$ 1,302	\$ 3,675	\$ (2,373)	(65%)	

For fiscal year ended April 30, 2016 the combination of SG&A and R&D expenses were down approximately 4% compared to prior fiscal year. Thus, the decrease in operating profit in fiscal year 2016 is mainly due to lower gross margin as discussed above. Both the FEI-NY and FEI-Zyfer segments recorded operating profits, however the FEI-NY segment was down from last year in each of FEI-Elcom, FEI-Asia and FEI-NY itself. This was offset by an over 100% increase in operating profit at the FEI-Zyfer segment.

For the year ended April 30, 2015, the combination of SG&A and R&D expenses were approximately the same as that spent in the prior fiscal year. Thus, the decrease in operating profit in fiscal year 2015 is entirely due to lower gross margin as discussed above. Both the FEI-NY and FEI-Zyfer segments recorded operating profits which were offset by operating losses at the Gillam-FEI segment.

Other Income (Expense)

Fiscal years ended April 30, (in thousands)				
	2016	2015	Change	
			\$	%
Investment income	\$ 492	\$ 1,042	\$ (550)	(53%)
Interest expense	(131)	(139)	8	6%
Other income (expense), net	412	(42)	454	NM
	<u>\$ 773</u>	<u>\$ 861</u>	<u>\$ (88)</u>	<u>(10%)</u>

Investment income is derived primarily from the Company's holdings of marketable securities. Earnings on these securities may vary based on fluctuating dividend payout levels and interest rates and the timing of purchases or sales of securities. During fiscal years 2016 and 2015, investment income included gains upon the sale or redemption of marketable securities of approximately \$131,000 and \$566,000, respectively. During fiscal year 2017, the Company anticipates that investment income will be approximately the same as that earned in fiscal year 2016, depending on the yield and size of its investment portfolio and the timing of any sales or redemptions of marketable securities.

In fiscal year 2016, interest expense was incurred on borrowings under the Company's \$25 million credit facility with a bank and on deferred compensation payments. During fiscal year 2016, interest expense relating to the line of credit was lower as compared to the prior fiscal year, offset by an increase in deferred compensation payments. Interest expense in future years will be dependent on interest rates in the U.S. and the level of the Company's borrowings under the credit facility.

During fiscal year 2016, other income included approximately \$380,000 from the proceeds of a life insurance policy of a former officer of the Corporation. During fiscal year 2015, other income consisted of insignificant non-operating expenses.

Income Tax Provision

Fiscal years ended April 30, (in thousands)				
	2016	2015	Change	
			\$	%
Effective tax rate on pre-tax book income:	\$ 1,070	\$ 1,710	\$ (640)	(37%)
	51.6%	37.7%		

For the year ended April 30, 2016, the provision for taxes was lower than the prior year due to lower pre-tax income. The effective tax rate increased due to increased pre-tax losses incurred at the Company's foreign subsidiaries for which it receives no tax benefit.

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 ("R&D credit") in the U.S. to lower its tax rate. (See Note 12 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 \$6.4 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 \$4.4 million which may be applied in annually limited amounts to offset future U.S.-sourced taxable income over the next 15 years.

LIQUIDITY AND CAPITAL RESOURCES

The Company's balance sheet continues to reflect a highly liquid position with working capital of \$75.6 million at April 30, 2016. Included in working capital at April 30, 2016 is \$17.2 million consisting of cash, cash equivalents and short-term investments. The Company's current ratio at April 30, 2016 is 9.6 to 1 compared to 10.0 to 1 at the end of the prior fiscal year.

Net cash provided by operating activities for the year ended April 30, 2016, was \$2.9 million compared to \$1.9 million for the prior fiscal year. During fiscal years 2016 and 2015, the Company incurred \$3.1 million and \$4.3 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. During fiscal year 2016, operating cash was reduced by increases to inventory offset by a decrease to accounts receivables. For fiscal year 2015, operating cash was reduced by increases to accounts receivable and reductions in accrued expenses and other liabilities. In fiscal year 2017, the Company anticipates that it will maintain positive cash flow from operations by continuing to generate operating profits and managing its inventory levels.

Net cash used in investing activities for the fiscal year ended April 30, 2016 was \$3.5 million compared to cash provided of \$1.2 million in fiscal year 2015. In fiscal year 2016, investing activities included net uses from the redemption, sale or purchase of marketable securities for \$89,000 and acquisitions of capital equipment and other long term assets for \$3.4 million. In fiscal year 2015 investing activities consisted of net proceeds from the redemption, sale or purchase of marketable securities of \$5.3 million and acquisitions of capital equipment and other long term assets for \$4.1 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 has a five-year, \$25 million credit facility from a bank. As of April 30, 2016, the Company has an outstanding balance of \$6.0 million under the credit facility. During fiscal year 2015, as certain marketable securities were sold or redeemed and as the Company generated positive operating cash flow, the Company paid down a portion of the credit facility as indicated in the next paragraph. The Company may draw on this bank credit facility to provide additional working capital and to fund acquisitions. The interest rate on the credit 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 credit facility, see Note 7 to the Consolidated Financial Statements. In addition, the Company's European subsidiaries have available approximately \$275,000 under a bank credit line to meet short-term cash flow requirements. The rate of interest on any borrowings is based on the one-month EURO Interbank Offered Rate (EURIBOR). The European subsidiaries had no borrowings against this line of credit during fiscal year 2016.

During the year ended April 30, 2016, cash provided by financing activities was \$141,000 consisting of the tax benefit arising from the exercise of stock-based awards. There were no additional borrowings or payments made under the bank credit facility. During the year ended April 30, 2015, cash used in financing activities was \$3.9 million. The Company borrowed \$2.3 million under its bank credit facility but also made payments of \$6.4 million against the credit facility. The Company realized \$200,000 from the tax benefit arising from the exercise of stock-based awards during fiscal year 2015. 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 fixed repurchase plan nor commitments to purchase additional shares in the future. As of the end of fiscal year 2016, 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 2017, where possible, the Company will secure partial customer funding for its R&D efforts but is targeting to spend its own funds at a rate of up to 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.

The Company's international business is subject to changes in demand or pricing resulting from fluctuations in currency exchange rates, primarily in the Euro to U.S. Dollar exchange rate and in the Chinese Renminbi to U.S. Dollar exchange rate.

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, 2016, the Company's consolidated backlog amounted to approximately \$32 million as compared to approximately \$37 million at the beginning of the fiscal year. (See Item 1). Approximately 75% of this backlog is expected to be filled during the Company's fiscal year ending April 30, 2017. 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. The Company expects any partially funded contracts to become fully funded over time and will add the additional funding 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.

The Company's liquidity is adequate to meet its operating and investment needs through at least July 29, 2017.

RECENT ACCOUNTING PRONOUNCEMENTS

In March 2016, the Financial Accounting Standards Board ("FASB") amended the existing accounting standards for stock-based compensation, Accounting Standards Update ("ASU") 2016-09, *Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*. The amendments impact several aspects of accounting for share-based payment transactions, including the income tax consequences, forfeitures, classification of awards as either equity or liabilities, and classification on the statement of cash flows. This guidance requires a mix of prospective, modified retrospective, and retrospective transition to all annual and interim periods presented and is effective for the Company beginning in fiscal 2018. The Company has not determined the full impact of implementation of this standard, but does not expect it will have a material effect on the Company's financial condition or results of operations.

In February 2016, the FASB issued ASU No. 2016-02 Leases (Topic 842). The objective of the update is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The amendments of the ASU 2016-02 are effective for fiscal years beginning after December 31, 2018 and early adoption is permitted. The Company is currently evaluating the impact of this standard on our consolidated financial statements.

In November 2015, the FASB issued ASU No. 2015-17 ("ASU 2015-17"), *Income Taxes (Topic 740): Balance Sheet Classification of Deferred Taxes*. The amendments in ASU 2015-17 seek to simplify the presentation of deferred income taxes and require that deferred tax liabilities and assets be classified as noncurrent in a classified statement of financial position. ASU 2015-17 is effective for financial statements issued for annual periods beginning after December 15, 2016, and interim periods within those annual periods, with early application permitted for all entities as of the beginning of an interim or annual reporting period. The Company has not determined the full impact of implementation of this standard, but believes it will not be material to net income. The Company believes that the main impact of adoption of the standard will be the reclassification of current deferred tax assets to an increase in noncurrent deferred tax assets for the period ending April 30, 2018.

In July 2015, the FASB issued ASU 2015-11, *Inventory (Topic 330): Simplifying the Measurement of Inventory* ("ASU 2015-11") which changes the measurement principle for inventory from the lower of cost or market to the lower of cost or net realizable value. ASU 2015-11 defines net realizable value as estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. The new guidance must be applied on a prospective basis and is effective for periods beginning after December 15, 2016, with early adoption permitted. The Company is currently evaluating the effect that the new guidance will have on its consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, *Presentation of Financial Statements – Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity's Ability to Continue as a Going Concern* ("ASU 2014-15"), which is effective for annual periods after December 15, 2016 and for annual periods and interim periods thereafter. Early application is permitted. Under ASU 2014-15, entities will be required to formally assess their ability to continue as a going concern and provide disclosures under certain circumstances. While current practice regarding such disclosures is often guided by U.S. auditing standards, the new standard explicitly requires the assessment at interim and annual periods, and provides management with its own disclosure guidance. The standard can be adopted early. The company is currently assessing the impact that adopting these new assessment and disclosure requirements will have on its financial statements and footnote disclosures.

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In May 2014, the FASB issued ASU No. 2014-09 , *Revenue from Contracts with Customers (Topic 606)* . ASU 2014-09 eliminates most of the existing industry-specific revenue recognition guidance and significantly expands related disclosures. The required disclosures will include both quantitative and qualitative information about the amount, timing and uncertainty of revenue from contracts with customers and the significant judgments used. Entities can retrospectively apply ASU 2014-09 or use an alternative transition method. In July 2015, the FASB approved a one-year deferral of the effective date of this ASU. Although the amending ASU has not yet been issued, since it will be amended, this ASU is effective for public companies for annual reporting periods beginning on or after December 15, 2017 and for the Company, must be adopted for its fiscal year 2019 beginning on May 1, 2018. The Company is in the process of determining the effect that ASU 2014-09 may have on its financial statements .

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 2016, as in fiscal year 2015, the impact of inflation on the Company's business has not been materially significant.

Item 7A. Quantitative and Qualitative Disclosure About Market Risk

This item is not required for smaller reporting companies.

Item 8. Financial Statements and Supplementary Data

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

Board of Directors and Shareholders of
Frequency Electronics, Inc.

We have audited the accompanying consolidated balance sheets of Frequency Electronics, Inc. and Subsidiaries (the "Company") as of April 30, 2016 and 2015, and the related consolidated statements of income, comprehensive income, cash flows and changes in stockholders' equity for each of the years then ended. 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, 2016 and 2015, and the consolidated results of their operations and their cash flows for each of the years then ended, in conformity with accounting principles generally accepted in the United States of America.

/s/ EisnerAmper LLP
EisnerAmper LLP

New York, New York
July 29, 2016

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

Consolidated Balance Sheets
 April 30, 2016 and 2015
 (In thousands, except par value)

	<u>2016</u>	<u>2015</u>
ASSETS:		
Current assets:		
Cash and cash equivalents	\$ 6,082	\$ 7,222
Marketable securities	11,111	11,186
Accounts receivable, net of allowance for doubtful accounts of \$189 in each of 2016 and 2015	9,000	9,689
Costs and estimated earnings in excess of billings, net	12,377	12,929
Inventories, net	41,278	38,239
Deferred and prepaid income taxes	3,213	3,063
Prepaid expenses and other	1,250	1,271
Total current assets	84,311	83,599
Property, plant and equipment, at cost, net of accumulated depreciation and amortization	13,072	12,686
Deferred income taxes	7,702	7,360
Goodwill and other intangible assets	617	617
Cash surrender value of life insurance and cash held in trust	12,819	11,825
Other assets	1,693	1,738
Total assets	\$ 120,214	\$ 117,825
LIABILITIES AND STOCKHOLDERS' EQUITY :		
Current liabilities:		
Accounts payable - trade	\$ 2,650	\$ 1,720
Accrued liabilities	6,108	6,630
Total current liabilities	8,758	8,350
Long-term debt - noncurrent	6,000	6,000
Deferred compensation	11,773	11,318
Deferred rent and other liabilities	331	347
Total liabilities	26,862	26,015
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 8,753 outstanding in 2016; 8,699 outstanding in 2015	9,164	9,164
Additional paid-in capital	55,576	54,360
Retained earnings	28,533	27,528
	93,273	91,052
Common stock reacquired and held in treasury - at cost (411 shares in 2016 and 465 shares in 2015)	(1,885)	(2,132)
Accumulated other comprehensive income	1,964	2,890
Total stockholders' equity	93,352	91,810
Total liabilities and stockholders' equity	\$ 120,214	\$ 117,825

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, 2016 and 2015

Consolidated Statements of Income

	<u>2016</u>	<u>2015</u>
	(In thousands, except per share data)	
Revenues	\$ 60,394	\$ 76,564
Cost of revenues	39,958	53,016
Gross margin	20,436	23,548
Selling and administrative expenses	13,205	14,207
Research and development expenses	5,929	5,666
Operating profit	1,302	3,675
Other income (expense):		
Investment income	492	1,042
Interest expense	(131)	(139)
Other income (expense), net	412	(42)
Income before provision for income taxes	2,075	4,536
Provision for income taxes	1,070	1,710
Net income	<u>\$ 1,005</u>	<u>\$ 2,826</u>
Net income per common share:		
Basic	<u>\$ 0.12</u>	<u>\$ 0.33</u>
Diluted	<u>\$ 0.11</u>	<u>\$ 0.32</u>
Average shares outstanding:		
Basic	<u>8,728</u>	<u>8,611</u>
Diluted	<u>8,937</u>	<u>8,910</u>

Consolidated Statements of Comprehensive Income

Net income	\$ 1,005	\$ 2,826
Other comprehensive income (loss):		
Foreign currency translation adjustment	(753)	(1,093)
Unrealized gain (loss) on marketable securities:		
Change in market value of marketable securities before reclassification, net of tax of \$51 and (\$176), respectively	(99)	343
Reclassification adjustment for realized gains included in net income, net of tax of \$57 and \$192, respectively	(74)	(374)
Total unrealized loss on marketable securities, net of tax	(173)	(31)
Total other comprehensive (loss)	(926)	(1,124)
Comprehensive income	<u>\$ 79</u>	<u>\$ 1,702</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, 2016 and 2015

	<u>2016</u>	<u>2015</u>
	(In thousands)	
Cash flows from operating activities:		
Net income	\$ 1,005	\$ 2,826
Adjustments to reconcile net income to net cash provided in operating activities:		
Deferred income tax benefit	(1,265)	(720)
Depreciation and amortization	2,712	2,944
Deferred lease obligation	(75)	(81)
Provision for losses on accounts receivable, inventories and warranty reserve	148	222
Gains on marketable securities	(131)	(566)
Loss (gain) on sale of fixed and other assets, net	(370)	64
Employee benefit plans expense	1,450	1,516
Stock-based compensation expense	824	1,077
Tax benefit from exercise of stock-based compensation	(141)	(200)
Changes in operating assets and liabilities:		
Accounts receivable	(1,723)	(3,206)
Costs and estimated earnings in excess of billings	3,340	(2,490)
Inventories	(3,306)	1,267
Prepaid expenses and other	(34)	42
Other assets	(570)	(529)
Accounts payable - trade	1,179	25
Accrued liabilities	(608)	(339)
Income taxes refundable/payable	1,013	594
Other liabilities	(525)	(564)
Net cash provided by operating activities	<u>2,923</u>	<u>1,882</u>
Cash flows from investing activities:		
Purchase of marketable securities	(1,356)	(1,956)
Proceeds from sale or redemption of marketable securities	1,267	7,271
Capital expenditures	(3,437)	(4,157)
Net cash (used in) provided by investing activities	<u>(3,526)</u>	<u>1,158</u>

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

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

Consolidated Statements of Cash Flows

Years ended April 30, 2016 and 2015

(Continued)

	<u>2016</u>	<u>2015</u>
	(In thousands)	
Cash flows from financing activities:		
Proceeds from credit line borrowing	\$ -	\$ 2,300
Payment of short-term credit and lease obligations	-	(6,400)
Tax benefit from exercise of stock-based compensation	141	200
Net cash provided (used in) by financing activities	<u>141</u>	<u>(3,900)</u>
Net (decrease) in cash and cash equivalents before effect of exchange rate changes	(462)	(860)
Effect of exchange rate changes on cash and cash equivalents	<u>(678)</u>	<u>384</u>
Net (decrease) in cash and cash equivalents	(1,140)	(476)
Cash and cash equivalents at beginning of year	<u>7,222</u>	<u>7,698</u>
Cash and cash equivalents at end of year	<u>\$ 6,082</u>	<u>\$ 7,222</u>
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest	<u>\$ 128</u>	<u>\$ 140</u>
Income taxes	<u>\$ 1,311</u>	<u>\$ 1,851</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, 2016 and 2015

(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		
Balance at April 30, 2014	9,163,940	\$ 9,164	\$ 53,181	\$ 24,702	593,131	\$ (2,715)	\$ 4,014	\$ 88,346
Contribution of stock to 401(k) plan			302		(40,324)	183		485
Stock-based compensation expense			1,072		(1,400)	5		1,077
Tax benefit from stock option exercise			200					200
Exercise of stock options and stock appreciation rights - net of shares tendered for exercise price			(395)		(86,244)	395		-
Change in unrealized gains and losses on marketable securities, net of taxes							(31)	(31)
Foreign currency translation adjustment							(1,093)	(1,093)
Net Income				2,826				2,826
Balance at April 30, 2015	9,163,940	9,164	54,360	27,528	465,163	(2,132)	2,890	91,810
Contribution of stock to 401(k) plan			283		(46,743)	215		498
Stock-based compensation expense			818		(1,300)	6		824
Tax benefit from stock option exercise			141					141
Exercise of stock options and stock appreciation rights - net of shares tendered for exercise price			(26)		(5,736)	26		-
Change in unrealized gains and losses on marketable securities, net of taxes							(173)	(173)
Foreign currency translation adjustment							(753)	(753)
Net Income				1,005				1,005
Balance at April 30, 2016	<u>9,163,940</u>	<u>\$ 9,164</u>	<u>\$ 55,576</u>	<u>\$ 28,533</u>	<u>411,384</u>	<u>\$ (1,885)</u>	<u>\$ 1,964</u>	<u>\$ 93,352</u>

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

FREQUENCY ELECTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

April 30, 2016 and 2015

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 13 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 at times be in excess of the FDIC and SIPC insurance limits. 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; three institutions at April 30, 2016 and 2015. 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.

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

April 30, 2016 and 2015

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.

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 was 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 the full amount of 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.

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

April 30, 2016 and 2015

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.

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 income taxes, 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 and stock appreciation rights.

Fair Values of Financial Instruments:

Cash and cash equivalents, short-term credit obligations, long term debt and cash surrender value 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.

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

April 30, 2016 and 2015

The weighted average fair value of each option or stock appreciation right (“SAR”) 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:

	Years ended April 30	
	2016	2015
Expected volatility	35%	35%
Dividend yield	0.0%	0.0%
Risk-free interest rate	1.35% and 1.50%	1.50% and 2.38%
Expected lives	5.0 years	5.0 and 8.5 years

The expected life assumption was determined based on the Company’s historical experience as well as the term of recent SAR agreements. 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. 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 or SARs.

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 March 2016, the Financial Accounting Standards Board (“FASB”) amended the existing accounting standards for stock-based compensation, Accounting Standards Update (“ASU”) 2016-09, *Compensation-Stock Compensation (Topic 718): Improvements to Employee Share-Based Payment Accounting*. The amendments impact several aspects of accounting for share-based payment transactions, including the income tax consequences, forfeitures, classification of awards as either equity or liabilities, and classification on the statement of cash flows. This guidance requires a mix of prospective, modified retrospective, and retrospective transition to all annual and interim periods presented and is effective for the Company beginning in fiscal 2018. The Company has not determined the full impact of implementation of this standard, but does not expect it will have a material effect on the Company’s financial condition or results of operations.

In February 2016, the FASB issued ASU No. 2016-02 Leases (Topic 842). The objective of the update is to increase transparency and comparability among organizations by recognizing lease assets and lease liabilities on the balance sheet and disclosing key information about leasing arrangements. The amendments of the ASU 2016-02 are effective for fiscal years beginning after December 31, 2018 and early adoption is permitted. The Company is currently evaluating the impact of this standard on our consolidated financial statements.

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

April 30, 2016 and 2015

In July 2015, the FASB issued ASU 2015-11, *Inventory (Topic 330): Simplifying the Measurement of Inventory* (“ASU 2015-11”) which changes the measurement principle for inventory from the lower of cost or market to the lower of cost or net realizable value. ASU 2015-11 defines net realizable value as estimated selling prices in the ordinary course of business, less reasonably predictable costs of completion, disposal and transportation. The new guidance must be applied on a prospective basis and is effective for periods beginning after December 15, 2016, with early adoption permitted. The Company is currently evaluating the effect that the new guidance will have on its consolidated financial statements.

In August 2014, the FASB issued ASU No. 2014-15, *Presentation of Financial Statements – Going Concern (Subtopic 205-40): Disclosure of Uncertainties about an Entity’s Ability to Continue as a Going Concern* (“ASU 2014-15”), which is effective for annual periods after December 15, 2016 and for annual periods and interim periods thereafter. Early application is permitted. Under ASU 2014-15, entities will be required to formally assess their ability to continue as a going concern and provide disclosures under certain circumstances. While current practice regarding such disclosures is often guided by U.S. auditing standards, the new standard explicitly requires the assessment at interim and annual periods, and provides management with its own disclosure guidance. The standard can be adopted early. The company is currently assessing the impact that adopting these new assessment and disclosure requirements will have on its financial statements and footnote disclosures.

In May 2014, the FASB issued ASU No. 2014-09, *Revenue from Contracts with Customers (Topic 606)*. ASU 2014-09 eliminates most of the existing industry-specific revenue recognition guidance and significantly expands related disclosures. The required disclosures will include both quantitative and qualitative information about the amount, timing and uncertainty of revenue from contracts with customers and the significant judgments used. Entities can retrospectively apply ASU 2014-09 or use an alternative transition method. In July 2015, the FASB approved a one-year deferral of the effective date of this ASU. Although the amending ASU has not yet been issued, since it will be amended, this ASU is effective for public companies for annual reporting periods beginning on or after December 15, 2017 and for the Company, must be adopted for its fiscal year 2019 beginning on May 1, 2018. The Company is in the process of determining the effect that ASU 2014-09 may have on its financial statements.

2. Earnings Per Share

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

	Years ended April 30,	
	2016	2015
Basic EPS Shares outstanding (weighted average)	8,727,874	8,610,950
Effect of Dilutive Securities	209,035	298,808
Diluted EPS Shares outstanding	8,936,909	8,909,758

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, 2016 and 2015, the number of excluded options and SARS were 388,625 and 271,500, respectively.

3. Costs and Estimated Earnings in Excess of Billings

At April 30, 2016 and 2015, costs and estimated earnings in excess of billings, net, consist of the following:

	2016	2015
	(in thousands)	
Costs and estimated earnings in excess of billings	\$ 12,460	\$ 14,057
Billings in excess of costs and estimated earnings	(83)	(1,128)
Net asset	\$ 12,377	\$ 12,929

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

April 30, 2016 and 2015

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 these long-term contracts is accounted for on the percentage of completion basis. During the years ended April 30, 2016 and 2015, revenue recognized under percentage of completion contracts was approximately \$32.5 million and \$46.8 million, respectively. If contract losses are anticipated, costs and estimated earnings in excess of billings are reduced for the full amount of such losses when they are determinable. Total anticipated contract losses at April 30, 2016 and 2015 were approximately \$450,000 and \$400,000, respectively.

4. Inventories

Inventories at April 30, 2016 and 2015, respectively, consisted of the following (in thousands):

	<u>2016</u>	<u>2015</u>
Raw Materials and Component Parts	\$ 25,110	\$ 24,274
Work in Progress	12,042	9,948
Finished Goods	4,126	4,017
	<u>\$ 41,278</u>	<u>\$ 38,239</u>

As of April 30, 2016 and 2015, approximately \$35.3 million and \$32.0 million, respectively, of total inventory is located in the United States, approximately \$5.0 million and \$5.4 million, respectively, is located in Belgium and approximately \$1.0 million and \$0.8 million, respectively, is located in China. The company buys inventory in bulk quantities which may be used over significant time periods; due to its nature the inventory does not deteriorate.

5. Property, Plant and Equipment and Leases

Property, plant and equipment at April 30, 2016 and 2015, consists of the following (in thousands):

	<u>2016</u>	<u>2015</u>
Buildings and building improvements	\$ 5,509	\$ 5,224
Machinery, equipment and furniture	55,874	52,987
	61,383	58,211
Less, accumulated depreciation	48,311	45,525
	<u>\$ 13,072</u>	<u>\$ 12,686</u>

Depreciation and amortization expense for the years ended April 30, 2016 and 2015 was \$2,660,000 and \$2,828,000, respectively.

Maintenance and repairs charged to operations for the years ended April 30, 2016 and 2015 was approximately \$611,000 and \$1,017,000, respectively.

The Company leases its Long Island, New York headquarters building at an annual rent of \$800,000 following the Company's exercise of its option to renew the lease for a second 5-year period. The lease will end in January 2019. 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 \$40,000 through the end of the lease which expires in March 2018. The lease for the FEI-Asia facility is for a one-year term with monthly rent of \$5,000 through February 2017. FEI-Zyfer leases office and manufacturing space encompassing 27,850 square feet. Monthly rental payments are currently \$31,200 for the remaining 16 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 \$1,000 per month.

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

April 30, 2016 and 2015

Rent expense under operating leases was approximately \$1.5 million for both fiscal years ended April 30, 2016 and 2015. The Company records rent expense on its New York building and FEI-Zyfer facility on the straight-line method over the lives of the respective leases. As a result, as of April 30, 2016 and 2015, the Company's balance sheet includes deferred rent payable of approximately \$214,000 and \$290,000, respectively, which will be recognized over the respective rental periods.

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

Years ending April 30,	Operating Leases
2017	\$ 1,713
2018	1,363
2019	600
Total future minimum lease payments	<u>\$ 3,676</u>

6. Marketable Securities

The cost, gross unrealized gains, gross unrealized losses and fair market value of available-for-sale securities at April 30, 2016 and 2015 are as follows (in thousands):

	April 30, 2016			
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Market Value
Fixed income securities	\$ 3,407	\$ 121	\$ (6)	\$ 3,522
Equity securities	7,197	974	(582)	7,589
	<u>\$ 10,604</u>	<u>\$ 1,095</u>	<u>\$ (588)</u>	<u>\$ 11,111</u>

	April 30, 2015			
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Market Value
Fixed income securities	\$ 3,379	\$ 104	\$ (16)	\$ 3,467
Equity securities	7,018	834	(133)	7,719
	<u>\$ 10,397</u>	<u>\$ 938</u>	<u>\$ (149)</u>	<u>\$ 11,186</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:

	Less than 12 months		12 Months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
April 30, 2016						
Fixed Income Securities	\$ -	\$ -	\$ 467	\$ (6)	\$ 467	\$ (6)
Equity Securities	574	(18)	2,232	(564)	2,806	(582)
	<u>\$ 574</u>	<u>\$ (18)</u>	<u>\$ 2,699</u>	<u>\$ (570)</u>	<u>\$ 3,273</u>	<u>\$ (588)</u>
April 30, 2015						
Fixed Income Securities	\$ 96	\$ (1)	\$ 461	\$ (15)	\$ 557	\$ (16)
Equity Securities	3,323	(133)	-	-	3,323	(133)
	<u>\$ 3,419</u>	<u>\$ (134)</u>	<u>\$ 461</u>	<u>\$ (15)</u>	<u>\$ 3,880</u>	<u>\$ (149)</u>

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

April 30, 2016 and 2015

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, 2016 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.

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,	
	2016	2015
Proceeds	\$ 1,267	\$ 7,271
Gross realized gains	\$ 147	\$ 571
Gross realized losses	\$ (16)	\$ (5)

Maturities of fixed income securities classified as available-for-sale at April 30, 2016 are as follows (at cost, in thousands):

Current	\$ 1,101
Due after one year through five years	516
Due after five years through ten years	1,790
	<u>\$ 3,407</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.

7. Debt Obligations

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. Proceeds from the Facility will be used for working capital and to finance acquisitions. During the year ended April 30, 2015, the Company borrowed an additional \$2.3 million under the Facility primarily to finance the acquisition of additional manufacturing equipment and repaid an aggregate of \$6.4 million from its operating cash flow and as a result of redemptions of certain fixed income marketable securities.

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

April 30, 2016 and 2015

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). Current outstanding borrowings under the Facility are all under Tranche A. 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 Tranche B borrowings. At April 30, 2016 and 2015, the rate was 1.1913% and 0.9305%, respectively, based on the one-month LIBOR rate. 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, if there are any borrowings under Tranche B, an interest charge coverage ratio. The calculation of both ratios is defined in the Credit Agreement. For the year ended April 30, 2016, the Company met the required covenants for its borrowings under Tranche A.

The Company's European subsidiaries have available 250,000 Euros (approximately \$275,000 based on current rates of exchange between the dollar and the Euro) in a bank credit line to meet short-term cash flow requirements. As of April 30, 2016 and 2015, no amounts were outstanding under such line of credit. Borrowings under the bank credit line, if any, must be repaid within one year of receipt of funds. Interest on this credit line is at 1.0% over the EURO Interbank Offered rate (EURIBOR). At April 30, 2016 and 2015, the rate was 0.692% and 1.12% respectively, based on the one-month EURIBOR.

8. Accrued Liabilities

Accrued liabilities at April 30, 2016 and 2015 consist of the following (in thousands):

	<u>2016</u>	<u>2015</u>
Vacation and other compensation	\$ 1,683	\$ 1,633
Incentive compensation	677	1,302
Payroll taxes	1,254	1,012
Deferred revenue	640	720
Warranty reserve	617	617
Cost conversion	450	450
Commissions	252	407
Other	535	489
	<u>\$ 6,108</u>	<u>\$ 6,630</u>

FREQUENCY ELECTRONICS, INC. AND SUBSIDIARIES
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April 30, 2016 and 2015

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 other assets in the accompanying balance sheets. During the fiscal years ended April 30, 2016 and 2015, the Company acquired product from Morion in the aggregate amount of approximately \$140,000 and \$201,000, respectively, and the Company sold product to Morion in the aggregate amount of approximately \$845,000 and \$615,000, respectively. At April 30, 2016, accounts receivable included \$33,000 due from Morion and \$37,000 was payable to Morion.

On October 22, 2012, the Company entered into an agreement to license its rubidium oscillator production technology to Morion. The agreement required the Company to sell certain fully-depreciated production equipment previously 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. During the fiscal year ended April 30, 2016, sales to Morion included \$375,000 for product and training services under this agreement. Per the amended agreement, the balance of \$1 million for the transfer of the license will be due once the United States Department of State ("State Department") approves the removal of certain provisions of the original agreement. The State Department has approved the technology transfer called for under the agreement.

On March 29, 2016, the Company renegotiated the \$1 million dollar amendment under the original agreement dated October 22, 2012 to \$602,000 due to the U.S. Government easing of export regulations. Of this amount \$392,500 was billed and paid during FY 2016 and the balance of \$210,000 will be billed during FY 2017.

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 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, 2016 and 2015. The other intangible assets were amortized over a three-year period from the date of acquisition. Amortization expense for the year ended April 30, 2015 was approximately \$73,000. As of April 30, 2015 these intangible assets were fully amortized.

11. 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, 2016 and 2015, the Company contributed 46,743 and 40,324 shares of common stock, respectively. The approximate value of these shares at the date of contribution was \$498,000 in fiscal year 2016 and \$485,000 in fiscal year 2015. 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 2016 and 2015, such transactions increased additional paid in capital by \$283,000 and \$302,000, respectively. As of April 30, 2016, all shares of the Company's common stock held by the two plans were combined for an aggregate holding of 790,136 shares, which are allocated to the accounts of the individual participants.

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

April 30, 2016 and 2015

On May 6, 2015, the ESOP Plan (see below) was merged into the Company's profit sharing plan. As of April 30, 2015, the profit sharing plan held an aggregate of 467,975 shares of the Company's common stock allocated to the accounts of the individual participants.

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. Under these plans, the Company charged approximately \$0.7 million and \$1.3 million to selling and administrative expenses for the fiscal years ended April 30, 2016 and 2015, 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 generally expire ten years after the date of grant (the most recent SAR award expires in five years) and are subject to certain restrictions on transferability of the shares obtained on exercise. Under the Company's 2005 Stock Award Plan ("Plan") the Company provided 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. Under the Plan, instruments granted under other plans which expire, are canceled, or are tendered in the exercise of such instruments, increase the shares available under the Plan.

As of April 30, 2013, a consultant, who is the son of the Company's president, had been granted options to purchase 37,500 shares of Company stock under NQSO plans at a weighted average exercise price of \$6.67. During the year ended April 30, 2015, the consultant elected cashless exercises of 20,000 shares at an exercise price of \$6.67, resulting in a net issuance of 8,638 shares. As of April 30, 2015, the consultant has no outstanding stock options. At the beginning of fiscal year 2015, eligible employees had been granted options to purchase approximately 172,500 shares of which 95,000 options with a weighted average exercise price of \$13.15 were outstanding and exercisable. During the year ended April 30, 2015, 57,000 options expired and were returned to the Plan. The remaining 38,000 shares were exercised by the employees using the cashless method resulting in the net issuance of 6,931 shares of Company stock. Total fiscal year 2015 cashless exercises of stock options under ISO and NQSO plans, including the consultant shares above, aggregated 58,000 shares. Accordingly, the Company issued 15,569 shares on exercise and returned 42,431 shares to the pool of available shares which may be used for future grants under the Plan.

As of April 30, 2016, eligible employees and directors have been granted SARS based on approximately 2,021,000 shares of Company stock, of which approximately 1,653,000 shares are outstanding and approximately 1,314,000 shares with a weighted average exercise price of \$8.45 are exercisable. As of April 30, 2015, eligible employees and directors had been granted SARS based on approximately 1,950,000 shares of Company stock, of which approximately 1,603,000 shares were outstanding and approximately 1,131,000 shares with a weighted average exercise price of \$8.27 were 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 Plan. During the year ended April 30, 2016, employees exercised SARS representing 19,500 shares of Company stock and received 5,736 shares of Company stock. The 13,764 share difference was returned to the pool of available shares and may be used for future grants. During the year ended April 30, 2015, employees exercised SARS representing 147,500 shares of Company stock and received 70,675 shares of Company stock. The 76,825 share difference was returned to the pool of available shares and may be used for future grants.

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

April 30, 2016 and 2015

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 and stock appreciation rights activity for the years ended April 30:

	Stock Options and Stock Appreciation Rights			
	Shares	Weighted- Average Exercise Price	Weighted Average Remaining Contractual Term	Aggregate Intrinsic Value
Outstanding – April 30, 2014	1,722,625	\$ 8.60	6.0 years	
Granted	145,000	13.02		
Exercised	(205,500)	7.72		\$ (1,133,640)
Expired or Canceled	(59,000)	14.32		
Outstanding – April 30, 2015	1,603,125	\$ 8.90	5.8 years	
Granted	72,000	12.30		
Exercised	(19,500)	9.15		\$ (19,110)
Expired or Canceled	(3,000)	10.39		
Outstanding – April 30, 2016	1,652,625	\$ 9.05	5.1 years	\$ 2,704,918
Exercisable	1,313,625	\$ 8.45	4.3 years	\$ 2,629,590
Available for future grants	16,336			

As of April 30, 2016, total unrecognized compensation cost related to nonvested options and stock appreciation rights under the plans was approximately \$1,094,000. These costs are expected to be recognized over a weighted average period of 2.3 years.

During the years ended April 30, 2016 and 2015, 151,500 and 244,625 shares, respectively, vested, the fair value of which was approximately \$661,000 and \$1,053,000, respectively. The weighted average grant date fair value of stock appreciation rights granted during the years ended April 30, 2016 and 2015, were approximately \$4.06 and \$4.45, 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 \$265,000 and \$394,000 for the years ended April 30, 2016 and 2015, respectively. Selling and administrative expenses include stock-based compensation expense of approximately \$559,000 and \$683,000 for the years ended April 30, 2016 and 2015, 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, 2016 and 2015, the Company realized \$141,000 and \$200,000 respectively, of tax benefits from the exercise of stock options and SARS.

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

April 30, 2016 and 2015

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 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 year ended April 30, 2015 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 of an option for 30,000 shares at an exercise price of \$14.76 expired during fiscal year 2015.

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, 2016 and 2015, 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 385,626 shares remain in the ESOP. On May 6, 2015, the ESOP plan was merged into the Company's profit sharing plan.

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, 2016 and 2015 was approximately \$959,000 and \$1,038,000, respectively.

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

April 30, 2016 and 2015

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.

12. Income Taxes

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

	Year Ended April 30,	
	2016	2015
U.S.	\$ 4,011	\$ 6,201
Foreign	(1,936)	(1,665)
	<u>\$ 2,075</u>	<u>\$ 4,536</u>

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

	2016	2015
Current:		
Federal	\$ 1,060	\$ 2,170
Foreign	-	-
State	250	260
Current provision	<u>1,310</u>	<u>2,430</u>
Deferred:		
Federal	(150)	(560)
Foreign	-	-
State	(90)	(160)
Deferred benefit	<u>(240)</u>	<u>(720)</u>
Total provision	<u>\$ 1,070</u>	<u>\$ 1,710</u>

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

	2016	2015
Statutory Rate	\$ 705	\$ 1,542
State and local tax	85	(126)
Valuation allowance on deferred tax assets	833	760
Effect of foreign operations	41	73
Nondeductible expenses	166	112
Domestic production activities deduction	(159)	(190)
Nontaxable life insurance cash value increase	(282)	(119)
Tax credits	(417)	(191)
Other items	98	(151)
	<u>\$ 1,070</u>	<u>\$ 1,710</u>

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

April 30, 2016 and 2015

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

	<u>2016</u>	<u>2015</u>
Deferred tax assets:		
Employee benefits	\$ 8,310	\$ 7,400
Inventory	1,860	1,580
Accounts receivable	490	570
Tax credits	1,260	860
Other assets	220	270
Net operating loss carryforwards	3,600	3,230
Total deferred tax asset	<u>15,740</u>	<u>13,910</u>
Deferred tax liabilities:		
Marketable securities	200	270
Property, plant and equipment	750	890
Other liabilities	70	-
Deferred State Income Tax	600	-
Net deferred tax asset	<u>14,120</u>	<u>12,750</u>
Valuation allowance	(3,280)	(2,390)
Net deferred tax assets	<u>\$ 10,840</u>	<u>\$ 10,360</u>

The components of the deferred tax asset, by balance sheet account, were as follows (in thousands):

	<u>2016</u>	<u>2015</u>
Deferred and prepaid income taxes	\$ 3,138	\$ 3,000
Deferred income taxes	7,702	7,360
Net deferred tax asset	<u>\$ 10,840</u>	<u>\$ 10,360</u>

A valuation allowance is provided when it is more likely than not that some portion, or all, of the deferred tax assets will not be realized. We consider the level of historical income, scheduled reversal of temporary differences, tax planning strategies and projected future taxable income in determining whether a valuation allowance is warranted. The valuation allowance of \$3.3 million as of April 30, 2016, is intended to provide for uncertainty regarding the ultimate realization of U.S. state investment tax credit carryovers and foreign net operating loss and tax credit carryovers. Based on these considerations, we believe it is more likely than not that we will realize the benefit of the net deferred tax asset of \$10.8 million as of April 30, 2016, which is net of the valuation allowance.

The consolidated valuation allowance increased by approximately \$890,000 during the year ended April 30, 2016. The change consists of an \$830,000 deferred tax provision plus a foreign exchange adjustment and reclass of deferred state taxes of \$60,000. For the year ended April 30, 2015, the change in valuation allowance was an increase of \$270,000 which consists of the \$760,000 deferred tax provision less a foreign exchange adjustment of \$490,000.

At April 30, 2016, the Company has available approximately \$6.4 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 \$4.4 million which may be applied in annually limited amounts to offset future U.S.-sourced taxable income over the next 15 years. As of April 30, 2016, the Company has state investment tax credits and foreign research and development credits of \$838,000 and \$425,000, respectively. The state investment tax credit expires beginning in 2023 through 2031.

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

April 30, 2016 and 2015

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. As such, the amount of unrecognized tax benefits at April 30, 2016 and April 30, 2015 were \$0. As of April 30, 2016 and April 30, 2015 the Company had \$0, accrued for the payment of interest and penalties. It is difficult to predict or estimate the change in the Company's unrecognized tax benefits over the next twelve months as a result of the progression of ongoing tax audits or other events. The Company believes, however, that there should be no change during the next twelve months.

The Company is subject to taxation in the U.S. and various state, local and foreign jurisdictions. Net operating losses generated by domestic and foreign entities in closed years and utilized in open years are subject to adjustment by the tax authorities.

13. 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 USSG, 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 historically minimal sales to outside customers. Beginning in late fiscal year 2014, FEI-Asia began shipping higher volumes of product to third parties as a contract manufacturer. 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.

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

April 30, 2016 and 2015

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>2016</u>	<u>2015</u>
Net revenues:		
FEI-NY	\$ 44,238	\$ 61,905
Gillam-FEI	5,942**	8,026**
FEI-Zyfer	12,286	9,215
Less intersegment revenues	(2,072)**	(2,582)**
Consolidated revenues	<u>\$ 60,394</u>	<u>\$ 76,564</u>
Operating profit (loss):		
FEI-NY	\$ 1,228	\$ 4,809
Gillam-FEI	(1,451)**	(1,706)**
FEI-Zyfer	1,996	961
Corporate	(471)	(389)
Consolidated operating profit	<u>\$ 1,302</u>	<u>\$ 3,675</u>

**For fiscal years ended April 30, 2016 and 2015, includes Gillam-FEI intersegment sales of \$847,000 and \$1.5 million, respectively, to the FEI-NY and FEI-Zyfer segments. Such sales consist principally of design and development of automatic test equipment for satellite hardware production and manufacture of assemblies and units of a wireline synchronization product for ultimate production and sale in the U.S. In the Gillam-FEI segment, these transactions reduced the operating loss in each of the fiscal years.

	<u>2016</u>	<u>2015</u>
Identifiable assets:		
FEI-NY (approximately \$2.5 and \$3 million in China)	\$ 62,992	\$ 63,541
Gillam-FEI (all in Belgium or France)	9,610	9,878
FEI-Zyfer	13,275	11,088
less intersegment receivables	(7,651)	(8,775)
Corporate	41,988	42,093
Consolidated identifiable assets	<u>\$ 120,214</u>	<u>\$ 117,825</u>
Depreciation and amortization (allocated):		
FEI-NY	\$ 2,338	\$ 2,562
Gillam-FEI	199	208
FEI-Zyfer	160	159
Corporate	15	15
Consolidated depreciation and amortization expense	<u>\$ 2,712</u>	<u>\$ 2,944</u>

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

April 30, 2016 and 2015

Major Customers

The Company's products are sold to both commercial and governmental customers. For the years ended April 30, 2016 and 2015, approximately 60% and 47% 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 2016, sales to four customers of the FEI-NY segment aggregated \$30.7 million or 69% of that segment's total sales. Two of these customers also exceeded 10% of the Company's consolidated revenues. During the year ended April 30, 2016, in the Gillam-FEI segment, sales to one 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 2015, sales to three customers of the FEI-NY segment aggregated \$33.1 million or 53% 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, 2015, in the Gillam-FEI segment, sales to one 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.

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)	
	2016	2015
Belgium	\$ 3,559	\$ 3,971
France	2,202	10,937
China	1,927	4,493
Israel	1,139	836
Russia	853	638
Germany	342	1,076
Other	1,507	1,610
	\$ 11,529	\$ 23,561

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):

	Year Ended April 30,	
	2016	2015
Balance at beginning of year	\$ 617	\$ 617
Warranty costs incurred	(322)	(296)
Product warranty accrual	322	296
Balance at end of year	\$ 617	\$ 617

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

April 30, 2016 and 2015

15. Other Comprehensive Income (Loss)

Changes in Accumulated Other Comprehensive Income (“AOCI”) by component and reclassifications out of AOCI are as follows (in thousands):

	Change in Market Value of Marketable Securities	Foreign Currency Translation Adjustment	Total
Balance April 30, 2014, net of taxes	\$ 1,016	\$ 2,998	\$ 4,014
Items of other comprehensive income (loss) before reclassification, pretax	519	(1,093)	(574)
Tax effect	(176)	-	(176)
Items of other comprehensive income (loss) before reclassification, net of taxes	343	(1,093)	(750)
Reclassification adjustments, pretax **	(566)		
Tax effect	192	-	(374)
Total other comprehensive income (loss), net of taxes	(31)	(1,093)	(1,124)
Balance April 30, 2015, net of taxes	985	1,905	2,890
Items of other comprehensive income (loss) before reclassification, pretax	(150)	(753)	(903)
Tax effect	51	-	51
Items of other comprehensive income (loss) before reclassification, net of taxes	(99)	(753)	(852)
Reclassification adjustments, pretax **	(131)		
Tax effect	57	-	(74)
Total other comprehensive income (loss), net of taxes	(173)	(753)	(926)
Balance April 30, 2016, net of taxes	\$ 812	\$ 1,152	\$ 1,964

**The reclassification adjustments represent net realized gains on the sale or redemption of available-for-sale marketable securities that were reclassified from AOCI to Other income (expense), net.

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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, 2016, 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, 2016. In making this assessment, management used the criteria established in Internal Control — Integrated Framework (2013) issued by the Committee of Sponsoring Organizations of the Treadway Commission. Based on this evaluation, management has concluded that the Company's internal control over financial reporting were effective as of April 30, 2016.

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

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.

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 year ended April 30, 2016 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 no later than 120 days after April 30, 2016, for the annual meeting of stockholders to be held on or about November 1, 2016. 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 no later than 120 days after April 30, 2016, for the annual meeting of stockholders to be held on or about November 1, 2016.

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 no later than 120 days after April 30, 2016, for the annual meeting of stockholders to be held on or about November 1, 2016.

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 no later than 120 days after April 30, 2016, for the annual meeting of stockholders to be held on or about November 1, 2016.

Item 14. Principal Accountant Fees and Services

This item is incorporated herein by reference from the Company's definitive proxy statement to be filed no later than 120 days after April 30, 2016, for the annual meeting of stockholders to be held on or about November 1, 2016.

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	21
Consolidated Balance Sheets - April 30, 2016 and 2015	22
Consolidated Statements of Income and Comprehensive Income - years ended April 30, 2016 and 2015	23
Consolidated Statements of Cash Flows - years ended April 30, 2016 and 2015	24-25
Consolidated Statements of Changes in Stockholders' Equity - years ended April 30, 2016 and 2015	26
Notes to Consolidated Financial Statements	27-45

(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, 2016 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 50 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/ Steven L. Bernstein

Steven L. Bernstein
Chief Financial Officer

Dated: July 29, 2016

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/ Joel Girsky</u> Joel Girsky	Chairman of the Board	7/29/16
<u>/s/ Joseph P. Franklin</u> Joseph P. Franklin	Director	7/29/16
<u>/s/ S. Robert Foley</u> S. Robert Foley	Director	7/29/16
<u>/s/ Richard Schwartz</u> Richard Schwartz	Director	7/29/16
<u>/s/ Martin B. Bloch</u> Martin B. Bloch	President and CEO (Principal Executive Officer)	7/29/16
<u>/s/ Steven L. Bernstein</u> Steven L. Bernstein	Chief Financial Officer	7/29/16

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 2016 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, 2016 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

Subsidiary & Name under which business is performed	Jurisdiction of Incorporation
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, 2016 on our audits of the consolidated financial statements as of April 30, 2016 and 2015 and for each of the years then ended which report is included in this Annual Report on Form 10-K to be filed on or about July 29, 2016.

/s/ EisnerAmper LLP
EisnerAmper LLP

New York, New York
July 29, 2016

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, 2016

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

Certification

I, Steven L. Bernstein, 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, 2016

By: /s/ Steven L. Bernstein
Steven L. Bernstein
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, 2016 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, 2016

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, 2016 as filed with the Securities and Exchange Commission on the date hereof (the "Report"), I, Steven L. Bernstein, 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/ Steven L. Bernstein
Steven L. Bernstein
Chief Financial Officer

July 29, 2016

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 .