Acquisitions

Alliances

strategic growth

Joint Ventures

Expanding Markets

1999 Annual Report

From left to right:
Edward J. Fred, Executive Vice President,
Chief Financial Officer and Secretary;
Arthur August, Chairman and President;
Frank Funicelli, Vice President of Operations;

shareholder message

Arthur August
Chairman of the Board and President

The Company remains dedicated to strategic growth through acquisitions, alliances, joint ventures, and expanding markets.

CPI has entered the new millennium in strong fashion by both supporting our commitment to increase shareholder value and provide a more stable revenue base. The year 1999 was noteworthy both for the number of contracts awarded to CPI Aerostructures as well as the return of our Kolar subsidiary to pre-Asian crisis revenue levels resulting in the highest revenues in our history. We expect this trend to continue in the year 2000 as our customer base projects future market growth.

Consolidated revenue for the year ended December 31, 1999 was $21.6 million compared to $19.8 million for the prior year. This increase was achieved despite the termination of the MD-90 program which made no contribution to sales in 1999. A large part of our growth was achieved by Kolar, which nearly equaled its 1997 revenue prior to the Asian slowdown.

Prior to the acquisition of Kolar, CPI has defined its strategic goals as growth through acquisition as a means to expand not only our revenue, but our customer base as well. The addition of Kolar was an initial step in support of this goal. Our timing was consistent with the actions of the larger firms in the Aerospace and Defense Industry and our plan was simple...focus on our core competency in the design and manufacture of precision parts and assemblies and find suitable acquisition candidates that would complement each other. We will not, however, sacrifice shareholder value just for the sake of growth. This was the case in early 2000, when we had to pass on the potential acquisition of a fine company when the cost, in terms of shareholder value became too great.

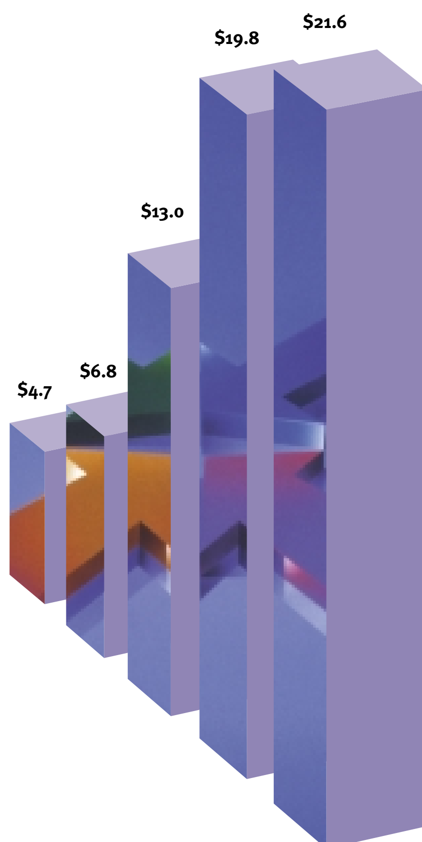
We believe our present operating divisions provide synergy to solicit more complex parts that could significantly increase our value to the customer, and consequently increase our sales. Kolar produces medium sized precision parts, to very strict just-in-time delivery requirements, for the high speed automated electronic manufacturing and automated processing equipment industries. CPI Aerostructures complements this capability with an assembly expertise applicable to military and commercial markets.

The Company remains dedicated to growth through the acquisition of businesses that would further enhance our overall technical capability and contribute products and customers in expanding markets. We will look for mature companies, preferably in niche markets and with complementing technologies. We believe there are still excellent candidates in the marketplace and intend to be prudent and diligent in our search.

On Behalf of the Board of Directors

Arthur August
Chairman of the Board and President

Consolidated Revenue
(in millions of dollars)



growth THROUGH acquisition

Products and Markets

During the last decade the aerospace industry has undergone significant changes. There were unprecedented mergers in the mid 1990's, the Asian crisis, explosive growth in airline revenues resulting in new aircraft purchases, downsizing, outsourcing, military budget constraints, expanded use of computer technology, shrinkage in the supplier base and new quality standards to name a few that have received widespread attention.

In this rapidly changing environment CPI has periodically evaluated its capabilities and markets with resultant changes in its strategic plan. It became evident that a growth strategy relying on the pursuit of new business with existing customers was no longer feasible and that growth through acquisition was necessary to penetrate new markets and broaden our business base. The successful implementation of this strategy, with the acquisition of Kolar, provided an initial expansion of CPI's customers and market base yielding greater diversification and stability of revenues. The continuation of this plan with acquisitions that have complementary markets and technical capability is intended to strengthen CPI's core capability in the design and manufacture of precision parts.

The process of acquisition has greatly expanded the Company's base of customers. A continuation of this process creates the opportunity to market each subsidiary's unique products to customers who have been closed to new suppliers due to the fierce competition in the industry. With a broader comprehensive variety of products and manufacturing capabilities, existing customers can be approached for bidding on a wider variety of products than previously available. This concept of "One Stop" shopping provides significant customer savings in their subcontracting process. Not only can a wider variety of precision parts be offered to such customers but, combined with CPI's assembly expertise, it is possible to offer complex assemblies with precision parts as components, as is occurring with our Kolar subsidiary. This approach enhances CPI's ability to bid lower prices and share contract work with more than one subsidiary, thus allowing for economies in design, purchasing and administration. Each of the subsidiaries offers a different customer base in which to implement this sales approach.

CPI Aerostructures is engaged in contract production of structural aircraft parts and sub-assemblies for the commercial and military segments of the aircraft industry. This segment of operations consists primarily of incorporating component aircraft parts supplied by third parties into complex sub-assemblies to satisfy specific customer

providing TOTAL capability

requirements and precision certification standards. The Company provides engineering, technical and program management services to its customers. At present, its major customers are the various U.S. military bases. Its market is 100% in the aerospace industry.

Kolar produces medium size parts to strict just-in-time requirements for the high speed automated electronic and processing equipment industries. They are 100% commercial with a prestigious customer list including Universal Instruments, IBM, Automatic Switch Co., Corning, DFF Corp., Curly Precision, Harris Tool, Hi Speed CheckWeigher, Lockheed Martin and Moog Industrial Controls.

The Consolidated Company:

The Company offers a single source for the manufacture and assembly of selective parts and sub-assembly's. With CPI's comprehensive variety of products and manufacturing capabilities, customers can be approached for bidding on a wide variety of products. This "One-Stop" shopping feature provides significant customer savings in the subcontracting process, thus creating additional growth opportunities.

Each of the subsidiaries of CPI is involved in the manufacture of precision parts, but each has unique products and technical capability within their present sphere of business. When combined they provide a wider variety of products and technical capabilities to be available to the entire customer base. This will allow for mutual sharing of design knowledge, prior problems solved, innovative manufacturing techniques and economies of purchasing and administrative functions. In addition, the administrative and accounting functions are integrated through a datalink network allowing for real time access to each subsidiaries raw material and finished goods inventory, shipments, cost data, schedules and other data. As an added advantage there is no duplication of technical and management personnel. Each subsidiary has in-place team prepared to maintain operations and customer support.

CPI Aerostructures

The overall aircraft market can be basically divided into commercial and military products. Each of these markets operates independently of the other. The commercial segment is market driven based on economic considerations such as airline profitability resulting in new orders, the age of existing inventory that may need replacement,
technological improvements that would affect cost of operations, competition from competitors and similar business issues. The military segment is more susceptible to variations based on political and national

defense priorities. In its plan to penetrate these markets CPI Aerostructures has elected to concentrate on the replacement spares for military aircraft already in the Government inventory. This is a more predictable market based on the need of the military to maintain their operational readiness and "Keep Them Flying". During the year 1999, CPI was awarded over 130 different contracts by the various military bases, with approximately $1.4 million in new contracts since October 1, 1999. The commercial aircraft market has undergone significant changes in the last decade. After all the mergers and acquisitions were completed the world market for large commercial aircraft (over 100 seat capacity) is presently dominated by Boeing and the European Airbus Consortium. With this contraction of producers came a shrinkage in their supplier base. This process and the lack of new commercial aircraft in the research and development phase has limited CPI's opportunities in this market. It is our opinion that this is a cyclical market condition and CPI Aerostructures will vigorously pursue new opportunities as they develop. For this market CPI will seek business in providing parts and sub-assemblies for new aircraft rather than replacement spares. The possibility for long term contracts and stability of revenues is a major advantage is this marketplace.

Kolar

The mission of Kolar has been to provide their customers with a total manufacturing concept that includes precision machining, electromechanical assembly, project management and a full service warehousing operation tailored to timely deliveries that satisfy customer quality and schedule requirements. Founded in Ithaca, New York in 1937, Kolar has grown to provide precision parts and sub-assemblies to prestigious electronic and materials processing equipment manufacturers, as well as to the military and commercial aircraft markets.

Tim Stone, President, Kolar, Inc.

While the majority of its equipment is state-of-the-art, computerized, numerically controlled machinery, it continues to manufacture selected parts on conventional machines and provides its own welding capability. One of its major accomplishments has been the development of a just-in-time delivery capability to allow its customers to minimize their inventory. Its largest customer manufactures equipment that produces electronic components. One such product is a high speed machine that mounts electronic components on printed circuit boards for which Kolar supplies detail parts and a major sub-assembly. The eventual printed circuit boards are used in cellular telephones, ATM machines, computers and a variety of other electronic devices. This machine is manufactured to exacting standards for an international market, and Kolar is one of the top rated suppliers to this customer. In the materials processing market Kolar's customer produces equipment used for the weighing and measuring of cartons and containers. Various industries require that their packaged products have a specific weight content. Kolar manufactures precision parts for major equipment manufacturers such as Universal Instruments, IBM, Automatic Switch Co., Corning, DFF Corporation, Gurley Precision, Harris Tool, Hi Speed CheckWeigher, Lockheed Martin and Moog Industrial Controls. The Kolar team is capable of providing technical assistance in the early stages of development to insure that the product is made to customer specifications, with the least cost and to the most efficient schedule.

precision WITH quality

Quality and Performance

In each of the markets served by CPI there has been a shrinking of the supplier base to concentrate on those companies who have demonstrated a previous commitment to improved quality and performance to customer specifications. One such standard adopted by industry in general has been those specifications set forth by the International Organization for Standardization (ISO-9000). This set of specifications has become the standard measure for many firms, especially those doing business in the international marketplace.

At CPI quality and on-time delivery are considered fundamental and given the highest priority to instill customer confidence and provide the necessary ingredients for continued business growth. Keeping pace with the competitive environment requires constant training, education and management attention. CPI offers the benefits of a small business combined with the ability to manufacture parts and sub-assemblies at competitive prices, while still maintaining project management and technical expertise from the initial contract award through tool design, production, inspection and customer acceptance. A fully integrated and computerized project control system is on-line to provide job cost, inventory, accounting and payroll data by contract. All the segments of the Company have excellent, long-term customer relationships and are qualified to the high standards required of military and commercial specifications.

The Kolar subsidiary received ISO-9000 certification in September of 1999, culminating nearly eighteen months of hard work and dedication to quality.

In Summary

CPI Aerostructures provides the expertise to bind its operating segments together as a manufacturer of detail parts with an assembly capability. We believe that this combination provides great synergy by allowing the solicitation of contracts for extremely complex parts which could significantly increase our value to the customer, increase sales and reduce costs. Many complex parts require the strong program management skills sought by the customer and which CPI Aerostructures has provided for many years. We will continue to seek acquisition candidates that have similar backgrounds, employ similar technologies, manufacture precision parts utilizing similar equipment and support similar markets albeit with differing products. This provides an excellent opportunity for exposure of the consolidated company to a broader variety of customers and thus an enhanced sales opportunity. Such acquisitions will always be evaluated on the basis of their contribution to shareholder value.

CPI Aerostructures, Inc. and Subsidiary

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Financial Highlights

Year ended December 31,	**1999**	1998	1997	1996	1995
			(Dollars in Millions)		
Operating Data:					
Revenues	**$21.6**	$ 19.8	$13.0	$ 6.8	$ 4.7
Gross Profit	**$ 5.9**	$ (5.0)**	$ 3.9	$ 2.6	$ 0.4
Net Income	**$ .8**	$ (8.6)**	$ 0.9	$ 0.5	$ (1.1)*
Balance Sheet Data:					
Working Capital	**$ 4.9**	$ 4.6	$13.1	$10.8	$10.1
Total Assets	**$22.7**	$21.9	$33.1	$13.1	$13.0
S/H Equity	**$ 7.2**	$ 6.1	$14.6	$11.0	$ 8.7

*Includes non-cash adjustment for terminated contract. Net income before adjustment $0.3 million.

**Includes non-cash adjustment for termination of MD-90 contract.

CPI Aerostructures, Inc. and Subsidiary

Management's Discussion and Analysis

The following discussion and analysis should be read in conjunction with the Financial Statements and Notes thereto appearing under Item 7 of this Report.

Certain statements discussed in this Report include forward-looking statements that involve risks and uncertainties, including the timely delivery and acceptance of the Company's products, the timing of commercial and government funding approvals, and the other risks detailed from time to time in the Company's SEC reports.

General

Consistent with industry practice, CPI uses the percentage of completion method of accounting for its business. Under this method, CPI recognizes revenues as costs are incurred under its contracts, measured by the percentage of actual costs incurred to date against estimated total costs. Under CPI's commercial contracts, CPI does not receive cash payments until products are shipped. Accordingly, revenues may be recognized by CPI even though associated cash payments have not been received. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are determined. Changes in contract performance may result in revisions to costs and income, which are recognized in the period in which revisions are determined to be required. CPI's recorded revenues may be written-off in later periods in the event CPI's cost estimates prove to be inaccurate or a contract is terminated. For Kolar, revenue is recognized when goods are shipped to customers.

Results of Operations

Year Ended December 31, 1999 as Compared to the Year Ended December 31, 1998

The Company's revenue for the year ended December 31, 1999 ("1999") was $21,603,000 compared to $19,810,000 for the year ended December 31, 1998 ("1998"), representing an increase of $1,793,000, or 9%. This increase reflects an increase in sales by Kolar. Sales by CPI decreased by approximately $2,413,000 from 1998 to 1999 due to the termination of the MD-90 contract with Rohr.

Gross profit for 1999 was $5,935,000 compared to gross loss of $4,953,000 for 1998, representing an increase of $10,888,000. Gross profit as a percentage of revenue for 1999 was 27%, compared to a negative percentage for 1998. This increase in gross profit percentage was attributable to the termination of the MD-90 program in 1998 resulting in a write-off of approximately $11,850,000.

Selling, general and administrative expenses for 1999 were $4,018,000 compared to $4,423,000 for 1998, representing a decrease of $405,000. This decrease is primarily attributable to the retirement of two employees, including an executive officer. Selling, general and administrative expenses as a percentage of revenue for 1999 and 1998 were 19% and 22%, respectively. Interest expense for 1999 was $1,117,000, compared to $1,264,000 for 1998, representing a decrease of $147,000.

The net income for 1999 was $809,000 compared to net loss of $8,566,000 for 1998, representing an increase of $9,375,000. Basic earnings per share was $.31 on 2,648,509 average shares outstanding compared to basic loss per share of $(3.23) on 2,647,259 average shares outstanding for fiscal 1998. Diluted earnings per share was $.30 in 1999 on 2,654,273 weighted average shares outstanding.

Liquidity and Capital Resources

General

A large portion of the Company's cash has been used for costs incurred on various commercial contracts that are in process. These costs are components of "Costs and estimated earnings in excess of billings on uncompleted contracts" and represents the aggregate costs and related earnings for uncompleted contracts for which the customer has not yet been billed. These costs and earnings are recovered upon shipment of products and presentation of billings in accordance with contract terms. CPI's continued requirement to incur significant costs, in advance of receipt of associated cash for commercial contracts has caused an increase in the gap between aggregate costs and earnings and the related billings to date.

Net cash provided by operating activities for 1999 was $1,458,000 compared to $8,000 for 1998. This increase in cash was primarily attributable to net income of $809,000, depreciation and amortization of $1,704,000, non-cash consulting fees of $275,000, change in deferred income taxes of $266,000, a decrease in income tax receivable of $486,000, an increase in accounts payable and accrued expenses of $232,000 and an increase in income taxes payable of $26,000 offset by an increase in accounts receivable of $656,000, an increase in costs and estimated earnings in excess of billings of $833,000, an increase in inventory of $772,000, an increase in prepaid expenses and other current assets of $19,000 and an increase in other assets of $380,000.

Net cash used in financing activities was $1,512,000 in 1999, compared to $1,377,000 in 1998. The Company repaid long term debt of $1,512,000 in 1999, as compared to $1,798,000 in 1998. The Company received $45,000 from the exercise of stock options and warrants in 1998. Net cash used in investing activities of $234,000 for 1999 and $79,000 for 1998 resulted from the Company's purchase of additional property and equipment in 1999.

As a result of the foregoing, the Company's cash at December 31, 1999 decreased by $289,000 from the prior year to $296,000. The Company believes it will have sufficient cash flow for 2000 to satisfy its cash requirements.

Financing Arrangements

The Company has an agreement with The Chase Manhattan Bank and Mellon Bank providing a line of credit through June 30, 2000, which will be used for working capital and other corporate purposes as needed. The Company has available up to $400,000 under the line of credit, subject to limits based on amounts of accounts receivable and inventory, as defined. Interest is at the bank's prime rate (8.5% at December 31, 1999) plus 1.5%. The line of credit is secured by substantially all assets of the Company. As of December 31, 1999, there was an outstanding balance of $375,000 on this line of credit.

On October 9, 1997, the Company incurred significant indebtedness in connection with the acquisition of Kolar Machine, Inc. The Company entered into a term loan agreement with The Chase Manhattan Bank and Mellon Bank in the amount of $9,400,000. This loan was payable in quarterly installments of $587,000, plus monthly interest at the Bank's published prime rate plus 1.5%, maturing December 31, 2001. This loan is collateralized by all of the assets of the Company and its subsidiary. The Company also entered into a mortgage loan agreement with The Chase Manhattan Bank in the amount of $975,000. This loan is payable in monthly installments of $9,487, including interest at 8.3%, maturing October 31, 2007. This loan is collateralized by Kolar's land and building. Additionally, the Company entered into a subordinated note agreement with the seller of Kolar in the amount of $4,000,000. Interest only is payable monthly at 8%, maturing December 31, 2001, payable 91 days following maturity. This note is currently convertible into 333,334 shares of CPI common stock.

In December 1998, the Company re-structured its term loan agreement with the Chase and Mellon banks. Under the new arrangement, the principal payment due in December 1998, was deferred and will be amortized evenly through December 31, 2001. Loan payments for 1999 were payable monthly, at the rate of $120,000 per month through December 31, 1999. Commencing January 2000, the amortization increased to $200,000 per month, and will increase to $317,000 per month commencing January 2001. Additionally, the seller of Kolar has deferred the Company's payment of interest to him for thirteen months, beginning with the December 1998 payment. This deferred interest will accrue and become payable upon maturity of the seller's note. Interest payments began again in January 2000.

Year 2000 Problem

The Company has evaluated the potential impact of the situation commonly referred to as the "Year 2000" ("Y2K") issue. The Y2K issue results from the problem with older computer software programs that only recognize the last two digits of the year in any date (e.g., "98" for "1998"). The Company has had no impacts of Y2K non-compliance from suppliers and customers.

Inflation

Inflation has historically not had a material effect on the Company's operations.

Impact of Accounting Standards Adopted by the Company

The impact of recently adopted accounting standards is discussed in Note 1 of Notes to Financial Statements.

Forward-Looking Statements

Certain of the statements contained in this Annual Report are forward-looking statements. While these statements reflect the Company's beliefs as of the date of this report, they are subject to uncertainties and risks that could cause actual results to differ materially. These factors include, but are not limited to, the demand for the Company's products and services, economic and competitive conditions, access to borrowed or equity capital on favorable terms, and other risks detailed in the Company's Annual Report on Form 10-K for the year ended December 31, 1999 and other filings with the Securities and Exchange Commission.

Consolidated Balance Sheet

December 31,	1999
ASSETS (Notes 5 and 7)	
Current Assets:	
Cash and cash equivalents	**$ 295,698**
Accounts receivable	**2,345,490**
Income tax refund receivable	**29,597**
Costs and estimated earnings in excess of billings on uncompleted contracts	**3,938,529**
Inventory	**3,209,931**
Deferred income taxes, net of valuation allowance of $2,152,000	**759,000**
Prepaid expenses and other current assets	**121,184**
Total current assets	**10,699,429**
Property, Plant and Equipment, net	**5,046,021**
Goodwill	**6,582,588**
Other Assets	**367,673**
Total Assets	**$22,695,711**
LIABILITIES AND SHAREHOLDERS' EQUITY	
Current Liabilities:	
Accounts payable	**$ 2,185,477**
Income taxes payable	**25,560**
Accrued expenses	**669,735**
Line of credit	**375,000**
Current portion of long-term debt	**2,537,177**
Total current liabilities	**5,792,949**
Long-term Debt	**9,023,024**
Interest Payable	**320,000**
Deferred Income Taxes	**366,000**
Total liabilities	**15,501,973**
Commitments and Contingencies	
Shareholders' Equity:	
Common stock—$.001 par value; authorized 50,000,000 shares, issued and outstanding 2,648,509 shares	**2,649**
Additional paid-in capital	**12,206,024**
Accumulated deficit	**(5,014,935)**
Shareholders' equity	**7,193,738**
Total Liabilities and Shareholders' Equity	**$22,695,711**

See Notes to Consolidated Financial Statements

Consolidated Statement of Operations

Year ended December 31,	**1999**	1998
Revenue	**$21,603,284**	$ 19,810,471
Cost of sales	**15,668,154**	24,763,293
Gross profit (loss)	**5,935,130**	(4,952,822)
Selling, general and administrative expenses	**4,018,232**	4,422,786
Income (loss) from operations	**1,916,898**	(9,375,608)
Other (income) expense:		
Interest income	**(667)**	(11,344)
Interest expense	**1,116,661**	1,263,868
Other income, net	**(311,013)**	(122,207)
Total other expenses, net	**804,981**	1,130,317
Income (loss) before provision (benefit) for income taxes	**1,111,917**	(10,505,925)
Provision (benefit) for income taxes	**303,000**	(1,940,000)
Net income (loss)	**$ 808,917**	$ (8,565,925)
Earnings (loss) per common share—basic	**$ .31**	$ (3.23)
Earnings per common share—diluted	**$ .30**	—
Shares used in computing earnings per common share:		
Basic	**2,648,509**	2,647,259
Diluted	**2,654,273**	—

See Notes to Consolidated Financial Statements

Consolidated Statement of Shareholders' Equity

Years ended December 31, 1998 and 1999

	Common Shares	Amount	Additional Paid-in Capital	Retained Earnings (Accumulated Deficit)	Total Shareholders' Equity
Balance at January 1, 1998	2,634,280	$2,634	$11,851,234	$ 2,742,073	$14,595,941
Net loss	—	—	—	(8,565,925)	(8,565,925)
Amortization of fair value of warrants issued in conjunction with consulting agreement	—	—	35,066	—	35,066
Shares issued upon exercise of stock warrants	14,229	15	45,222	—	45,237
Balance at December 31, 1998	2,648,509	2,649	11,931,522	(5,823,852)	6,110,319
Net income	—	—	—	808,917	808,917
Amortization of fair value of warrants issued in conjunction with consulting agreement	—	—	274,502	—	274,502
Balance at December 31, 1999	2,648,509	$2,649	$12,206,024	$(5,014,935)	$ 7,193,738

See Notes to Consolidated Financial Statements

Consolidated Statement of Cash Flows

Year ended December 31,	**1999**	1998
Cash flows from operating activities:		
Net income (loss)	**$ 808,917**	$(8,565,925)
Adjustments to reconcile net income (loss) to net cash provided by operating activities:		
Depreciation and amortization	**1,704,030**	1,394,923
Noncash consulting fees	**274,502**	35,066
Deferred portion of provision for income taxes	**266,000**	(1,454,000)
Changes in operating assets and liabilities:		
(Increase) decrease in accounts receivable	**(656,283)**	131,071
(Increase) decrease in income tax refund receivable	**486,403**	(516,000)
(Increase) decrease in costs and estimated earnings in excess of billings on uncompleted contracts	**(832,605)**	9,817,845
Increase in inventory	**(771,516)**	(121,284)
Increase in prepaid expenses and other current assets	**(19,183)**	—
(Increase) decrease in other assets	**(379,740)**	29,752
Increase (decrease) in accounts payable and accrued expenses	**231,959**	(200,105)
Increase (decrease) in income taxes payable	**25,560**	(543,000)
Increase in interest payable	**320,000**	—
Net cash provided by operating activities	**1,458,044**	8,343
Cash flows from investing activities:		
Purchase of property, plant and equipment	**(245,438)**	(78,892)
Proceeds from sale of fixed assets	**11,183**	—
Net cash used in investing activities	**(234,255)**	(78,892)
Cash flows from financing activities:		
Proceeds from line of credit	**200,000**	375,000
Proceeds from officer's note	**130,000**	—
Repayment of long-term debt	**(1,512,387)**	(1,797,575)
Repayment of officer's note	**(130,000)**	—
Repayment of line of credit	**(200,000)**	—
Proceeds from exercise of stock warrants	—	45,237
Net cash used in financing activities	**(1,512,387)**	(1,377,338)
Net decrease in cash	**(288,598)**	(1,447,887)
Cash and cash equivalents at beginning of year	**584,296**	2,032,183
Cash and cash equivalents at end of year	**$ 295,698**	$ 584,296
Supplemental disclosures of cash flow information:		
Cash paid during the year for:		
Interest	**$ 795,365**	$ 1,237,201
Income taxes	**$ 11,197**	$ 560,819
Supplemental schedule of noncash financing activity:		
Financing obligation incurred in connection with the acquisition of equipment	**$ 505,274**	—

See Notes to Consolidated Financial Statements

1. Principal Business Activity and Summary of Significant Accounting Policies:

The Company consists of CPI Aerostructures, Inc. ("CPI") and Kolar, Inc. ("Kolar"), a wholly owned subsidiary formed in October 1997, collectively the "Company."

CPI's operations consist of the design and production of complex aerospace structural subassemblies under U.S. government and commercial contracts. The length of the Company's contracts varies but is typically between one and two years for U.S. government contracts and up to 10 years for commercial contracts.

Kolar's principal business is the precision computer numerical control machining of metal products on a contract-order basis. The Company operates in and distributes from New York State.

CPI's revenue is recognized based on the percentage of completion method of accounting for long-term contracts measured by the percentage of total costs incurred to date to estimated total costs at completion for each contract. Contract costs include all direct material, labor costs, tooling and those indirect costs related to contract performance, such as indirect labor, supplies, tools, repairs and depreciation costs. Selling, general and administrative costs are charged to expense as incurred. Estimated losses on uncompleted contracts are recognized in the period in which such losses are determined. Changes in job performance may result in revisions to costs and income and are recognized in the period in which revisions are determined to be required. In accordance with industry practice, costs and estimated earnings in excess of billings on uncompleted contracts, included in the accompanying consolidated balance sheet, contain amounts relating to contracts and programs with long production cycles, a portion of which will not be realized within one year. CPI's recorded revenue may be adjusted in later periods in the event that CPI's cost estimates prove to be inaccurate or a contract is terminated.

Kolar's revenue is recognized when goods are shipped to customers.

Inventory is stated at the lower of cost (first-in, first-out method) or market.

In December 1998, based on information received from Rohr Industries, Inc. ("Rohr"), CPI recognized a termination of its contract to produce apron assemblies for the MD-90, and recorded a noncash charge to cost of sales amounting to approximately $11,850,000.

The Company maintains cash in bank deposit accounts which, at times, may exceed federally insured limits. The Company has not experienced any losses in such accounts. The Company believes it is not exposed to any significant credit risk on cash.

The Company considers all highly liquid investments with an original maturity of three months or less to be cash equivalents.

Depreciation and amortization of property, plant and equipment is provided for by the straight-line method over the estimated useful lives of the respective assets or the life of the lease, for leasehold improvements.

The Company has incurred approximately $549,000 of costs of obtaining debt, and has deferred such costs. These costs will be amortized over the life of the debt. The unamortized portion of these deferred financing costs, approximately $259,000 at December 31, 1999, is included in other assets.

On June 24, 1999, the shareholders of the Company voted to enact a one-for- three reverse stock split. All earnings per share calculations, number of shares and equity transactions have been restated as if the reverse split occurred on January 1, 1998.

The preparation of financial statements in conformity with generally accepted accounting principles requires the use of estimates by management. Actual results could differ from these estimates.

In accordance with the provisions of Statement of Financial Accounting Standards ("SFAS") No. 123, Accounting for Stock-Based Compensation, the Company has elected to apply APB Opinion No. 25 and related interpretations in accounting for its stock options issued to employees and, accordingly, does not recognize additional compensation cost as required by SFAS No. 123. The Company, however, has provided the pro forma disclosures as if the Company had adopted the cost recognition requirements.

Basic earnings per common share is computed using the weighted average number of shares outstanding. Diluted earnings per common share is computed using the weighted-average number of shares outstanding adjusted for the incremental shares attributed to outstanding options and warrants to purchase common stock. Incremental shares of 5,764 were used in the calculation of diluted earnings per common share in 1999. The convertible securities attributable to the note payable—seller (see Note 5) have been excluded from the fully diluted computation as their effect would be antidilutive. In 1998, diluted earnings per share are not presented as the result is antidilutive.

2. Costs and Estimated Earnings in Excess of Billings on Uncompleted Contracts:

At December 31, 1999, costs and estimated earnings in excess of billings on uncompleted contracts consist of:

	U.S. Government	Commercial	Total
Costs incurred on uncompleted contracts	$3,438,306	$10,581,169	$14,019,475
Estimated earnings	1,147,122	5,358,173	6,505,295
	4,585,428	15,939,342	20,524,770
Less billings to date	2,566,070	14,020,171	16,586,241
Costs and estimated earnings in excess of billings on uncompleted contracts	$2,019,358	$ 1,919,171	$ 3,938,529

Unbilled costs and estimated earnings are billed in accordance with applicable contract terms. As of December 31, 1999, approximately $1,407,000 of the balances above are not expected to be collected within one year.

3. Inventory:

Inventory consists of the following:

Raw materials	$1,033,104
Work-in-progress	767,851
Finished goods	1,408,976
	$3,209,931

4. Property, Plant and Equipment:

Property, plant and equipment, at cost, consists of the following:

December 31, 1999		Estimated Useful Life
Land	$ 412,200	
Machinery and equipment	5,470,248	5 to 10 years
Building	918,693	39 years
Furniture and fixtures	60,034	7 years
Automobiles and trucks	101,498	5 years
Leasehold improvements	66,791	3 years
	7,029,464	
Less accumulated depreciation and amortization	1,983,443	
	$5,046,021	

Approximately $505,000 of equipment was financed in 1999 through capital lease obligations. As of December 31, 1999, the Company recorded approximately $29,000 of depreciation expense on this equipment.

5. Long-Term Debt:

Long-term debt consists of the following:

Note payable—bank (a)	$ 6,197,500
Note payable—bank (b)	891,713
Note payable—seller (c)	4,000,000
Other (d)	470,988
	11,560,201
Less current maturities	2,537,177
	$ 9,023,024

(a) The note, as amended in December 1998, is payable to a commercial bank in monthly installments of $200,000 from January 2000 through December 2000, and $317,000 from January 2001 through December 2001, plus monthly interest at the bank's published prime rate (8.50% at December 31, 1999) plus 1.5%. This note and the line of credit disclosed in Note 8 are collateralized by substantially all of the assets of the Company. The amended note provides that since certain conditions were not met by March 31, 1999, the Company was subjected to an additional $300,000 fee on this note.

(b) The note is payable to a commercial bank in monthly installments of $9,487, including interest at 8.3%, maturing October 31, 2007. This note is collateralized by Kolar's land and building.

(c) In 1997, the Company acquired substantially all of the assets of Kolar Machine Inc. The acquisition was partially financed through a $4,000,000 note payable to the seller ("Seller") of Kolar Machine Inc. The note payable to the Seller bears interest at 8% per annum. The Seller has deferred the Company's payment of interest on this note until January 2000. The accrued interest through December 1999 will be payable upon maturity of the Seller's note. Monthly interest payments will begin again in January 2000. This note matures April 1, 2002. The note payable—Seller is convertible into 333,334 shares of the Company's common stock at any time prior to the maturity of the note.

(d) This item consists of various capital leases on equipment as well as auto loans.

Maturities of long-term debt are as follows:

Year ending December 31,	
2000	$ 2,537,177
2001	3,938,926
2002	4,142,713
2003	149,819
2004	145,385
Thereafter	646,181
	$11,560,201

At December 31, 1999, the carrying value of the Company's long-term debt approximated its estimated fair value based upon current borrowing rates for similar issues.

6. Commitments:

The Company leases office and warehouse facilities under a noncancelable operating lease expiring in March 2000.

In September 1999, the Company entered into a noncancelable operating lease expiring in August 2002 for additional office and warehouse space.

The aggregate future minimum rental commitment under these leases are as follows:

Year ending December 31,	
2000	$ 92,073
2001	51,720
2002	34,480
	$178,273

Total rental expense for the years ended December 31, 1999 and 1998 amounted to $176,121 and $164,578, respectively. The Company is required to pay additional expenses, as defined.

The Company has employment agreements with four employees. The aggregate future commitment under these agreements are as follows:

Year ending December 31,	
2000	$ 638,077
2001	515,000
	$1,153,077

These agreements provide for additional bonus payments that are calculated, as defined.

7. Income Taxes:

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

Year ended December 31,	**1999**	1998
Current:		
Federal	**$ 4,000**	$ (497,000)
State and local	**33,000**	11,000
	37,000	(486,000)
Deferred:		
Federal	**231,000**	(1,309,000)
State and local	**35,000**	(145,000)
	266,000	(1,454,000)
	$303,000	$(1,940,000)

The difference between the income tax provision (benefit) computed at the federal statutory rate and the actual tax provision (benefit) is accounted for as follows:

Year ended December 31,	**1999**	1998
Taxes (benefit) computed at the federal statutory rate	**$ 378,000**	$(3,572,000)
State income taxes (benefit), including deferred, net of federal benefit	**25,000**	(686,000)
Other, including officers' life insurance and various permanent differences	**8,000**	14,000
Nonutilization of net operating loss carryforward		2,304,000
Utilization of net operating loss carryforward	**(108,000)**	—
	$ 303,000	$(1,940,000)

The components of deferred income tax assets (liabilities) are as follows:

	Current	Noncurrent
Long-term contracts	$ (11,000)	—
Property, plant and equipment	—	$(366,000)
Inventory	52,000	—
Net operating loss carryforwards	2,870,000	—
Valuation allowance	(2,152,000)	—
	$ 759,000	$(366,000)

As of December 31, 1999, the Company had net operating loss carryforwards of approximately $7,348,000 for federal income tax purposes expiring in 2013.

8. Line of Credit:

The Company has an aggregate $400,000 line of credit agreement, expiring June 30, 2000, with The Chase Manhattan Bank and Mellon Bank for working capital and other corporate purposes as needed. Borrowings are subject to limits based on amounts of accounts receivable and inventory, as defined. Interest is at the banks' prime rate (8.50% at December 31, 1999) plus 1.5%. The line of credit and the note payable described in Note 5(a) are collateralized by substantially all of the assets of the Company.

9. Employee Stock Option Plans:

In April 1992, the Company adopted the 1992 Stock Option Plan (the "1992 Plan"). The 1992 Plan, for which 83,334 common shares are reserved for issuance, provides for the issuance of either incentive stock options or nonqualified stock options to employees, consultants or others who provide services to the Company. The initial options granted to employees and directors with three or more years of service became exercisable as to one-third of the shares each year beginning on September 16, 1992. The initial options granted to those with less than three years of service became exercisable as to one-third of the shares each year beginning on September 16, 1993. The options may not be exercised more than five years from the date of issuance. In 1995, the option price for all outstanding employees' and director's stock options was lowered to $9.00.

In 1995, the Company adopted the 1995 Stock Option Plan (the "1995 Plan"), as amended, for which 200,000 common shares are reserved for issuance. The 1995 Plan provides for the issuance of either incentive stock options or nonqualified stock options to employees, consultants or others who provide services to the Company. The options' exercise price is equal to the closing price of the Company's shares on the day of issuance, except for incentive stock options granted to the Company's president, which are exercisable at 110% of the closing price of the Company's shares on the date of issuance.

In 1998, the Company adopted the 1998 Stock Option Plan (the "1998 Plan"). The 1998 Plan, as amended, reserved 463,334 common shares for issuance. The 1998 Plan provides for the issuance of either incentive stock options or nonqualified stock options to employees, consultants or others who provide services to the Company. The options' exercise price is equal to the closing price of the Company's shares on the day of issuance, except for incentive stock options granted to the Company's president, which are exercisable at 110% of the closing price of the Company's shares on the date of issuance.

The Company has 42,778 options available for future grant under the 1992 Plan, no options available for grant under the 1995 Plan, and 150,332 options available for grant under the 1998 Plan.

If the Company had elected to recognize compensation cost based on the fair value of the options granted at grant date as prescribed by SFAS No. 123, net income (loss) and earnings (loss) per share would have been adjusted to the pro forma amounts indicated in the table below:

	As Reported		Pro Forma	
	1999	1998	**1999**	1998
Net income (loss)	**$808,917**	$(8,565,925)	**$596,000**	$(8,733,702)
Earnings (loss) per share:				
Basic	**$ .31**	$ (3.23)	**$ .23**	$ (3.30)
Diluted	**$ .30**	$ —	**$ .22**	$ —

A summary of the status of the Company's three stock option plans as of December 31, 1999 and 1998 and changes during those years are as follows:

	1999		1998	
Fixed Options	**Options**	**Weighted-Average Exercise Price**	Options	Weighted-Average Exercise Price
Outstanding at beginning of year	**327,468**	**$5.97**	209,134	$5.52
Granted during year	**269,000**	**2.64**	118,334	6.72
Exercised	—	—	—	—
Forfeited	**81,155**	**5.72**	—	—
Outstanding at end of year	**515,313**	**$4.27**	327,468	$5.97

The following table summarizes information about stock options outstanding and exercisable at December 31, 1999:

Range of Exercise Price	Number Outstanding and Exercisable	Weighted-Average Remaining Contractual Life	Exercise Price
$2.53 – $9.00	515,313	3.79 years	$4.27

The Company's assumptions used to calculate the fair values of options issued were (i) risk-free interest rate of 5.25%, (ii) expected life of five years, (iii) expected volatility of 174.71% and (iv) expected dividends of zero.

10. Warrants and Options:

The Company sold 33,334 warrants to the Company's Underwriter ("Underwriter's Warrants") in September 1992 for an aggregate of $100. The Underwriter's Warrants, as adjusted, entitle the Underwriter, or its assignees, to purchase up to 188,680 shares of common stock at an exercise price of $3.18 and an aggregate of 33,334 warrants exercisable at $7.50. In 1997, 68,714 of the Underwriter's Warrants were exercised. The balance of the Underwriter's Warrants expired on September 24, 1999.

In February 1995, the Company issued stock options to a consultant to purchase 40,000 common shares at $9.00 per share, which options and accompanying consulting agreement were terminated by the Company and are the subject of a lawsuit. In April 1995, the Company also granted options to purchase 6,667 shares at $6.00 per share to its counsel. All of these options are outside the employee stock option plans and expire in April 2000. In January 1996, the Company issued stock options to purchase 6,167 shares at $3.18 per share to a director.

In March 1996, the Company issued 100,000 warrants to Barber and Bronson, Inc. as partial compensation for acting as the Company's Placement Agent for its private placement of equity. These warrants entitle the Placement Agent to purchase 100,000 shares of common stock at an exercise price of $3 during the five-year period commencing June 19, 1996. In 1997, 10,000 of these warrants were exercised.

In September 1996, the Company issued options to purchase 3,334 shares of common stock to two directors at an exercise price of $6.00 per share of common stock. These options expire in 2001.

In February 1997, the Company issued options to purchase 3,334 shares of common stock to two directors at an exercise price of $6.18 per share of common stock. These options expire in 2002.

In January 1998, the Company issued options to purchase 25,000 shares of common stock to a consultant, who was also a director, at an exercise price of $7.50 per share of common stock. In February 1998, the Company issued options to purchase 3,334 shares of common stock to two directors at an exercise price of $6.93 per share of common stock. These options expire in 2003.

In March 1998, the Company issued 33,334 warrants to Gaines Berland, Inc. as compensation for acting as the Company's investment banker pursuant to a consulting agreement. These warrants entitle the investment banker to purchase 33,334 shares of common stock at an exercise price of $7.50 during the five-year period commencing April 1, 1998. This agreement was terminated in 1999. The Company recorded a charge to operations of $198,734 to write off the unamortized portion of warrants issued under this agreement.

In May 1999, the Company issued 100,000 warrants to Catalyst Financial Corp as partial compensation for acting as the Company's investment banker pursuant to a consulting agreement. These warrants entitle the investment banker to purchase 100,000 shares of common stock at an exercise price of $1.875 during the five-year period commencing May 4, 1999. In December 1999, the Company issued options to purchase 15,000 shares of common stock to a consultant at the exercise price of $2.53 per share of common stock. Also in December 1999, the Company issued options to purchase 10,000 shares of common stock to two directors at an exercise price of $2.53 per share of common stock.

11. MD-90 Contract:

In March 1991, CPI entered into an agreement with Rohr, pursuant to which the Company agreed to provide Rohr with apron assemblies and related components in connection with production of the then proposed McDonnell Douglas MD-90 jet aircraft. During the year ended December 31, 1998, approximately 23% of the Company's revenue was derived from this program.

In 1997, the Boeing Company acquired the McDonnell Douglas Corporation. Boeing announced that it planned to terminate the MD-90 program unless it received sufficient additional orders for such aircraft.

In December 1998, based on information received from Rohr, the Company recognized a termination of this contract. This termination resulted in the Company writing off approximately $11,850,000 of previously recorded revenue. The effect of this write-off is included in cost of sales in 1998.

12. Employee Benefit Plans:

On September 11, 1996, CPI's board of directors instituted a defined contribution plan under Section 401(k) of the Internal Revenue Code (the "Code"). On October 1, 1998, the Company amended and standardized both the CPI and Kolar plans as required by the Code. Pursuant to the amended plan, qualified employees may contribute a percentage of their pre-tax eligible compensation to the Plan and the Company will match a percentage of each employee's contribution. Additionally, the Company has a profit-sharing plan covering all eligible employees. Contributions by the Company are at the discretion of management. The amount of contributions recorded by the Company in 1999 and 1998 amounted to $119,627 and $116,355, respectively.

13. Contingencies:

From time to time the Company is subject to routine litigation incidental to its business. The Company believes that the settlement of any pending legal proceedings will not have a material adverse effect on the Company's financial condition.

14. Segment Information:

The Company's operations are classified into two business segments: production of complex aerospace structural subassemblies ("Aerospace") and computer numerical control machining of metal products ("Machining").

Summarized financial information by business segment for 1999 and 1998 are as follows:

December 31,	**1999**	1998
Net sales:		
Aerospace	**$ 6,079,936**	$ 8,492,753
Machining	**15,523,348**	11,317,718
	$21,603,284	$ 19,810,471
Operating income (loss):		
Aerospace	**$ 474,212**	$(10,174,230)
Machining	**1,442,686**	798,622
	$ 1,916,898	$ (9,375,608)
Total assets:		
Aerospace	**$ 5,814,906**	$ 5,897,982
Machining	**16,880,805**	16,037,904
	$22,695,711	$ 21,935,886

December 31,	**1999**	1998
Depreciation and amortization:		
Aerospace	**$ 39,913**	$664,879
Machining	**718,433**	83,746
	$758,346	$748,625
Capital expenditures:		
Aerospace	**$ 23,488**	$ 42,512
Machining	**727,224**	36,380
	$750,712	$ 78,892

15. Major Customers:

Approximately 55% and 40% of the Company's sales in 1999 and 1998, respectively, were to Universal Instruments Inc. ("Universal").

Approximately 22% and 17% of the Company's sales in 1999 and 1998, respectively, were to the U.S. government.

Approximately 23% of the Company's sales in 1998 was to Rohr. At December 31, 1999, approximately 50% and 16% of accounts receivable were due from Universal and Rohr, respectively.

Independent Auditor's Report

To the Board of Directors
CPI Aerostructures, Inc.

We have audited the accompanying consolidated balance sheet of CPI Aerostructures, Inc. and Subsidiary as of December 31, 1999 and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the two years in the period ended December 31, 1999. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of CPI Aerostructures, Inc. and Subsidiary as of December 31, 1999, and the results of their operations and their cash flows for each of the two years in the period ended December 31, 1999 in conformity with generally accepted accounting principles.

GOLDSTEIN GOLUB KESSLER LLP
New York, New York

February 11, 2000

Market for Common Equity and Related Stockholder Matters

Market Information

The Company's securities are traded in the over-the-counter market and listed on the National Association of Securities Dealers Automated Quotation SmallCap Market ("Nasdaq").

The following tables set forth for the last two fiscal years, the range of high and low last sales prices of CPI's Common Stock for the periods indicated, as reported by Nasdaq. Nasdaq prices represent inter-dealer quotations, without retail mark-up, mark-down or commission, and may not necessarily represent actual transactions.

Period	High	Low
1998		
Quarter Ended March 31, 1998	$8.438	$6.938
Quarter Ended June 30, 1998	$9.375	$6.188
Quarter Ended September 30, 1998	$6.563	$2.438
Quarter Ended December 31, 1998	$6.000	$2.438
1999		
Quarter Ended March 31, 1999	$3.656	$2.063
Quarter Ended June 30, 1999	$2.344	$1.281
Quarter Ended September 30, 1999	$1.183	$1.25
Quarter Ended December 31, 1999	$3.094	$1.094

On March 15, 2000, the closing sale price for the Company's Common Stock on the Nasdaq was $3.750.

Holders

On March 15, 2000, there were 146 holders of record of the Company's Common Stock. The Company reasonably believes that there are in excess of 2,500 beneficial holders of its Common Stock.

Dividend Policy

To date, the Company has not paid any dividends on its Common Stock. The payment of dividends, if any, in the future is within the discretion of the Board of Directors and will depend on the Company's earnings, if any, its capital requirements and financial condition and other relevant factors. The Board of Directors does not intend to declare any cash or other dividends in the foreseeable future, but instead intends to retain earnings, if any, for use in the Company's business operations.

In addition, the Company's Credit Agreement with its several lenders provides that the Company may not declare or pay any dividend on its Common Stock so long as any amounts are owing to the several lenders. See "Item 6. Management's Discussion and Analysis—Financing Arrangements."

Officers

Arthur August
President and Chief Executive Officer

Edward J. Fred
Executive Vice President,
Chief Financial Officer and Secretary

Frank Funicelli
Vice President of Operations

Board of Directors

Arthur August
Chairman of the Board
President and Chief Executive Officer

Edward J. Fred
Executive Vice President,
Chief Financial Officer and Secretary

Walter Paulick
President
W.R. Paulick and Associates, Inc.
Financial Consulting Firm

Kenneth McSweeney
Principal
K.F. McSweeney, Unlimited

Corporate Headquarters

CPI Aerostructures, Inc.
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Edgewood, NY 11717
Tel: (631) 586-5200
Fax: (631) 586-5814
www.cpiaero.com

Transfer Agent

Communications regarding change of address, transfer of stock ownership, or lost stock certificates should be directed to:

North American Transfer
147 West Merrick Road
Freeport, NY 11520

Common Stock

CPI Aerostructures' common stock trades on The Nasdaq SmallCap Market under the symbol CPIA.

Independent Auditors

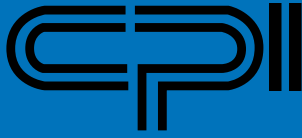
Goldstein Golub Kessler, LLP
1185 Avenue of the Americas
New York, NY 10036

Stockholder Contact and Form 10-KSB

Stockholders are encouraged to contact the Company with questions or requests for information. A copy of the Company's Annual Report on Form 10-K for the year ended December 31, 1999, as filed with the Securities and Exchange Commission, will be sent to stockholders free of charge upon written request. Inquiries should be directed to:

Chief Financial Officer
CPI Aerostructures, Inc.
200A Executive Drive
Edgewood, NY 11717
(631) 586-5200
or contact the Company at its website, www.cpiaero.com

Design: (RWI) robertwebsterinc.com



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