RESPIRONICS®

www.respironics.com

realize

2004 ANNUAL REPORT

Corporate Profile Respironics is a leading developer, manufacturer and distributor of innovative products and programs that serve the global sleep and respiratory markets. Focusing on emerging market needs, the Company is committed to providing valued solutions to help improve outcomes for patients, clinicians and healthcare providers. Respironics markets its products in more than 125 countries and employs over 3,200 associates worldwide.

Realize the Potential. By focusing on the sleep and respiratory marketplaces, Respironics realizes the potential exists to discover new therapies, new solutions, and new products that serve our markets. Respironics, with its strong tradition of pioneering innovation, is positioned to identify these new areas of opportunity by anticipating customer needs and providing valued solutions.

1 vision

To be the *worldwide leader* in anticipating needs and providing valued solutions to the sleep and respiratory markets.

John L. Miclot
President and Chief Executive Officer

Daniel J. Bevevino
Vice President and Chief Financial Officer

Craig B. Reynolds
Executive Vice President and Chief Operating Officer

From the President

Respironics has just completed another outstanding fiscal year with record results for our shareholders. We excelled in our core businesses across the divisions, enabling us to exceed our targets and further strengthen our balance sheet. This accomplishment demonstrates strength and balance in our performance, and equally reflects the successful execution of our strategic plan and the depth of our talent base.

We realize that it is our commitment to our shareholders, customers and patients that enables us to focus our energy, capabilities and resources. This focus has allowed us to achieve success and build momentum for both the Company and for our marketplace. We realize that our strategic plan and vision have provided a solid foundation needed to maintain this momentum and continue this success.

Early in the year, with guidance from Respironics' Board of Directors, our senior management team outlined a refined strategic direction and introduced a new vision statement to drive the Company. Both the strategy and the vision statement are focused on strengthening our leadership position by understanding and anticipating our customers' needs within the sleep and respiratory industries. This 'market needs' approach challenges Respironics to not only identify needs via a deep understanding of the marketplace, but to answer those needs with innovative solutions. Next, we must successfully deliver those solutions to the marketplace.

It is an aggressive and proactive approach that requires all of our associates to strengthen relationships with customers, increase communication with one another, and demonstrate agility in comprehending trends in the markets. This direction has proven to be effective since its implementation and will continue to be a driving force in the next fiscal year.

The strategic plan continues to emphasize leadership in our core market segments of obstructive sleep apnea, our ventilation portfolio via Total Ventilation Solutions℠, and our international expansion initiatives. At the same time, the Company plans to extend its presence in the broader sleep and respiratory marketplaces, exploring new opportunities and seeking areas for continued growth.

In the Homecare Division, diagnosis of sleep disorders and therapy for improved patient compliance continue to drive our leadership in sleep medicine. Respironics' proprietary C-Flex™ technology, inventive patient interfaces, and diagnostic devices provide solutions recognized in the global sleep marketplace. Our Hospital Division's comprehensive Total Ventilation Solutions program – which incorporates invasive and noninvasive ventilation, as well as respiratory gas monitoring – offers protocols to help accelerate the patient recovery process and reduce overall hospital stays.

Respironics' International Division continues to expand and strengthen distribution channels worldwide, working within each country's unique healthcare network to provide customers with the tools they need to help treat patients.

The world's sleep and respiratory markets hold great potential for continued growth and innovation. Undiagnosed patients with sleep disorders, and the growing number of patients worldwide with respiratory diseases, present us with the opportunity to provide solutions to aid our customers and their patients. As we continue to develop solutions to meet the needs of customers in our core markets, we also look to explore opportunities outside of these traditional market spaces. In order to assure the appropriate focus on broadening the scope of the Company, we have initiated efforts in three of our newer business segments: Children's Medical Ventures, which is focused on sleep and respiratory development in the Neonatal Intensive Care Unit; Sleep Well Ventures, which is focused on broadening our presence in sleep beyond obstructive sleep apnea; and respiratory drug delivery, which is focused on expanding our product portfolio in the area of drug delivery via the respiratory pathway. We are investing in these opportunities with the goal of developing additional growth drivers for the future.

We expect fiscal year 2005 to be another record-breaking year. Our objective is to continue to reinforce our leadership position in our core markets and to explore and expand new opportunities. Our associates will be focused on continued growth driven by strategic acquisitions and organic expansion, as well as a rich and active set of initiatives in under-penetrated segments to help us achieve our corporate strategic and fiscal goals.

I would like to extend my thanks and appreciation to our customers, our shareholders and our associates for their continued support and commitment to our Company. When I consider the many advantages we have, our dedicated and professional employees are at the top of that list. Their experience, talent and energy are what distinguish us from the competition. Together, we remain focused on serving our shareholders and customers, and we look forward to realizing even greater results in the new fiscal year.

Sincerely,

John Miclot
President and Chief Executive Officer

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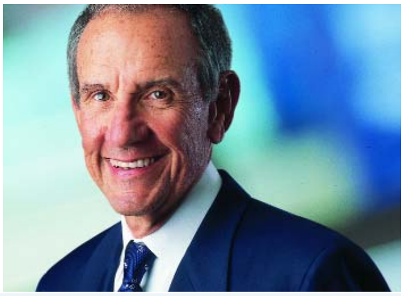
CONSECUTIVE QUARTERS OF GROWTH



From the Chairman

It gives me great pleasure to report to our shareholders that Respironics has enjoyed another strong fiscal year and is well positioned for the future.

In the beginning, I was alone on the company payrolls. I knew that every nickel this company earned would be available only if a happy customer had sent payment for a product that served his or her needs.

In addition to product satisfaction, customers would be happy only if every interaction with the company was pleasant and satisfying. If Respironics were to succeed, customers had to be dealing only with ethical, committed and competent people at all levels within the company. This meant that every employee was to play an important part in keeping that customer satisfied, either directly or behind the scenes.

Now, almost 30 years later, on the shop floors, in the offices and in the field, Respironics has more than 3,200 associates on its payroll, and continues to grow. Our people are recruited and retained based on ethics, commitment and ability. They understand that happy customers make our world go around and make our company a wonderful place to work. They derive personal satisfaction and a sense of achievement knowing that our products have not only changed many people's lives for the better, but saved many as well. And, it is this end result that presents the highest level of motivation and satisfaction for our people.

Enabling our people to achieve their outstanding performance year after year is a senior management team with notable talent, dedication, and integrity of purpose. Their imagination, resourcefulness and consistent results provide a high degree of comfort to the Respironics' Board of Directors that shareholders' interests are remarkably well served.

Our Board of Directors is comprised of four management people and eight outstanding independent Directors. This group's wide range of business experience and acumen is helping to reshape Respironics' governance policies and procedures. We do this not only to comply with recent federal legislation and SEC regulations, but also to use the individual and collective strengths of our members to support and counsel the management team. As shareholders themselves, these Board members are firmly committed and highly capable of representing and protecting the interests of Respironics' shareholders as a whole.

I believe that this company will continue to expand and realize opportunities worldwide. The committed people of Respironics – with a continuity of purpose, ethical values, focus and vision – are poised to carry us to a very bright future.

Thank you for your support.

Sincerely,

Gerald E. McGinnis
Advanced Technology Officer and
Chairman of the Board


52
million adults
in the United States suffer from obstructive sleep apnea.

> SLEEP DISORDERS

Current

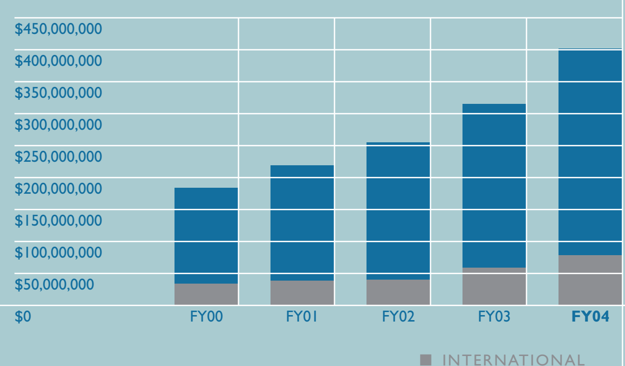
Respironics is the worldwide leader in the treatment of sleep-disordered breathing – driving success through innovation and a deep understanding of this market segment's needs. Obstructive sleep apnea (OSA) therapy, which has been a cornerstone of Respironics' business, continues to be a key growth driver of the Homecare Division. Fifty-two million adults in the United States suffer from OSA, and of these, 17.8 million suffer from symptomatic and severe asymptomatic OSA. Only 15 percent of those who suffer from OSA are currently treated for this severe disorder. This solid market base presents significant potential for Respironics' innovative diagnostic and therapeutic solutions.

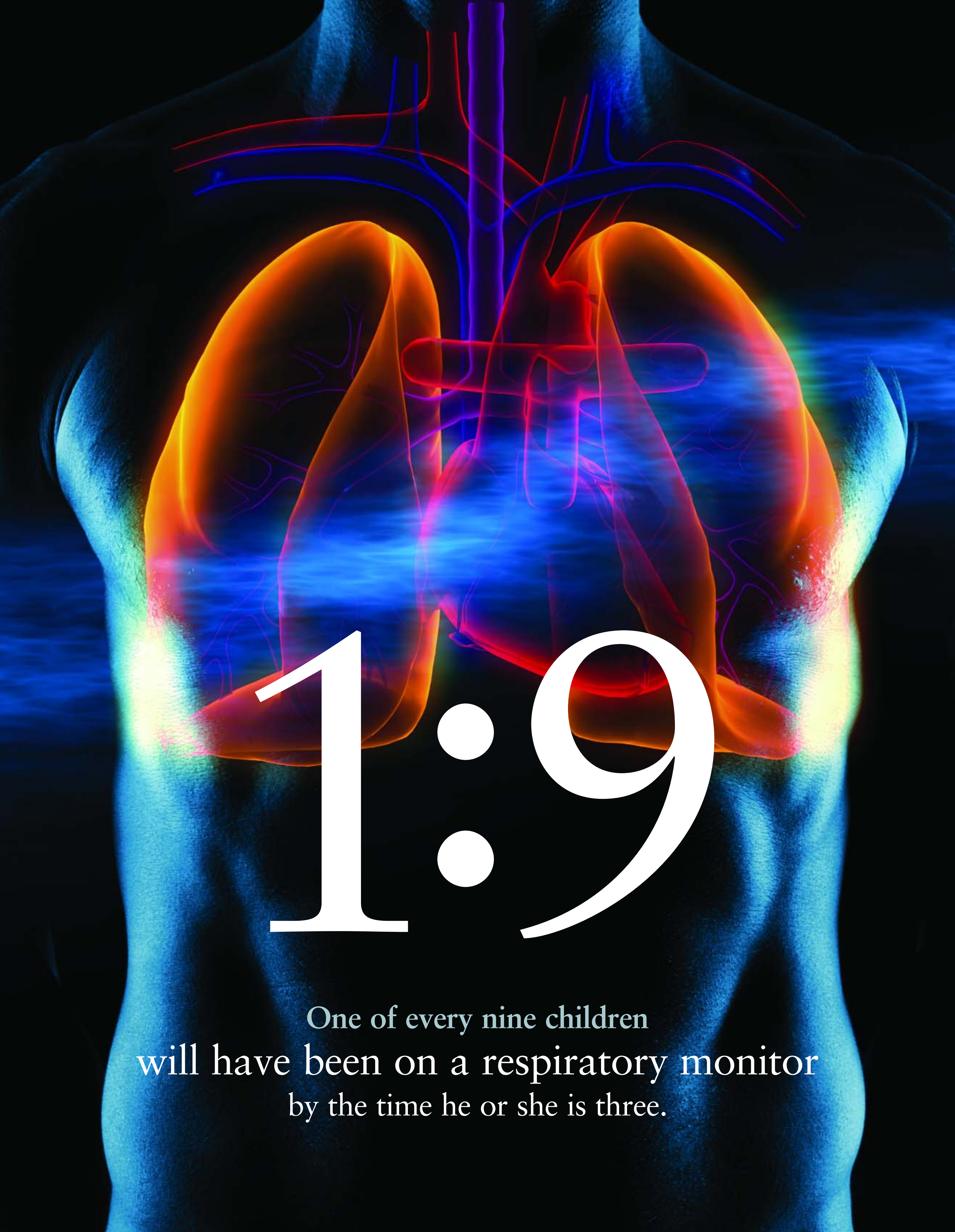
Our proprietary C-Flex™ technology and innovative mask designs – devised to help increase sleep therapy compliance by increasing patients' comfort – continue to lead the sleep market. Respironics' diagnostic screening devices and lab systems supply the tools and information that healthcare professionals need to diagnose patients' sleep disorders. Relationships with homecare providers, sleep labs and physicians are robust and provide us with insight for research, development and continued market expansion.

Future

Understanding patient and caregiver needs will continue to drive Respironics' success. The future of Respironics' business in the sleep marketplace extends beyond traditional sleep-disordered breathing, treatment and compliance. An emerging market segment designated as "the problem sleeper" provides significant untapped potential. Approximately 50 percent of adults in the United States describe themselves as being "problem sleepers" suffering from sleep disruptions that impact their quality of life. Beyond traditional OSA, opportunities exist in helping those with airway instability, insomnia, disrupted circadian rhythms, and those people who lack general sleep wellness. Our strategy will focus on offering solutions to these populations to help improve their quality of life. Respironics has committed resources to identify and provide valued solutions in this new frontier in sleep wellness.

> SLEEP THERAPY REVENUE




1:9
One of every nine children
will have been on a respiratory monitor
by the time he or she is three.

> RESPIRATORY DISORDERS

Current

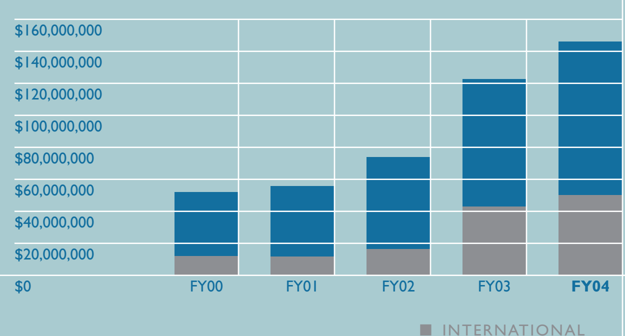
The prevalence of respiratory diseases worldwide continues to increase. Current statistics show that chronic obstructive pulmonary disease (COPD) – which includes chronic bronchitis and emphysema – is now the fourth leading cause of death among Americans and is expected to become the third leading cause by 2020. Twenty million people in the United States suffer from asthma; seven million of these are children. One of every nine children will have been on a respiratory monitor by the time he or she is three.

To meet the needs of these growing populations, Respironics provides a broad range of respiratory solutions, from the pre-hospital emergency setting, to the hospital, and ultimately to the home. The Company offers a comprehensive series of ventilators, asthma monitoring and management systems, oxygen delivery devices, cardiac and infant monitors, and respiratory gas analyzers to help manage patients with respiratory disorders throughout their lifetimes, from neonates to adults. Respironics Total Ventilation Solutions℠ provides a platform for managing patients in a variety of care environments. Capabilities include invasive ventilation, noninvasive ventilation and respiratory gas monitoring, providing healthcare professionals with a comprehensive set of options to optimize treatment for their patients while helping to reduce the cost of care.

Future

For Respironics, the opportunity to expand in the respiratory market space is significant. Not only are gains anticipated in the existing $4 billion market that Respironics participates in today, but; the company has also targeted certain additional segments of the $10 billion global respiratory market. Respiratory drug delivery systems and ambulatory oxygen are examples of the numerous opportunities for expanding our market presence in this space. Strategic acquisitions, international expansion and a plan to broaden the product portfolio are focused initiatives to facilitate our advances in this growing market.

> HOSPITAL REVENUE




7.5%
of the adults in India have
symptomatic sleep apnea.

> INTERNATIONAL MARKET

Current

Strategic international acquisitions, combined with strengthened distribution channels, have increased Respironics' influence in the global sleep and respiratory marketplaces. Operating within six continents, the Company supplies valued solutions to the hospital, homecare and respiratory drug delivery markets.

The niche for Respironics' products is evident. Data shows that the percentage of people affected by sleep-disordered breathing fluctuates worldwide, but on average a 4 percent prevalence of severe symptomatic sleep apnea syndrome is evident in populations studied. Estimates from Hong Kong suggest that 4.1 percent of the adults surveyed have symptomatic sleep apnea. In Europe, estimates range from 4 to 6 percent, and in India the number is estimated to be 7.5 percent.

Respiratory disease is a worldwide concern among adults as well as children. More than 150 million people around the globe have been diagnosed with asthma. Chronic obstructive pulmonary disease (COPD) is ranked with HIV/AIDS as the fourth leading cause of death worldwide. Data suggests that respiratory diseases are now the most common long-term illnesses among children, and are most often cited as the cause for hospital emergency room admissions.

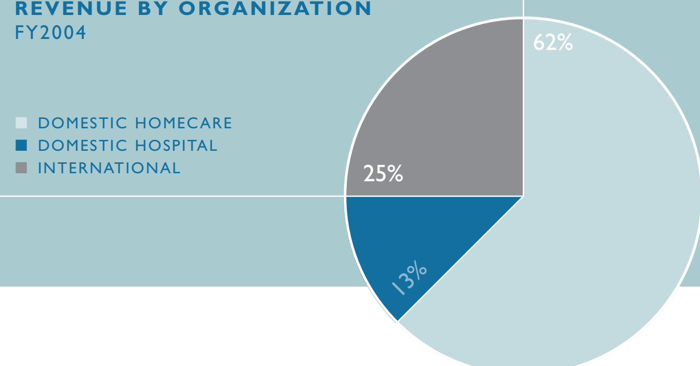
Future

Respironics is positioned to address the increasing needs of populations suffering with sleep-disordered breathing and respiratory illnesses worldwide. The Company's global network of associates is growing to meet the challenges of the future.

The prevalence of respiratory and sleep-related diseases is expected to increase in the future. Recent projections show that, by 2020, chronic obstructive pulmonary disease will escalate to become the third leading cause of mortality, accounting for six million deaths worldwide. Further, the steady increase in the incidence of asthma witnessed in recent decades is expected to continue as a result of increased urbanization among the world's population.

As awareness of sleep-disordered breathing and apnea increases, and facilities for diagnosis spread, the number of patients determined to have sleep disorders and in need of treatment is expected to grow. Emerging markets for sleep-disordered breathing include South America and Asia, areas where Respironics is well established.

> REVENUE BY ORGANIZATION
FY2004

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> EXECUTIVE OFFICERS

Gerald E. McGinnis [12]
Advanced Technology Officer and
Chairman of the Board

John L. Miclot [13]
President and Chief Executive Officer

Daniel J. Bevevino [1]
Vice President and Chief Financial Officer

Steven P. Fulton [4]
Vice President and General Counsel

Susan A. Lloyd [9]
Vice President, Respiratory Drug Delivery

William J. Post [15]
President, Homecare

Craig B. Reynolds [16]
Executive Vice President and
Chief Operating Officer

Geoffrey C. Waters [17]
President, International

Paul L. Woodring [18]
President, Hospital

> CORPORATE OFFICERS

(not shown)

Dorita A. Pishko
Corporate Secretary

James C. Woll
Vice President and Corporate Controller

> BOARD OF DIRECTORS

Gerald E. McGinnis [12]
Advanced Technology Officer and
Chairman of the Board

James W. Liken [7]
Vice Chairman

John L. Miclot [13]
President and Chief Executive Officer

Douglas A. Cotter [2]
Private Investor

J. Terry Dewberry [3]
Private Investor

Donald H. Jones [5]
Chairman, Triangle Capitol Corporation
(an investment firm)

Joseph C. Lawyer [6]
Vice Chairman, Reunion Industries Inc.
(a designer and manufacturer of fabricated
and machined parts and products)

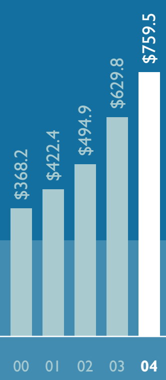
Candace L. Littell [8]
President, Littell Group, Inc. (a consulting
firm specializing in healthcare reimbursement
strategy for medical technology companies)

Mylle H. Mangum [10]
Chief Executive Officer, IBT (a company that
creates retail locations for financial institutions)

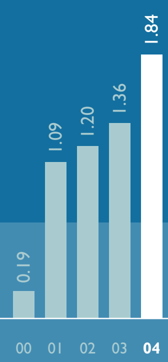
Sean C. McDonald [11]
President and Chief Executive Officer,
Precision Therapeutics (a biomedical company
providing comprehensive, personalized
cancer management information)

John C. Miles II [14]
Chairman, DENTSPLY International (the world's
largest manufacturer of dental products)

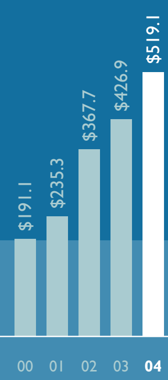
Craig B. Reynolds [16]
Executive Vice President and
Chief Operating Officer



Net Sales
dollars in millions



Diluted Earnings per Share
dollars



Shareholders' Equity
dollars in millions

Financial Highlights

(amounts in thousands except per share data)

Year Ended June 30	2004	2003	2002	2001	2000
Net Sales	$ 759,550	$ 629,817	$ 494,919	$ 422,438	$ 368,184
Net Income	65,020 [1]	46,581	38,417	33,571	5,752
Diluted Earnings per Share	1.84 [1]	1.36 [2]	1.20 [3]	1.09	0.19 [4]
Diluted Shares Outstanding	35,309	34,344	32,008	30,886	30,004
Working Capital	301,032	212,787	198,966	171,985	155,095
Long-Term Obligations	26,897	16,513	59,502	80,055	108,095
Total Assets	711,139	582,196	550,911	367,295	352,577
Shareholders' Equity	519,053	426,869	367,720	235,268	191,106

[1] Includes the impact of restructuring and acquisition-related expenses related primarily to the restructuring of operations at the Wallingford, Connecticut manufacturing facility. These costs reduced net income by $10,942 ($0.19 per share) in fiscal year 2004.

[2] Includes the impact of restructuring and acquisition-related expenses related to the integration of Novametrix Medical Systems Inc. ("Novametrix") and restructuring of operations at the Kennesaw, Georgia and Wallingford, Connecticut manufacturing facilities, and other acquisition-related costs. These costs reduced net income by $11,286 ($0.32 per share) in fiscal year 2003.

[3] Includes the impact of a non-recurring purchase accounting adjustment related to reversing acquisition date inventory fair market value adjustments as inventory was sold subsequent to the acquisition of Novametrix, restructuring and acquisition-related expenses related to the integration of Novametrix, and an asset impairment charge. These costs reduced net income by $3,853 ($0.12 per share) in fiscal year 2002.

[4] Includes the impact of restructuring expenses related to the Company's July 1999 restructuring, a specific addition to the allowance for doubtful accounts due to a customer bankruptcy, and a one-time reduction in income tax expense. These costs reduced net income by $19,611 ($0.66 per share) in fiscal year 2000.

2004 Financial Review

Management's Discussion and Analysis of Results of Operations and Financial Condition

> RESULTS OF OPERATIONS

Fiscal Year Ended June 30, 2004, Compared to Fiscal Year Ended June 30, 2003:

Year Ended June 30	2004	2003	Percent Increase (Decrease)
Net sales	$759,549,845	$629,817,447	21%
Cost of goods sold	356,625,125	310,385,469	15%
	402,924,720	319,431,978	26%
General and administrative expenses (excluding acquisition earn-out expenses)	100,231,728	83,730,678	20%
Acquisition earn-out expenses	8,533,000	2,036,000	
Sales, marketing and commission expenses	147,739,729	116,299,669	27%
Research and development expenses	29,477,699	24,047,538	23%
Contribution to foundation	2,844,475	–	
Restructuring and acquisition-related expenses	10,942,352	17,788,719	(38%)
Other (income) expense, net	(2,078,417)	639,520	
	297,690,566	244,542,124	22%
Income before income taxes	**105,234,154**	**74,889,854**	**41%**
Income taxes	40,214,309	28,308,365	42%
NET INCOME	**$ 65,019,845**	**$ 46,581,489**	**40%**
Diluted earnings per share	**$ 1.84**	**$ 1.36**	**36%**
Diluted shares outstanding	35,309,350	34,344,003	

Net Sales: Net sales for the year ended June 30, 2004 were $759,550,000, representing a 21% increase over sales of $629,817,000 recorded for the year ended June 30, 2003. The Company's sales growth occurred across all product groups, summarized as follows:

	Year Ended June 30					
	2004		2003		Dollar Increase	Percent Increase
Domestic homecare products	$471,645,000	62%	$388,166,000	62%	$ 83,479,000	22%
Domestic hospital products	95,876,000	13%	79,776,000	13%	16,100,000	20%
International products	192,029,000	25%	161,875,000	25%	30,154,000	19%
Total	$759,550,000	100%	$629,817,000	100%	$129,733,000	21%

Domestic homecare sales for the year ended June 30, 2004 were driven primarily by growth in sales of sleep apnea therapy devices, masks and accessories (the Company's largest product line), which represented $66,880,000 of the increase over the prior year, or 26% growth. The Company's growth in sleep apnea therapy products was achieved through the success of recent product introductions and the Company's overall product breadth in sleep apnea therapy, strength of the sales force and the success of customer programs, and growth of the domestic sleep apnea therapy market (estimated to be approximately 15% to 20%). Sales of developmental infant care products and oxygen products constituted the majority of the remainder of the sales increase over the prior year.

Sales of domestic hospital products for the year ended June 30, 2004 were driven primarily by growth in sales of hospital ventilators and accessories, which represented $13,439,000 of the increase over the prior year, or 30% growth, evidencing the growing acceptance of the Company's approach to the management of ventilated patients in the hospital setting.

The Company's international growth included sales from both homecare and hospital products; the most significant increases came from homecare sleep apnea therapy devices and accessories ($19,901,000 of the increase over the prior year) and hospital ventilation systems and accessories ($6,395,000 of the increase over the prior year). The primarily geographic drivers for these revenue gains were Europe and the Far East/Asia Pacific, where the Company has made significant investments in sales force and marketing programs. In Japan, in particular, the Company has experienced continued growth from the May 2002 acquisition of Fuji. Changes in foreign currency exchange rates contributed $6,808,000 of revenues during the year ended June 30, 2004 (less than 1% of net sales) compared to the prior year. Included in net sales for the year ended June 30, 2003 are revenues of approximately $10,000,000 resulting from the demand for ventilation products associated with the treatment of SARS (severe acute respiratory syndrome) during the fourth quarter of fiscal year 2003 that did not recur during the year ended June 30, 2004.

Gross Profit: The Company's gross profit was 53% of net sales for the year ended June 30, 2004 compared to 51% of net sales for the year ended June 30, 2003. The increase in gross profit percentage was primarily due to higher revenue, product sales mix (between sales of electro-mechanical devices and masks and accessories, and between domestic and international sales), material cost reductions (achieved through the Company's successful negotiations with suppliers and product design changes), and reduced indirect manufacturing costs resulting from the Company's restructuring of operations at its Kennesaw, Georgia manufacturing facility. See Note P to the Consolidated Financial Statements for additional information regarding the restructuring.

General and Administrative Expenses (excluding acquisition earn-out expenses): General and administrative expenses were $100,232,000 (13% of net sales) for the year ended June 30, 2004 as compared to $83,731,000 (13% of net sales) for the year ended June 30, 2003. The increase for the year ended June 30, 2004 was due primarily to higher employee compensation, consistent with the growth of the Company's business and the strong financial performance achieved during the year, increases in product warranty costs, and an impairment loss on a specific investment that experienced an other than temporary decline in fair market value (as of June 30, 2004 the total remaining carrying value of the investment is $1,254,000).

Acquisition Earn-out Expenses: During the years ended June 30, 2004 and 2003, the Company incurred acquisition earn-out expenses related to the Company's May 2002 Fuji acquisition of $8,533,000 (1% of net sales) and $2,036,000 (less than 1% of net sales), respectively. The increase in this expense compared to the prior year was due to Fuji's positive financial performance during the year ended June 30, 2004. See Note Q to the Consolidated Financial Statements for additional information regarding the Fuji acquisition.

Sales, Marketing and Commission Expenses: Sales, marketing and commission expenses were $147,740,000 (19% of net sales) for the year ended June 30, 2004 as compared to $116,300,000 (18% of net sales) for the year ended June 30, 2003. The increase was driven by higher variable sales force compensation consistent with the increase in sales levels from the prior year. Also during the year ended June 30, 2004, the Company made significant investments in sales and marketing programs and sales force, especially in international markets.

Research and Development Expenses: Research and development expenses were $29,478,000 (4% of net sales) for the year ended June 30, 2004 as compared to $24,047,000 (4% of net sales) for the year ended June 30, 2003. The increases were due to the Company's continuing commitment to research, development and new product introductions. New product introductions in 2004 included the REMstar Plus with C-Flex CPAP device; BiPAP Pro II with Bi-Flex and BiPAP Plus bi-level obstructive sleep apnea therapy unit; new masks, including the Comfort Lite, ComfortGel, Contour Deluxe, Performa Classic, and Performa Trak; product software enhancements to the Encore Pro Patient Data Management Software, Sleep Link, and Esprit ventilation system; the NICO version 5.0 cardiac output monitoring system; and the Millennium M10 Concentrator. In addition, the PLV-C portable volume ventilator and neonatal CPAP received 510(k) approval from the FDA during the year ended June 30, 2004, and are scheduled for market release during the 2005 fiscal year. Significant product development efforts are ongoing, and new product launches in many of the Company's major product lines are scheduled for the next six to eighteen months. Additional development work and clinical trials are being conducted in certain product areas and markets outside the Company's current core products and patient groups.

Contribution to Foundation: During the year ended June 30, 2004, the Company made contributions totaling $2,844,000 (less than 1% of net sales) to the newly established Respironics Sleep and Respiratory Research Foundation (the "Foundation"). The Foundation was formed for scientific, educational, and charitable purposes and will be used to promote awareness of and research into the medical consequences of sleep and respiratory problems.

Restructuring and Acquisition-Related Expenses: During the year ended June 30, 2004, the Company incurred restructuring and acquisition-related expenses of $10,942,000, related primarily to the restructuring of operations at the Wallingford, Connecticut manufacturing facility. See Notes P and Q to the Consolidated Financial Statements for additional information regarding restructuring and acquisition-related expenses.

During the year ended June 30, 2003, the Company incurred restructuring and acquisition-related expenses of $18,144,000, related to the integration of Novametrix and restructuring of operations at the Kennesaw, Georgia and Wallingford, Connecticut manufacturing facilities, and other acquisition-related costs. Of this amount, $17,789,000 is included in restructuring and acquisition-related expenses, and $355,000 is included in cost of goods sold in the Consolidated Statement of Operations for the year ended June 30, 2003.

Other (Income) Expense, Net: Other (income) expense, net was $(2,078,000) for the year ended June 30, 2004 as compared to $640,000 for the year ended June 30, 2003. The change was due to realized and unrealized foreign currency exchange gains primarily caused by the strengthening Japanese Yen and Euro against the U.S. Dollar during the year ended June 30, 2004, offset by recognized losses on designated cash flow hedges that are more fully described in Note I to the Consolidated Financial Statements. Also contributing to the change were lower interest expenses resulting from a reduction in the amount of outstanding borrowings under the Company's Revolving Credit Agreement and larger cash balances, offset by higher amounts of long-term equipment financing (and related interest expense) at Fuji.

Income Taxes: The Company's effective income tax rate was approximately 38% for the years ended June 30, 2004 and 2003. The income tax benefits associated with various ongoing tax planning strategies, primarily in the state and international tax areas, were offset by higher acquisition earn-out expenses, which are not deductible for income tax purposes.

The Company has not provided a valuation allowance for deferred income tax assets because it has determined that it is more likely than not that such assets can be realized, at a minimum, through carrybacks to prior years in which taxable income was generated.

Net Income: As a result of the factors described above, the Company's net income was $65,020,000 (9% of net sales) or $1.84 per diluted share for the year ended June 30, 2004 as compared to net income of $46,581,000 (7% of net sales) or $1.36 per diluted share for the year ended June 30, 2003. The restructuring and acquisition-related expenses described above constituted a reduction of $0.19 and $0.32 per diluted share on an after-tax basis, respectively, for the years ended June 30, 2004 and 2003.

Fiscal Year Ended June 30, 2003, Compared to Fiscal Year Ended June 30, 2002:

Year Ended June 30	2003	2002	Percent Increase
Net sales	$629,817,447	$494,918,654	27%
Cost of goods sold	310,385,469	260,795,012	19%
	319,431,978	234,123,642	36%
General and administrative expenses (excluding acquisition earn-out expenses)	83,730,678	60,718,793	38%
Acquisition earn-out expenses	2,036,000	–	
Sales, marketing and commission expenses	116,299,669	86,188,885	35%
Research and development expenses	24,047,538	17,317,462	39%
Restructuring and acquisition-related expenses	17,788,719	4,294,120	
Other (income) expense, net	639,520	1,568,165	
	244,542,124	170,087,425	44%
Income before income taxes	**74,889,854**	**64,036,217**	**17%**
Income taxes	28,308,365	25,619,349	10%
NET INCOME	**$ 46,581,489**	**$ 38,416,868**	**21%**
Diluted earnings per share	$ 1.36	$ 1.20	13%
Diluted shares outstanding	34,344,003	32,008,359	

Net Sales: Net sales for the year ended June 30, 2003 were $629,817,000, representing a 27% increase over sales of $494,919,000 recorded for the year ended June 30, 2002. The Company's sales growth occurred across all product groups, summarized as follows:

	Year Ended June 30					
	2003		2002		Dollar Increase	Percent Increase
Domestic homecare products	$388,166,000	62%	$339,339,000	69%	$ 49,177,000	14%
Domestic hospital products	79,776,000	13%	57,468,000	11%	21,959,000	38%
International products	161,875,000	25%	98,112,000	20%	63,762,000	65%
Total	$629,817,000	100%	$494,919,000	100%	$134,898,000	27%

Domestic homecare sales for the year ended June 30, 2003 were driven primarily by growth in sales of sleep apnea therapy devices, masks and accessories (the Company's largest product line), and sales of developmental infant care products acquired from Novametrix, partially offset by decreases in sales of the Company's home oxygen products.

Sales of domestic hospital products for the year ended June 30, 2003 were driven primarily by growth in sales of hospital ventilators and accessories and sales of cardiorespiratory monitoring devices acquired from Novametrix.

The Company's growth internationally included sales from both homecare and hospital products, with the most significant increases coming from homecare sleep apnea therapy devices, incremental revenues resulting from the Novametrix and Fuji acquisitions, and demand for ventilation products associated with the treatment of SARS during the fourth quarter of fiscal year 2003.

In total, sales for the year ended June 30, 2003 included approximately $35,400,000 of incremental net sales from the products of Novametrix, a leading cardiorespiratory monitoring company that was acquired by the Company during the fourth quarter of fiscal year 2002. Sales for the year ended June 30, 2003 also included approximately $28,500,000 of incremental sales for Fuji, a provider of respiratory products and services in which the Company obtained a majority interest in the fourth quarter of fiscal year 2002. The Company's results of operations include the results of both companies since the acquisition dates. For additional information regarding Novametrix and Fuji, see Note Q to the Consolidated Financial Statements.

Excluding the acquired revenues, sales for the year ended June 30, 2003 represented a 14% increase over sales recorded for the year ended June 30, 2002.

Gross Profit: The Company's gross profit was 51% of net sales for the year ended June 30, 2003 compared to 47% of net sales for the year ended June 30, 2002. The increase in gross profit percentage was primarily due to higher revenue, product sales mix, cost reductions, and the impact of higher gross margins from acquired entities.

General and Administrative Expenses (excluding acquisition earn-out expenses): General and administrative expenses were $83,731,000 (13% of net sales) for the year ended June 30, 2003 as compared to $60,719,000 (12% of net sales) for the year ended June 30, 2002. The increase for the year ended June 30, 2003 was due primarily to general and administrative expenses for the Company's two acquired companies, Novametrix and Fuji. The remaining increases in general and administrative expenses resulted from higher spending in a variety of areas, including employee compensation and information systems, consistent with the growth of the Company's business, and increases in business insurance and product warranty costs. General and administrative expenses for the year ended June 30, 2002 included goodwill amortization expense in the amount of $3,507,000. As of July 1, 2002 the Company ceased amortizing goodwill due to the adoption of Financial Accounting Standards Board Statement No. 142, "Goodwill and Other Intangible Assets." For additional information, see Note A to the Consolidated Financial Statements.

Sales, Marketing and Commission Expenses: Sales, marketing and commission expenses were $116,300,000 (18% of net sales) for the year ended June 30, 2003 as compared to $86,189,000 (17% of net sales) for the year ended June 30, 2002. The majority of the increase was due to sales and marketing expenses for the Company's two acquired companies, Novametrix and Fuji, and increases in sales levels from the year ago periods. The remainder of the increase was due to increased investments in the Company's core sales and marketing programs.

Research and Development Expenses: Research and development expenses were $24,047,000 (4% of net sales) for the year ended June 30, 2003 as compared to $17,317,000 (3% of net sales) for the year ended June 30, 2002. A significant amount of the increase in absolute dollars was due to research and development expenses incurred at Novametrix. The remaining increases were due to the Company's continuing commitment to research, development, and new product introductions. In the 2003 fiscal year, several new products were introduced, such as the REMstar Pro with C-Flex, REMstar Plus True Compliance, and REMstar Lite CPAP devices; the Synchrony Avaps bi-level obstructive sleep apnea therapy unit; new masks, including the ComfortFull and Image 3 Deluxe; product software enhancements including the Encore Pro communication link, Sleep Link with modem, and enhancements to the Esprit ventilation system; and the Stardust II diagnostic unit.

Restructuring and Acquisition-Related Expenses: During the year ended June 30, 2003, the Company incurred restructuring and acquisition-related expenses of $18,144,000, related to the integration of Novametrix and restructuring of operations at the Kennesaw, Georgia and Wallingford, Connecticut manufacturing facilities, and other acquisition-related costs. Of this amount, $17,789,000 is included in restructuring and acquisition-related expenses, and $355,000 is included in cost of goods sold in the Consolidated Statement of Operations for the year ended June 30, 2003. See Notes P and Q to the Consolidated Financial Statements for additional information regarding restructuring and acquisition-related expenses.

As part of the acquisition of Novametrix, during the fourth quarter of fiscal year 2002, the Company incurred a non-recurring purchase accounting adjustment in cost of goods sold of $1,653,000 related to reversing acquisition date inventory fair market value adjustments as inventory was sold subsequent to the acquisition. Also during the fourth quarter of fiscal year 2002, the Company incurred restructuring and acquisition-related expenses of $2,288,000 related to the Novametrix acquisition, primarily for the elimination and centralization of certain duplicate back-office functions. During the fourth quarter of fiscal year 2002, the Company also incurred an impairment charge of $2,006,000, representing the write-off of intangible assets, inventory, and fixed assets related to an oxygen monitoring technology development project that was cancelled based in part on the results of a review of that technology by engineers at Novametrix.

Other (Income) Expense, Net: Other (income) expense was $640,000 for the year ended June 30, 2003 as compared to $1,568,000 for the year ended June 30, 2002. The decrease was due to reductions in the amount of outstanding borrowings and interest rates under the Company's Revolving Credit Agreement.

Income Taxes: The Company's effective income tax rate was approximately 38% for the year ended June 30, 2003 as compared to 40% for the year ended June 30, 2002. This reduction was due primarily to the impact of eliminating non-deductible goodwill amortization effective July 1, 2002, and the income tax benefits associated with various ongoing tax planning strategies.

The Company has not provided a valuation allowance for deferred income tax assets because it has determined that it is more likely than not that such assets can be realized, at a minimum, through carrybacks to prior years in which taxable income was generated.

Net Income: As a result of the factors described above, the Company's net income was $46,581,000 (7% of net sales) or $1.36 per diluted share for the year ended June 30, 2003 as compared to net income of $38,417,000 (8% of net sales) or $1.20 per diluted share for the year ended June 30, 2002. The restructuring and acquisition-related expenses described above constituted a reduction of $0.32 and $0.12 per diluted share on an after-tax basis, respectively, for the years ended June 30, 2003 and 2002.

> FINANCIAL CONDITION, LIQUIDITY AND CAPITAL RESOURCES

The Company had working capital of $301,032,000 at June 30, 2004 and $212,787,000 at June 30, 2003. Net cash provided by operating activities for the year ended June 30, 2004 was $140,937,000, compared to $124,293,000 for the year ended June 30, 2003 and $87,484,000 for the year ended June 30, 2002. The increase in cash provided by operating activities for all years was primarily due to an increase in net income before the impact of depreciation and amortization expense. Fiscal year 2003 cash flow was also positively impacted by increases in accrued expenses in excess of the increases in these balances in the prior year.

Net cash used by investing activities was $62,386,000, $47,444,000, and $44,556,000 for fiscal years 2004, 2003, and 2002, respectively. The majority of the cash used by investing activities for all periods represented capital expenditures, including the purchase of leasehold improvements, production equipment, computer hardware and software, telecommunications and office equipment; in the years ended June 30, 2004 and 2003, the production of equipment leased to customers; and in the 2002 fiscal year, the purchase of the Company's corporate headquarters facility. In the current fiscal year, cash used by investing activities also includes the Company's acquisition of Caradyne, which is more fully described in Note Q to the Consolidated Financial Statements. In the year ended June 30, 2003, cash used by investing activities also included transaction costs related to the Novametrix acquisition and the Company's acquisition of the BiliChek Non-invasive Bilirubin Analyzer product line from SpectRx, Inc. that are more fully described in Note Q to the Consolidated Financial Statements. In fiscal year 2002, cash used by investing activities also included the purchase price paid for Novametrix and Fuji, net of cash acquired. In addition, cash used by investing activities in all three fiscal years included the acquisition of intangible assets and additional purchase price paid for previously acquired businesses pursuant to the terms of the acquisition agreements. The funding for investing activities in all periods was provided by positive cash flow from operating activities and accumulated cash and cash equivalents.

Net cash provided by financing activities of $17,995,000 during the year ended June 30, 2004 consists primarily of proceeds from the issuance of common stock under the Company's stock option plans. During the years ended June 30, 2003 and 2002, cash used by financing activities of $43,284,000 and $7,914,000, respectively, consists of repayments under the Company's various long-term obligations, partially offset by proceeds from the issuance of common stock under the Company's stock option plans. The Company repaid $10,494,000 on its long-term obligations during the year ended June 30, 2004, including the remaining $10,000,000 balance that was outstanding under the Revolving Credit Facility in August 2003. Offsetting these repayments, the Company received $10,419,000 in proceeds from equipment financing at its Fuji subsidiary in Japan. Debt pay-downs, net of borrowings, were $53,527,000 and $16,667,000 for the 2003 and 2002 fiscal years, respectively.

On August 1, 2002 one of the Company's significant homecare dealer customers announced that it filed a voluntary petition to reorganize under Chapter 11 of the U.S. Bankruptcy Code in order to restructure its bank debt. On July 1, 2003, the U.S. Bankruptcy Court approved the customer's reorganization plan. The confirmed plan allowed the customer to continue its business operations uninterrupted, and all creditors and vendors were to be paid 100% of all amounts they were owed, either immediately or over time with interest. The Company received all scheduled installment payments on its pre-petition balance during the year ended June 30, 2004 based on the reorganization plan.

The Company believes that its sources of funding – consisting of projected positive cash flow from operating activities, the availability of additional funds under its revolving credit facility (totaling approximately $149,006,000 at June 30, 2004), and its accumulated cash and cash equivalents – will be sufficient to meet its current and presently anticipated short-term and long-term needs for operating activities (including payments against restructuring accruals), investing activities, and financing activities (primarily consisting of scheduled payments on long-term debt).

> CONTRACTUAL OBLIGATIONS AND OFF-BALANCE SHEET ARRANGEMENTS

The Company has contractual financial obligations and commercial financial commitments consisting primarily of long-term debt, capital lease obligations, and non-cancelable operating leases. See Notes G and J to the Consolidated Financial Statements for additional information about these obligations and commitments. The composition and nature of these obligations and commitments have not changed materially since June 30, 2003.

On August 19, 2002, the Company entered into a Revolving Credit Agreement with a group of banks under which a total of $150,000,000 is available through August 2005 with terms and financial covenants similar to those contained in the Company's prior credit facility. The new Revolving Credit Agreement is unsecured and contains certain financial covenants with which the Company must comply. The Company is currently in compliance with these covenants. The interest rate on the revolving credit facility is based on a spread over the London Interbank Borrowing Rate ("LIBOR"). As of June 30, 2004, no amounts are outstanding under the Revolving Credit Facility.

Subsequent to June 30, 2004, the Company amended the Revolving Credit Agreement to extend the maturity date through August 31, 2009. The Revolving Credit Facility has substantially the same terms after the amendment (but generally more favorable and flexible to the Company, including potentially lower interest rate spreads over LIBOR and greater flexibility to make investments).

The following table summarizes significant contractual obligations and commercial commitments of the Company as of June 30, 2004:

Contractual Obligations and Commercial Commitments

		Payments Due by Period			
Contractual Obligations	Total	Up to 1 Year	1-3 Years	3-5 Years	Over 5 Years
Long-term debt	$ 3,685,000	$ 486,000	$ 3,199,000	$ –	$ –
Capital lease obligations	33,748,000	10,051,000	18,013,000	5,684,000	–
Operating leases	33,397,000	8,892,000	11,968,000	7,169,000	5,368,000
Amounts payable to selling parties of previously acquired businesses	14,047,000	1,338,000	12,709,000	–	–
TOTAL CONTRACTUAL OBLIGATIONS	$ 84,877,000	$ 20,767,000	$ 45,889,000	$ 12,853,000	$ 5,368,000

		Amount of Commitment Expiration Per Period			
Other Commercial Commitments	Total Amounts Committed	Up to 1 Year	1-3 Years	3-5 Years	Over 5 Years
Letters of credit	$ 1,198,000	$ 1,198,000	$ –	$ –	$ –

In addition to the amounts payable to the selling parties of previously acquired businesses that are set forth in the contractual obligations and commercial commitments table above, the Company may be obligated to make additional future payments under earn-out provisions pertaining to the acquisitions of Fuji, BiliChek, and Caradyne for which the total amount of the obligations will not be known until the occurrence of future events. The amounts reflected in the contractual obligations and commercial commitments table above include the future payments that have accrued as of June 30, 2004 in accordance with the earn-out provisions and the Company's other fixed obligations under the acquisition agreements. See Note Q to the Consolidated Financial Statements for additional information about these obligations.

The contractual obligations and commercial commitments table above does not reflect obligations under purchase orders that arise in the ordinary course of business and that are typically fulfilled within ninety days. In addition to ordinary course purchase orders, the Company enters into supply agreements and distribution agreements in the ordinary course of business, some of which make the purchase of minimum quantities of products a condition to exclusivity or to obtaining or retaining more favorable pricing. Since failure to purchase the minimum amounts under these agreements generally does not result in a breach of contract, but only to an option on the part of the vendor to terminate the Company's exclusivity or increase the product prices the Company pays to the vendor, they are not included in the contractual obligations and commercial commitments table above.

In connection with customer leasing programs, the Company uses independent leasing companies for the purpose of providing financing to certain customers for the purchase of the Company's products. The Company is contingently liable, in the event of a customer default, to the leasing companies within certain limits for unpaid installment receivables initiated by or transferred to the leasing companies. The transfers of certain of these installment receivables meets the criteria of Financial Accounting Standards Board ("FASB") Statement No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities," and therefore are not recorded on the Company's financial statements. The total exposure for unpaid installment receivables meeting these criteria and not recorded on the Company's financial statements was approximately $13,950,000 at June 30, 2004 as compared to $12,147,000 at June 30, 2003. The estimated fair value of the Company's contingent recourse guarantee is $581,000 and $252,000 as of June 30, 2004 and 2003, respectively. Approximately 8% of the Company's net sales were made under these financing arrangements during the year ended June 30, 2004, of which a portion was made with recourse. The Company is not dependent on these off-balance sheet arrangements.

The remainder of these installment receivables (consisting of installment receivables acquired as part of the Novametrix acquisition) do not meet the criteria of FASB No. 140 and therefore are recorded as collateralized borrowing arrangements. Accordingly, at June 30, 2004 and 2003, the Company has included $1,049,000 of receivables sold with recourse in prepaid expenses and other current assets, and has recorded offsetting amounts at those dates in accrued expenses and other current liabilities. Effective March 31, 2003, the Company entered into an agreement with the third party financing company that is counter-party to these receivables. The terms of the agreement place a cap on the Company's recourse obligation at $1,049,000.

> QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK

The Company is exposed to market risk from changes in interest rates and foreign exchange rates.

Interest Rates: The Company's primary interest rate risk relates to its long-term debt obligations. At June 30, 2004, the Company had total long-term obligations, including the current portion of those obligations, of $37,433,000. Of that amount, $37,233,000 was in fixed rate obligations and $200,000 was in variable rate obligations. As of June 30, 2004, a 10% change in interest rates would not have a material impact on the Company's results of operations. The Company has no interest rate hedging agreements.

Foreign Exchange Rates: The Company's functional currency is the U.S. Dollar, and a substantial majority of the Company's sales, expenses, and cash flows are transacted in U.S. Dollars. The Company also conducts business in various foreign currencies, primarily the Japanese Yen, the Euro, the Hong Kong Dollar and the Chinese Yuan. As part of the Company's risk management strategy, the Company put in place a hedging program beginning on July 1, 2003 under which the Company enters into foreign currency option and forward contracts to hedge a portion of cash flows denominated in Japanese Yen. These contracts are entered into to reduce the risk that the Company's earnings and cash flows, resulting from certain forecasted and recognized currency transactions, will be affected by changes in foreign currency exchange rates. See Note I to the Consolidated Financial Statements for additional information about the Company's foreign currency hedging activities.

For the year ended June 30, 2004, sales denominated in currencies other than the U.S. Dollar totaled $103,092,000, or approximately 14% of net sales. An adverse change of 10% in exchange rates would have resulted in a decrease in sales of $9,372,000 for the year ended June 30, 2004 had no currency hedging contracts been put in place. Foreign currency gains included in the determination of the Company's net income, including amounts related to designated cash flow hedges, were $3,311,000 for the year ended June 30, 2004.

Inflation: Inflation has not had a significant effect on the Company's business during the periods discussed.

> NEW ACCOUNTING PRONOUNCEMENTS

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities" in an effort to expand upon and strengthen existing accounting guidance that addresses when a company should include in its financial statements the assets, liabilities and activities of variable interest entities, including special-purpose entities or off-balance sheet structures. The consolidation requirements of FIN No. 46 apply immediately to variable interest entities created after January 31, 2003. As amended, the consolidation requirements apply to older entities in the first fiscal year or interim period ending after March 15, 2004. Certain of the disclosure requirements apply in all financial statements issued after January 31, 2003, regardless of when the variable interest entity was established. The impact of adopting FIN No. 46 was not material to the Company's financial position and results of operations.

In April 2003, the FASB issued Statement of Financial Accounting Standards No. 149, "Amendment of Statement 133 on Derivative Instruments and Hedging Activities." This statement amends and clarifies financial accounting and reporting for derivative instruments, including certain derivative instruments embedded in other contracts and for hedging activities under FASB No. 133. This statement is effective for contracts entered into or modified after June 30, 2003 and for hedging relationships designated after June 30, 2003. The impact of adopting FASB No. 149 was not material to the Company's financial position and results of operations.

In May 2003, the FASB issued Statement of Financial Accounting Standards No. 150, "Accounting for Certain Financial Instruments with Characteristics of both Liabilities and Equity." This statement affects the issuer's accounting for three types of freestanding financial statements: mandatorily redeemable shares, put and forward purchase contracts that require the issuer to buy back some of its shares in exchange for cash or other assets, and certain obligations that can be settled in shares. This statement is effective for all financial instruments entered into or modified after May 31, 2003, and otherwise effective at the beginning of the first interim period beginning after June 15, 2003. The impact of adopting FASB No. 150 was not material to the Company's financial position and results of operations.

In December 2003, the SEC published Staff Accounting Bulletin (SAB) No. 104, "Revenue Recognition." This SAB updates portions of the SEC staff's interpretive guidance provided in SAB 101 and included in Topic 13 of the Codification of Staff Accounting Bulletins. SAB 104 deletes interpretive material no longer necessary, and conforms the interpretive material retained, because of pronouncements issued by the FASB's EITF on various revenue recognition topics, including EITF 00-21, "Revenue Arrangements with Multiple Deliverables." SAB No. 104 also incorporates into the SAB Codification certain sections of the SEC staff's "Revenue Recognition in Financial statements – Frequently Asked Questions and Answers." SAB No. 104 does not have a material impact on the Company's financial position and results of operations since the Company's revenue recognition practices previously conformed to the interpretations codified by SAB No. 104.

> CRITICAL ACCOUNTING POLICIES

The Company's Consolidated Financial Statements are prepared in accordance with accounting principles generally accepted in the United States, which require the Company to make estimates and assumptions that may affect the reported financial condition and results of operations should actual results differ. The Company bases its estimates and assumptions on the best available information and believes them to be reasonable under the circumstances. The Company believes that of its significant accounting policies, the following may involve a higher degree of judgment and complexity.

Revenue Recognition: The Company's revenues are recognized when title to product passes to the customer, which generally occurs upon shipment to a customer location and, in the case of rental revenue and long-term service contracts, is recognized ratably over the period the product is rented or service is performed. The Company's revenue transactions are sometimes made pursuant to standard terms and conditions included in distributor agreements and customer contracts. These contracts generally include price lists that apply to specified products shipped to customers during the terms of their agreement. These contracts also generally include rights of return provisions that only permit customers to return sold product in the case of defective product or order entry, shipping, or similar error made by the Company. Product returns, which are recorded as a reduction of net sales and cost of sales, are generally insignificant in relation to net sales. The Company accrues for estimated sales returns and allowances based on historical trends, adjusted for specific product programs and individual transactions where appropriate. The Company does not offer variable sales prices for subsequent events; all prices are fixed when customers' orders are received. Certain customers' and group purchasing organizations' contracts provide customers with price rebates based on their level of purchases from the Company. Rebates are accrued by the Company as a reduction in net sales as they are earned by customers. Price discounts that may be awarded to customers for payment of invoices within specified periods are recorded as reductions to net sales at the time of payment and are generally insignificant in relation to net sales. As part of the Company's sales process, pricing discounts may be provided for large orders to support sales initiatives, including new product introductions. In the Company's domestic sales activities, a number of independent manufacturers' representatives are used to sell the Company's products. These independent representatives are paid a direct commission on sales made to customers in their respective territories and are an integral component of the Company's domestic sales force. The Company does not ship or sell its products to these representatives, and therefore does not recognize any revenue from transactions with these independent representatives. The Securities and Exchange Commission's Staff Accounting Bulletin ("SAB") Nos. 101 and 104, "Revenue Recognition," provides guidance on the application of generally accepted accounting principles to selected revenue recognition issues. The Company has concluded that its revenue recognition policy is appropriate and in accordance with generally accepted accounting principles and SAB Nos. 101 and 104.

Allowance for Uncollectible Accounts Receivable: Accounts receivable are reduced by an allowance for amounts that may become uncollectible in the future. Provisions to increase the allowance for uncollectible accounts receivable are recorded as a component of general and administrative expenses in the Company's Consolidated Statements of Operations during the fiscal years ended June 30, 2004, 2003, and 2002. Substantially all of the Company's receivables are due from healthcare product providers, distributors, and hospitals. The Company's customers are located throughout the United States and around the world. A significant portion of products sold to providers, distributors, and hospitals, both foreign and domestic, is ultimately funded through government reimbursement programs or through private insurance programs. As a consequence, changes in these programs can have an adverse impact on distributor and hospital liquidity and profitability. In addition, because a concentration of market share exists in the homecare product industry in the United States among national and large regional providers, the Company experiences a comparable concentration of credit risk with these customers. The estimated allowance for uncollectible amounts is based primarily on the Company's evaluation of the payment pattern, financial condition, cash flows, and credit history of its customers as well as current industry and economic conditions. Adverse changes in these factors may impair the ability of the Company's customers to make payments; as a consequence, additional allowances for uncollectible accounts receivable may be required. The Company is also contingently liable, within certain limits, in the event of a customer default on unpaid installment receivables initiated by or transferred to several independent leasing companies in connection with customer leasing programs. The Company monitors the collection status of these installment receivables and provides amounts necessary for estimated losses in the allowance for doubtful accounts.

Inventories and Related Allowance for Obsolete and Excess Inventory: Inventories are valued at the lower of cost or market value and have been reduced by an allowance for excess and obsolete inventories. Provisions to increase the allowance for obsolete and excess inventory are recorded as a component of cost of goods sold in the Company's Consolidated Statements of Operations during the fiscal years ended June 30, 2004, 2003, and 2002. The estimated allowance is based on the Company's review of inventories on hand compared to historical and estimated future usage and sales. If it is determined that inventory on hand is in excess of estimated future usage and sales because of changes in competitive conditions, new product introductions, product obsolescence, changes in customer demand, or other reasons, additional allowances for obsolete and excess inventory may need to be provided. The establishment of these additional allowances may have an adverse impact on earnings, depending on the extent and amount of inventory affected.

Intangible Assets: Intangible and product technology related assets are amortized to expense over their useful lives. These useful lives are based on the Company's estimates of the period that the assets will generate positive cash flows. Intangible assets are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of such assets may not be recoverable. If such carrying amounts are determined to be unrecoverable because of changes in technology, extended delays in obtaining regulatory approval, competition, significant changes in the Company's strategic business objectives, utilization of the asset, or other reasons, the carrying amounts would be written down to their fair market values. These adjustments may have an adverse impact on earnings, depending on the significance of the carrying amounts and the extent of the required adjustments.

Contingencies: As a normal part of its business operations, the Company incurs liabilities that may be difficult to quantify precisely, such as future warranty obligations, potential liabilities relating to legal or regulatory matters, and tax exposures. The Company follows the requirements of Statement of Financial Accounting Standards No. 5, "Accounting for Contingencies," which dictate when a charge to income should be taken to accrue for a loss contingency. These requirements necessitate the application of judgment regarding the likelihood and amount of the liability.

> CAUTIONARY STATEMENT FOR PURPOSES OF THE "SAFE HARBOR" PROVISIONS OF THE PRIVATE SECURITIES REFORM ACT OF 1995

The statements contained in this Annual Report, including those contained in "Management's Discussion and Analysis of Results of Operations and Financial Condition," along with statements in reports filed with the Securities and Exchange Commission, external documents and oral presentations which are not historical are "forward-looking statements" within the meaning of Section 27A of the Securities Act of 1933, as amended, and Section 21B of the Securities Exchange Act of 1934, as amended. These forward-looking statements represent the Company's present expectations or beliefs concerning future events. The Company cautions that such statements are qualified by important factors that could cause actual results to differ materially from the expected results included in the forward-looking statements. Those factors include, but are not limited to, the following: developments in the healthcare industry; the success of the Company's marketing, sales and promotion programs; future sales and acceptance of the Company's products and programs; the timing and success of new product introductions; new product development; anticipated cost savings; FDA and other regulatory requirements and enforcement actions; future results from acquisitions; growth rates in foreign markets; regulations and other factors affecting operations and sales outside the United States (including potential future effects of the change in sovereignty of Hong Kong); foreign currency fluctuations; customer consolidation and concentration; increasing price competition and other competitive factors in the sale of products; interest rate fluctuations; expiration of intellectual property rights; intellectual property and related litigation; other litigation; future levels of earnings and revenues; and third party reimbursement.

Consolidated Balance Sheets

At June 30	2004	2003
> ASSETS		
Current Assets		
Cash and cash equivalents	$192,445,866	$ 95,900,114
Trade accounts receivable	140,633,793	128,126,999
Inventories	85,539,100	83,986,140
Prepaid expenses and other current assets	8,621,042	7,890,194
Deferred income tax benefits	25,373,010	24,111,838
Total current assets	452,612,811	340,015,285
Property, Plant and Equipment		
Land	3,214,679	2,868,310
Buildings	17,258,260	16,888,036
Production and office equipment	245,978,933	218,839,491
Leasehold improvements	7,989,040	7,630,418
	274,440,912	246,226,255
Less allowances for depreciation and amortization	163,383,655	147,546,282
	111,057,257	98,679,973
Other Assets	37,466,117	34,591,712
Goodwill	110,003,068	108,909,352
TOTAL ASSETS	$711,139,253	**$582,196,322**
> LIABILITIES AND SHAREHOLDERS' EQUITY		
Current Liabilities		
Accounts payable	$ 52,789,363	$ 40,531,413
Accrued expenses and other current liabilities	88,255,213	68,389,269
Current portion of long-term obligations	10,536,473	18,307,876
Total current liabilities	151,581,049	127,228,558
Long-Term Obligations	26,896,842	16,513,243
Other Non-Current Liabilities	13,608,331	11,585,202
Shareholders' Equity		
Common Stock, $.01 par value; authorized 100,000,000 shares; issued 38,478,511 shares at June 30, 2004 and 37,505,700 shares at June 30, 2003; outstanding 34,983,269 shares at June 30, 2004 and 33,957,221 at June 30, 2003	384,785	375,057
Additional capital	249,594,545	226,884,681
Accumulated other comprehensive income (loss)	458,621	(3,557,902)
Retained earnings	310,051,723	245,031,878
Treasury stock	(41,436,643)	(41,864,395)
Total shareholders' equity	519,053,031	426,869,319
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	$711,139,253	**$582,196,322**

See notes to consolidated financial statements.

Consolidated Statements of Operations

Year Ended June 30	2004	2003	2002
Net sales	$759,549,845	$629,817,447	$494,918,654
Cost of goods sold	356,625,125	310,385,469	260,795,012
	402,924,720	319,431,978	234,123,642
General and administrative expenses (excluding acquisition earn-out expenses)	100,231,728	83,730,678	60,718,793
Acquisition earn-out expenses	8,533,000	2,036,000	–
Sales, marketing and commission expenses	147,739,729	116,299,669	86,188,885
Research and development expenses	29,477,699	24,047,538	17,317,462
Contribution to foundation	2,844,475	–	–
Restructuring and acquisition-related expenses	10,942,352	17,788,719	4,294,120
Other (income) expense, net	(2,078,417)	639,520	1,568,165
	297,690,566	244,542,124	170,087,425
Income before income taxes	**105,234,154**	**74,889,854**	**64,036,217**
Income taxes	40,214,309	28,308,365	25,619,349
NET INCOME	**$ 65,019,845**	**$ 46,581,489**	**$ 38,416,868**
Basic earnings per share	**$ 1.89**	**$ 1.39**	**$ 1.24**
Basic shares outstanding	34,376,771	33,585,173	31,079,282
Diluted earnings per share	**$ 1.84**	**$ 1.36**	**$ 1.20**
Diluted shares outstanding	35,309,350	34,344,003	32,008,359

See notes to consolidated financial statements.

Consolidated Statements of Shareholders' Equity

	Common Stock		Additional
	Shares	Amount	Capital
BALANCE AT JUNE 30, 2001	**34,013,785**	**$340,138**	**$121,720,289**
Shares sold pursuant to stock option and purchase plans	472,617	4,726	8,377,899
Net acquisition and use of treasury stock	–	–	–
Income tax benefit from exercise of stock options	–	–	2,766,453
Stock issued for business acquired	2,399,393	23,994	80,972,382
Comprehensive income:			
Net income for the year ended June 30, 2002	–	–	–
Foreign currency translation adjustments	–	–	–
Total comprehensive income	–	–	–
BALANCE AT JUNE 30, 2002	**36,885,795**	**368,858**	**213,837,023**
Shares sold pursuant to stock option and purchase plans	619,905	6,199	9,883,283
Income tax benefit from exercise of stock options	–	–	3,164,375
Comprehensive income:			
Net income for the year ended June 30, 2003	–	–	–
Foreign currency translation adjustments	–	–	–
Total comprehensive income (loss)	–	–	–
BALANCE AT JUNE 30, 2003	**37,505,700**	**375,057**	**226,884,681**
Shares sold pursuant to stock option and purchase plans	972,811	9,728	17,632,372
Income tax benefit from exercise of stock options	–	–	5,077,492
Comprehensive income:			
Net income for the year ended June 30, 2004	–	–	–
Foreign currency translation adjustments	–	–	–
Unrealized losses on derivatives qualifying as hedges	–	–	–
Total comprehensive income (loss)	–	–	–
BALANCE AT JUNE 30, 2004	38,478,511	$384,785	$249,594,545

See notes to consolidated financial statements.

Accumulated Comprehensive Income (Loss)	Retained Earnings	Treasury Stock Shares	Treasury Stock Amount	Total
$(4,237,433)	**$160,033,521**	**3,639,169**	**$(42,588,367)**	**$235,268,148**
–	–	–	–	8,382,625
–	–	(46,444)	370,377	370,377
–	–	–	–	2,766,453
–	–	–	–	80,996,376
–	38,416,868	–	–	38,416,868
1,519,220	–	–	–	1,519,220
1,519,220	38,416,868	–	–	39,936,088
(2,718,213)	**198,450,389**	**3,592,725**	**(42,217,990)**	**367,720,067**
–	–	(44,246)	353,595	10,243,077
–	–	–	–	3,164,375
–	46,581,489	–	–	46,581,489
(839,689)	–	–	–	(839,689)
(839,689)	46,581,489	–	–	45,741,800
(3,557,902)	**245,031,878**	**3,548,479**	**(41,864,395)**	**426,869,319**
–	–	(53,237)	427,752	18,069,852
–	–	–	–	5,077,492
–	65,019,845	–	–	65,019,845
4,232,150	–	–	–	4,232,150
(215,627)	–	–	–	(215,627)
4,016,523	65,019,845	–	–	69,036,368
$ 458,621	$310,051,723	3,495,242	$(41,436,643)	$519,053,031

Consolidated Statements of Cash Flows

Year Ended June 30	2004	2003	2002
Operating Activities			
Net income	$ 65,019,845	$ 46,581,489	$ 38,416,868
Adjustments to reconcile net income to net cash provided by operating activities:			
Depreciation	38,456,432	39,268,196	28,578,753
Amortization	6,099,888	7,684,000	5,653,328
Income tax benefit from exercise of stock options	5,077,492	3,164,375	2,766,453
Provision for asset write-offs	–	–	2,005,722
Provision for bad debts	5,163,819	4,626,000	3,275,000
Acquisition earn-out expenses, net of amounts paid	6,308,236	2,036,000	–
Provision (benefit) for deferred income taxes	(757,030)	(1,216,000)	3,251,495
Changes in operating assets and liabilities:			
Accounts receivable	(16,993,791)	(11,471,926)	(7,905,452)
Inventories and other current assets	(2,154,529)	3,271,232	9,052,239
Accounts payable and other current liabilities	30,984,491	31,662,346	5,728,845
Other assets and liabilities	3,731,677	(1,312,256)	(3,339,608)
Net cash provided by operating activities	**140,936,530**	**124,293,456**	**87,483,643**
Investing Activities			
Purchase of property, plant and equipment	(51,391,196)	(42,075,069)	(39,829,553)
Proceeds from sale of property, plant and equipment	–	3,835,000	–
Acquisition of intangible assets	(1,441,962)	(2,120,380)	–
Acquisition of business, net of cash acquired	(9,552,589)	(7,083,607)	(4,726,200)
Net cash used by investing activities	**(62,385,747)**	**(47,444,056)**	**(44,555,753)**
Financing Activities			
Proceeds from long-term obligations	10,418,891	–	4,531,085
Payment on long-term obligations	(10,493,774)	(53,527,047)	(21,198,203)
Issuance of common stock	18,069,852	10,243,077	8,753,002
Net cash provided (used) by financing activities	**17,994,969**	**(43,283,970)**	**(7,914,116)**
Increase in cash and cash equivalents	96,545,752	33,565,430	35,013,774
Cash and cash equivalents at beginning of period	95,900,114	62,334,684	27,320,910
CASH AND CASH EQUIVALENTS AT END OF PERIOD	**$192,445,866**	**$ 95,900,114**	**$ 62,334,684**

See notes to consolidated financial statements.

Notes to Consolidated Financial Statements

> NOTE A: SIGNIFICANT ACCOUNTING POLICIES

Basis of Consolidation: The Consolidated Financial Statements include the accounts of Respironics, Inc. (the "Company") and its wholly and majority owned subsidiaries. All significant inter-company accounts and transactions have been eliminated in consolidation.

Cash and Cash Equivalents: The Company considers all highly liquid investments with maturities of 30 days or less when purchased to be cash and cash equivalents. Cash and cash equivalents are stated at cost, which approximates market.

Inventories: Inventories are valued at the lower of cost (determined on a first-in, first-out moving average basis) or market.

Property, Plant and Equipment: Property, plant and equipment is recorded on the basis of cost. Costs incurred to purchase or develop software for internal use, including upgrades and enhancements, are capitalized during the software application development stage in accordance with Statement of Position No. 98-1, "Accounting for the Costs of Computer Software Developed or Obtained for Internal Use." Depreciation is computed using the straight-line method based upon the estimated useful lives of the respective assets, which are 30 years for buildings and range from two to five years for production and office equipment. Leasehold improvements are depreciated over their lease terms, or useful lives if shorter. Amortization of assets under capital leases is included in depreciation expense. Maintenance and repairs are charged to expense as incurred.

Capitalized Software Production Costs: Software development costs have been capitalized when technological feasibility was established and are being amortized to the cost of goods sold over the estimated economic lives (generally three to seven years) of the products that include such software. Total net capitalized software production costs were $11,025,000 and $9,950,000 at June 30, 2004 and 2003, respectively. During the fiscal years ended June 30, 2004, 2003, and 2002, the Company recorded $1,786,000, $1,785,000, and $428,000, respectively, of amortization expense related to capitalized software production costs.

Goodwill and Intangible Assets: Goodwill is the cost in excess of the fair value of (tangible and intangible) net assets of businesses acquired. In June 2001, the Financial Accounting Standards Board ("FASB") issued Statement No. 141, "Business Combinations," and Statement No. 142, "Goodwill and Other Intangible Assets," effective for fiscal years beginning after December 15, 2001. Under these rules, goodwill and intangible assets deemed to have indefinite lives are no longer amortized but are subject to annual impairment tests in accordance with the Statements. Other intangible assets continue to be amortized over their useful lives. The Company applied the provisions of FASB No. 141 to account for business combinations consummated after July 1, 2001, including the acquisitions of Novametrix, Fuji, BiliChek, and Caradyne discussed in Note Q to these Consolidated Financial Statements.

Effective July 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," under which goodwill and intangible assets deemed to have indefinite lives are no longer amortized but are subject to annual impairment tests. The Company performed the required transitional impairment test with the adoption of FASB No. 142 and has determined that no impairment exists as of July 1, 2002. The Company has also performed its annual impairment tests as of December 31, 2003 and 2002 and determined that no impairment exists. The Company will update this annual test as of December 31 in future years, and on an interim basis as determined necessary in accordance with FASB No. 142.

Effective July 1, 2002, the Company adopted Statement of Financial Accounting Standards No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets." FASB No. 144 superseded FASB No. 121, "Accounting for the Impairment of Long-Lived Assets and for Long-Lived Assets to be Disposed Of"; however, it retained the fundamental provisions of that statement related to the recognition and measurement of the impairment of long-lived assets to be held and used. The Company evaluates the carrying value of long-lived assets, including intangible assets, to be held and used when events and circumstances indicate that the carrying amount of an asset may not be recovered. Such evaluation considers projected future operating results, trends, and other circumstances. If factors indicated long-lived assets could be impaired, the Company would use an estimate of the related undiscounted future cash flows over the remaining life of the long-lived asset in measuring whether the asset is recoverable. If such an analysis indicated that impairment had occurred, the Company would adjust the book value of the long-lived asset to fair value. Assets to be disposed of are reported at the lower of the carrying amount or fair value, less costs to sell.

Product Warranties: Estimated future warranty costs related to certain products are charged to operations in the period in which the related revenue is recognized. See Note F to these Consolidated Financial Statements for additional information about the Company's product warranties.

Comprehensive Income: Comprehensive income consists of net income, foreign currency translation adjustments, and unrealized gains (losses) on derivatives qualifying as hedges, and is presented in the Consolidated Statements of Shareholders' Equity. The Company does not provide for U.S. income taxes on foreign currency translation adjustments since it does not provide for such taxes on the undistributed earnings of foreign subsidiaries.

Foreign Currency Translation: Foreign currency assets and liabilities are translated into U.S. dollars at the rate of exchange existing at the statement date or historical rates depending upon the nature of the account. Income and expense amounts are translated at the average of the monthly exchange rates. Adjustments resulting from these translations are credited or charged directly to accumulated comprehensive income (loss). Gains and losses resulting from foreign currency transactions, denominated in other than the functional currency of the entity, are credited or charged directly to income.

Stock Options: Stock options are granted to certain employees and certain members of the Company's Board of Directors at the fair market value of the Company's stock on the date of the grant. Proceeds from the exercise of common stock options are credited to shareholders' equity at the date the options are exercised. There are no charges or credits to income with respect to stock options. The Company follows the requirements of Accounting Principles Board ("APB") Opinion No. 25, "Accounting for Stock Issued to Employees," as amended, in accounting for stock-based compensation.

Earnings per Share: Basic earnings per share are based on the weighted-average number of shares actually outstanding. Diluted earnings per share are based on the weighted-average number of shares actually outstanding and dilutive potential shares, such as dilutive stock options and warrants which are determined using the treasury stock method.

Revenue Recognition: Revenue is recognized from sales when title to product passes to the customer, which generally occurs upon shipment to a customer location. Rental and service revenues are recognized ratably over the period the product is rented or service is performed.

Shipping and Handling Costs: Shipping and handling costs are expensed as incurred and are included in cost of goods sold.

Advertising Costs: Advertising costs are expensed during the period in which they are incurred. Total advertising expenses for the fiscal years ended June 30, 2004, 2003, and 2002 were $2,345,000, $1,516,000, and $965,000, respectively.

Income Taxes: Provisions for income taxes include deferred taxes resulting from temporary differences in income for financial and tax purposes using the liability method. Such temporary differences result primarily from differences in the carrying value of assets and liabilities.

The Company does not provide for federal income taxes on the undistributed earnings of its foreign subsidiaries (other than dividends which are taxed currently) because such earnings are reinvested and, in the opinion of management, will continue to be reinvested indefinitely.

Use of Estimates: The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the amounts reported in the financial statements and accompanying notes. Actual results could differ from those estimates.

Changes in Presentation of Comparative Financial Statements: Certain amounts in the June 30, 2003 and 2002 financial statements were reclassified to conform with the presentation in the current period.

> NOTE B: CASH EQUIVALENTS

Cash equivalents consist primarily of money market accounts and certificates of deposit issued by large commercial banks located in the United States, Hong Kong, Japan, Germany, France and Ireland.

> NOTE C: ACCOUNTS RECEIVABLE

Trade accounts receivable in the Consolidated Balance Sheets is net of allowances for doubtful accounts of $14,871,000 as of June 30, 2004 and $12,495,000 as of June 30, 2003.

> NOTE D: INVENTORIES

Inventories consisted of the following, net of allowances for obsolete and excess inventories of $13,200,000 and $10,682,000 at June 30, 2004 and 2003, respectively.

June 30	2004	2003
Raw materials	$ 24,439,000	$ 18,091,000
Work-in-process	9,221,000	8,727,000
Finished goods	51,879,000	57,168,000
	$ 85,539,000	$ 83,986,000

> NOTE E: GOODWILL AND INTANGIBLE ASSETS

Changes in the carrying amount of goodwill for the year ended June 30, 2004 were as follows:

Balance at June 30, 2003	$108,909,000
Goodwill on businesses acquired	–
Additional purchase price to former owners of businesses previously acquired	1,094,000
BALANCE AT JUNE 30, 2004	$110,003,000

Net income and earnings per share excluding goodwill amortization expense are as follows:

Year Ended	June 30, 2004	June 30, 2003	June 30, 2002
Net income as reported	$ 65,020,000	$ 46,581,000	$ 38,417,000
Goodwill amortization expense (net of tax)	–	–	3,302,000
NET INCOME EXCLUDING GOODWILL AMORTIZATION EXPENSE	$ 65,020,000	$ 46,581,000	$ 41,719,000
Basic earnings per share:			
Net income as reported	$ 1.89	$ 1.39	$ 1.24
Goodwill amortization expense (net of tax)	–	–	0.11
BASIC EARNINGS PER SHARE EXCLUDING GOODWILL AMORTIZATION EXPENSE	$ 1.89	$ 1.39	$ 1.35
Diluted earnings per share:			
Net income as reported	$ 1.84	$ 1.36	$ 1.20
Goodwill amortization expense (net of tax)	–	–	0.10
DILUTED EARNINGS PER SHARE EXCLUDING GOODWILL AMORTIZATION EXPENSE	$ 1.84	$ 1.36	$ 1.30

The Company's intangible assets are comprised of product-related intellectual property acquired from third parties, the appraised fair market values of product-related intellectual property and employee contracts obtained through business acquisitions (including the acquisitions disclosed in Note Q), and patent registration costs. Intangible assets at June 30 are summarized below, net of accumulated amortization of $8,266,000 and $10,328,000 as of June 30, 2004 and 2003, respectively.

	2004	2003
Product-related intellectual property	$ 27,101,000	$ 26,143,000
Patent registration costs	2,461,000	1,827,000
Employee contracts	159,000	304,000
TOTAL INTANGIBLE ASSETS	$ 29,721,000	$ 28,274,000

Intangible asset amortization is computed using the straight-line method based upon the estimated useful lives of the respective assets, which range from one to sixteen years.

Intangible asset amortization expense was $4,037,000, $5,899,000, and $2,716,000 during the years ended June 30, 2004, 2003, and 2002, respectively. The estimated aggregate intangible asset amortization expenses for the next five years are as follows:

2005	$ 4,107,000
2006	3,832,000
2007	3,465,000
2008	2,415,000
2009	2,165,000

> NOTE F: ACCRUED EXPENSES AND OTHER CURRENT LIABILITIES

Accrued expenses and other current liabilities at June 30 consist of the following:

	2004	2003
Promotional programs and royalties	$ 7,025,000	$ 5,589,000
Product warranties	8,011,000	4,848,000
Restructuring and acquisition-related	7,064,000	9,997,000
Recourse obligations	1,049,000	1,049,000
Deferred service revenues	3,891,000	3,097,000
Compensation and related	31,105,000	22,229,000
Taxes	15,731,000	12,545,000
Contribution to foundation	1,250,000	–
Other	13,129,000	9,035,000
TOTAL	$ 88,255,000	$ 68,389,000

Generally, the Company's standard product warranties are for a one- or two-year period (based on the specific product sold and country in which the Company does business) that covers both parts and labor. The Company provides for the estimated cost of product warranties at the time revenue is recognized. The Company's product warranty liability reflects management's best estimate of probable liability under its product warranties. Management estimates the liability based on the Company's stated warranty policies, which project the estimated warranty obligation on a product-by-product basis based on the historical frequency of claims, the cost to replace or repair its products under warranty, and the number of products under warranty based on the warranty terms and historical units shipped. The warranty liability also includes estimated warranty costs that may arise from specific product issues. The Company periodically assesses the adequacy of its recorded warranty liabilities and adjusts the amounts as necessary. The Company also engages in the sale of extended warranties for which revenue is deferred and recognized over the warranty terms, which are generally between two and eight years. Changes in the liability for product warranty and deferred service revenues associated with these service programs for the year ended June 30, 2004 are as follows:

Product Warranties

Balance as of June 30, 2003	$ 4,848,000
Warranty accruals during the year	9,761,000
Service costs incurred during the year	(6,598,000)
BALANCE AT JUNE 30, 2004	$ 8,011,000

Deferred Service Revenues

Balance as of June 30, 2003	$ 3,097,000
Revenues deferred during the year	1,776,000
Amounts recorded as revenue during the year	(982,000)
BALANCE AT JUNE 30, 2004	$ 3,891,000

> NOTE G: LONG-TERM OBLIGATIONS

Long-term obligations consist of the following:

June 30	2004	2003
Revolving Credit Agreement, due in August 2009 including interest at a floating rate (2.09% at June 30, 2003)	$ –	$ 10,000,000
Bank Debt with varying maturities (final maturity in May 2007) including interest rates ranging from 0.8% to 1.7%	2,768,000	2,582,000
Capital Lease Obligations, payable in monthly installments with varying completion dates through April 2009 including interest rates ranging from 1.5% to 2.8%	33,748,000	20,833,000
Other	917,000	1,406,000
	37,433,000	34,821,000
Less current portion	10,536,000	18,308,000
	$ 26,897,000	**$ 16,513,000**

On August 19, 2002, the Company entered into a Revolving Credit Agreement with a group of banks under which a total of $150,000,000 is available through August 2009 (as amended and as more fully described below), replacing a $125,000,000 Commercial Bank Credit Agreement that had similar terms. The new Revolving Credit Agreement is unsecured and contains certain financial covenants with which the Company must comply, including those relating to current ratio, ratio of total liabilities to tangible net worth, minimum tangible net worth, leverage, and interest coverage (as these terms are defined in the Revolving Credit Agreement). The Company is currently in compliance with these covenants. The interest rate on the revolving credit facility is based on a spread over the London Interbank Borrowing Rate ("LIBOR"). The Commercial Bank Revolving Credit Agreement includes a commitment fee, currently equal to 0.20%, on the unused portion of the facility. In August 2003, the Company paid the remaining $10,000,000 of borrowings that were outstanding under the Revolving Credit Agreement. This amount is classified with the current portion of long-term obligations in the Consolidated Balance Sheet as of June 30, 2003. No amounts are outstanding under the Revolving Credit Facility as of June 30, 2004.

Subsequent to June 30, 2004, the Company amended the Revolving Credit Agreement to extend the maturity date through August 31, 2009. The Revolving Credit Facility has substantially the same terms after the amendment (but generally more favorable and flexible to the Company, including potentially lower interest rate spreads over LIBOR and greater flexibility to make investments).

The Capital Lease Obligations are primarily for equipment rented to outside customers by the Company's Fuji subsidiary. Other long-term obligations in the above table include an Economic Development Revenue Bond, Industrial Development Authority Loans, and a Redevelopment Authority Loan that are secured by mortgages on the Company's manufacturing facility in Murrysville, Pennsylvania. Proceeds from the bonds and the loans were used to finance the construction and expansion of some of the Company's facilities.

Scheduled maturities of long-term obligations for the next five years are as follows:

	Maturities of Long-Term Debt
2005	$ 10,536,000
2006	12,317,000
2007	8,895,000
2008	4,482,000
2009	1,203,000
Thereafter	–
TOTAL	$ 37,433,000

Interest paid was $1,745,000, $2,607,000, and $2,983,000 for the years ended June 30, 2004, 2003, and 2002, respectively.

> NOTE H: FAIR VALUE OF FINANCIAL INSTRUMENTS

The following methods and assumptions were used to estimate the fair value of financial instruments:

Cash and Cash Equivalents: The carrying amount approximates fair value because of the short maturity of those investments.

Long-Term Obligations: The fair values of long-term debt obligations are established from the market values of similar issues. The carrying amounts of the Company's obligations approximate their fair values at June 30, 2004 and 2003.

Foreign Currency Exchange Derivative Contracts: Foreign currency exchange derivative contracts are recorded in the Consolidated Balance Sheets at fair value. As of June 30, 2004, foreign currency options contracts with a fair value of $70,000 are recorded with prepaid expenses and other current assets, and foreign currency forward contracts with a fair value of $161,000 are recorded with accrued expenses and other current liabilities.

> NOTE I: DERIVATIVE INSTRUMENTS AND HEDGING ACTIVITIES

The Company's functional currency is the U.S. Dollar, and a substantial majority of the Company's sales, expenses, and cash flows are transacted in U.S. Dollars. The Company also does business in various foreign currencies, primarily the Japanese Yen, the Euro, the Hong Kong Dollar and the Chinese Yuan. As part of the Company's risk management strategy, management put in place a hedging program beginning on July 1, 2003 under which the Company enters into foreign currency option and forward contracts to hedge a portion of cash flows denominated in Japanese Yen.

During the year ended June 30, 2004, the Company acquired foreign currency option and forward contracts to hedge a portion of forecasted cash flows and recognized foreign currency transactions denominated in Japanese Yen. These foreign currency option and forward contracts have notional amounts of approximately $36,745,000 as of June 30, 2004 and mature at various dates through September 28, 2005. As of June 30, 2004, foreign currency options contracts with a fair value of $70,000 are recorded with prepaid expenses and other current assets, and foreign currency forward contracts with a fair value of $161,000 are recorded with accrued expenses and other current liabilities.

These contracts are entered into to reduce the risk that the Company's earnings and cash flows, resulting from certain forecasted and recognized currency transactions, will be affected by changes in foreign currency exchange rates. However, the Company may be impacted by changes in foreign exchange rates related to the portion of the forecasted transactions that is not hedged. The success of the hedging program depends, in part, on forecasts of the Company's transactions in Japanese Yen. Hedges are placed for periods consistent with identified exposures, but not longer than the end of the year for which the Company has substantially completed its annual business plan.

The Company may experience unanticipated foreign currency exchange gains or losses to the extent that there are timing differences between forecasted and actual activity during periods of currency volatility. However, since the critical terms of contracts designated as cash flow hedges are the same as the underlying forecasted and recognized currency transactions, changes in fair value of the contracts should be highly effective in offsetting the present value of changes in the expected cash flows from the forecasted and recognized currency transactions. The ineffective portion of changes in the fair value of contracts designated as hedges, if any, is recognized immediately in earnings. The Company did not recognize material gains or losses resulting from either hedge ineffectiveness or changes in forecasted transactions during the year ended June 30, 2004.

The effective portion of any changes in the fair value of the derivative instruments, designated as cash flow hedges, is recorded in other comprehensive income (loss) ("OCI") until the hedged forecasted transaction occurs or the recognized currency transaction affects earnings. Once the forecasted transaction occurs or the recognized currency transaction affects earnings, the effective portion of any related gains or losses on the cash flow hedge is reclassified from OCI to earnings. In the event the hedged forecasted transaction does not occur, or it becomes probable that it will not occur, the ineffective portion of any gain or loss on the related cash flow hedge would be reclassified from OCI to earnings at that time.

During the year ended June 30, 2004, the Company recorded realized and unrealized foreign currency gains of approximately $3,311,000, net of net losses related to designated cash flow hedges. These amounts are classified with other (income) expense, net in the Consolidated Statements of Operations. As of June 30, 2004, a loss of $216,000 was included in OCI. This loss is expected to be charged to earnings during the year ended June 30, 2005 as the hedged transactions occur, and it is expected that the loss will be more than offset by currency gains on the items being hedged.

> NOTE J: OPERATING LEASES

The Company leases its service centers, its central distribution center, and certain of its offices, warehouses and manufacturing facilities in the United States and also leases its offices, warehouses and manufacturing facilities in the Far East and in Europe. Certain of these leases contain renewal options and rent escalation clauses.

The minimum rentals due under noncancelable leases with recurring terms of one year or more as of June 30, 2004 are as follows:

Year Ended June 30	Amount
2005	$ 8,892,000
2006	6,665,000
2007	5,303,000
2008	4,121,000
2009	3,048,000
Thereafter	5,368,000
TOTAL	$ 33,397,000

Total rent expense for the years ended June 30, 2004, 2003, and 2002, was $8,338,000, $8,320,000, and $5,255,000, respectively.

> NOTE K: CONTINGENCIES

Litigation: On March 5, 2004, the Company filed a lawsuit against Invacare Corporation ("Invacare") in the United States District Court for the Western District of Pennsylvania alleging that Invacare's manufacture, sale and marketing of a new CPAP device infringes one or more of eleven U.S. patents of Respironics. In its complaint, the Company has sought preliminary and permanent injunctive relief, damages, and an award of three times actual damages because of Invacare's willful infringement of Respironics' patents. In its answer to the complaint, Invacare has denied the infringement allegations of the complaint. The parties currently are engaged in discovery.

On August 10, 2004, Invacare filed a lawsuit against the Company in the United States District Court in the Northern District of Ohio alleging that the Company has engaged in monopolization, restraint of trade, and unfair competition in the sale and distribution of sleep apnea products. The lawsuit's claims include allegations that the Company's actions and alleged market power have foreclosed competitors from alleged markets and have created markets where there has not been competitive pricing or availability for competitive product offerings. In the lawsuit, Invacare seeks damages in an unspecified amount and to treble such damages pursuant to the antitrust laws, as well as attorney's fees and punitive damages. Invacare also seeks injunctive relief as to certain marketing practices. The Company is vigorously defending itself in this suit.

The Company is, as a normal part of its business operations, a party to other legal proceedings in addition to those described above. Legal counsel has been retained for each proceeding, and none of these proceedings is expected to have a material adverse impact on the Company's results of operations or financial condition.

Contingent Obligations Under Recourse Provisions: In connection with customer leasing programs, the Company uses independent leasing companies to provide financing to certain customers for the purchase of the Company's products. The Company is contingently liable, in the event of a customer default, to the leasing companies within certain limits for unpaid installment receivables initiated by or transferred to the leasing companies. The transfers of certain of these installment receivables meets the criteria of Statement of Financial Accounting Standards No. 140, "Accounting for Transfers and Servicing of Financial Assets and Extinguishment of Liabilities," and therefore are not recorded on the Company's financial statements. The total exposure for unpaid installment receivables meeting these criteria and not recorded on the Company's financial statements was approximately $13,950,000 at June 30, 2004 as compared to $12,147,000 at June 30, 2003. The estimated fair value of the Company's contingent recourse guarantee is $581,000 and $252,000 as of June 30, 2004 and 2003, respectively. Approximately 8% of the Company's net sales were made under these financing arrangements during the year ended June 30, 2004, of which a portion was made with recourse. The Company is not dependent on these off-balance sheet arrangements.

The remainder of these installment receivables (consisting of installment receivables acquired as part of the Novametrix acquisition) do not meet the criteria of FASB No. 140 and therefore are recorded as collateralized borrowing arrangements. Accordingly, at June 30, 2004 and 2003, the Company has included $1,049,000 of receivables sold with recourse in prepaid expenses and other current assets, and has recorded offsetting amounts at those dates in accrued expenses and other current liabilities. Effective March 31, 2003, the Company entered into an agreement with the third party financing company that is counter-party to these receivables. The terms of the agreement place a cap on the Company's recourse obligation at $1,049,000.

> NOTE L: INCOME TAXES

Income before income taxes consisted of the following:

Year Ended June 30	2004	2003	2002
United States	$ 86,647,000	$ 53,223,000	$ 55,870,000
Foreign	18,587,000	21,667,000	8,166,000
TOTAL	**$105,234,000**	**$ 74,890,000**	**$ 64,036,000**

Income taxes (benefit) consisted of:

Year Ended June 30	2004	2003	2002
Current:			
Federal	$ 29,451,000	$ 19,683,000	$ 16,874,000
Foreign	7,713,000	6,680,000	1,527,000
State	3,807,000	3,678,000	3,876,000
	40,971,000	**30,041,000**	**22,277,000**
Deferred:			
Federal	(1,550,000)	(851,000)	2,922,000
Foreign	1,208,000	(517,000)	90,000
State	(415,000)	(365,000)	330,000
	(757,000)	(1,733,000)	3,342,000
TOTAL INCOME TAXES	$ 40,214,000	$ 28,308,000	$ 25,619,000

The difference between the statutory U.S. federal income tax rate and the Company's effective income tax rate is explained below:

Year Ended June 30	2004	2003	2002
Statutory federal income tax rate	35%	35%	35%
Increases (decreases):			
State taxes, net of federal benefit	2	3	4
Foreign taxes	2	(2)	(2)
Tax credits	–	(2)	(1)
Non-deductible expenses	(1)	3	3
Other items, net	–	1	1
EFFECTIVE INCOME TAX RATE	38%	38%	40%

Deferred income tax assets consist of the following:

June 30	2004	2003
Allowance for bad debts	$ 5,623,000	$ 4,907,000
Depreciation and amortization	(2,701,000)	(386,000)
Inventory reserves	3,600,000	2,612,000
Inter-company profit in inventories	5,203,000	3,398,000
Product warranty reserves	3,819,000	2,629,000
Restructuring and acquisition-related liabilities and reserves	3,348,000	4,654,000
Net operating loss carryforward, limited by Section 382	–	713,000
Business credits carryforward, limited by Section 383	644,000	712,000
Foreign net operating loss carryforward	451,000	920,000
Other	5,386,000	3,953,000
TOTAL	$ 25,373,000	$ 24,112,000

Undistributed earnings of the foreign subsidiaries on which no U.S. income tax has been provided amounted to $38,717,000 at June 30, 2004.

Income taxes paid were $36,621,000, $13,710,000, and $19,170,000 for the years ended June 30, 2004, 2003, and 2002, respectively.

On April 12, 2002, the Company acquired Novametrix Medical Systems Inc., which had a federal and state net operating loss for the period ending April 12, 2002 of approximately $5,800,000 that was scheduled to expire by 2022. As of June 30, 2004, the full amount of this operating loss was utilized. Additionally, Novametrix had unused research tax credits of approximately $475,000 which expire in varying amounts through 2013, and alternative minimum tax credits of $237,000 which do not have expiration dates. As a result of the ownership change, the utilization of the net operating loss and the credit carryforwards is limited each year by Internal Revenue Code Sections 382 and 383, respectively. The Company expects to fully utilize the net operating loss and credit carryforwards prior to their expiration.

> NOTE M: STOCK OPTION AND PURCHASE PLANS

The Company has in place the 1992 Stock Incentive Plan (the "1992 Plan") and the 2000 Stock Incentive Plan (the "2000 Plan"), which provide options to eligible employees, and in the case of the 2000 Plan, to eligible consultants and non-employee directors (as described below in the case of non-employee directors), to purchase common stock for a period up to ten years at option prices not less than fair market value at the time of the grant. Under the 1992 Plan, options become exercisable no sooner than six months from the date of the grant at rates that vary depending on the plan and are subject to possible acceleration in certain circumstances. Under the 2000 Plan, options become exercisable at such times or upon the occurrence of such events as determined by the Committee administering the 2000 Plan. Under the 1992 and 2000 Plans, options may include cash payment rights, and restricted shares of the Company's common stock may also be awarded. The 1992 Plan had a total of 3,000,000 shares approved for issuance, including 1,000,000 shares that were approved by the Company's shareholders when the 1992 Plan was adopted and an additional 2,000,000 shares that were approved by the Company's shareholders in November 1998. The 1992 Plan expired on September 28, 2002, and no new options will be granted under the 1992 Plan in the future. The 2000 Plan has a total of 3,276,000 shares approved for issuance, including 1,400,000 shares that were approved by the Company's shareholders when the 2000 Plan was adopted and an additional 1,876,000 shares that were approved by shareholders in November 2003.

Options are also granted under the 2000 Plan to members of the Company's Board of Directors who are not employees of the Company. Each non-employee director receives an option to purchase 6,500 shares (increased from 5,100 shares by an amendment to the 2000 Plan on May 23, 2003) on the third business day following the Company's annual meeting of shareholders. Additionally, each non-employee director is granted an option to purchase 10,000 shares on the first business day following the date they become a member of the Board of Directors. These grants will continue until options for all the shares available under the 2000 Plan have been granted. Such options are granted at fair market value on the date of grant. For options granted to non-employee directors, 25% of the shares are exercisable one year after the date of the grant, 25% are exercisable two years after the date of grant, and the remaining 50% are exercisable three years after the date of grant. All options granted under the 2000 Plan expire ten years after the date of grant.

Each of the Company's equity compensation plans was approved by security holders.

Healthdyne had in place, prior to its merger with the Company, four stock option plans: the 1993 Stock Option Plan; the 1993 Non-Employee Director Stock Option Plan; the 1995 Stock Option Plan II; and the 1996 Stock Option Plan. At the date of the merger, the outstanding Healthdyne options were converted into a total of 1,360,061 options to purchase Respironics common stock. Under the terms of the Healthdyne plans, all such options became immediately exercisable at the date of the merger and the plans terminated as to new grants. All future stock option grants will be made from Respironics stock option plans.

Novametrix had in place, prior to its merger with the Company, five stock option plans: the 1990 Stock Option Plan; the 1994 Stock Option Plan; the 1997 Long Term Incentive Plan; the 1999 Incentive Plan; and the 2000 Long Term Incentive Plan. Novametrix also had in place certain stock option agreements, separately from its plans, with its President and its Chief Operating Officer. At the date of the merger, the outstanding Novametrix options were converted into a total of 416,125 options to purchase Respironics common stock. Under the terms of the Novametrix plans and agreements, all such options become immediately exercisable in connection with the merger and the plans terminated as to new grants. All future stock option grants will be made from Respironics stock option plans.

The following table summarizes stock option activity:

Year Ended June 30	2004	2003	2002
Option Shares			
Outstanding at beginning of period	2,700,000	2,764,000	2,174,000
Granted	797,000	711,000	1,181,000
Exercised	(908,000)	(654,000)	(486,000)
Canceled	(38,000)	(121,000)	(105,000)
Outstanding at end of period	**2,551,000**	**2,700,000**	**2,764,000**
Weighted-average exercise price	**$ 31.62**	**$ 24.02**	**$ 19.69**
Exercisable at end of period	**1,035,000**	**1,231,000**	**1,105,000**
Shares available for future grant	**1,917,000**	**830,000**	**1,649,000**
Price range of granted options	**$40.68-$54.55**	**$29.32-$36.26**	**$10.33-$33.75**

The range of grant and exercise prices above for the 2002 fiscal year includes the post-conversion option prices for options granted by Novametrix prior to its merger with the Company.

The following table summarizes information about stock options outstanding at June 30, 2004:

Range of Exercise Prices	Number of Options Outstanding	Weighted-Average Remaining Contractual Life
$ 5-$10	188,000	5.17 years
$11-$20	332,000	5.42 years
$21-$30	135,000	4.70 years
$31-$40	1,098,000	7.70 years
$41-$45	647,000	9.16 years
$46-$55	151,000	9.54 years

The per share weighted-average fair value of stock options granted during 2004, 2003, and 2002, was $14.38, $14.25, and $17.35, respectively, on the date of grant using the Black-Scholes option-pricing model with the following assumptions:

	2004	2003	2002
Expected volatility	32.1%	45.2%	53.0%
Expected dividend yield	none	none	none
Risk-free interest rate	3.7%	2.3%	4.1%
Expected life of stock options	5	5	5

The Company applies APB Opinion No. 25, as amended, in accounting for its stock option plans, and accordingly, no compensation cost has been recognized for its stock options in the financial statements. Had the Company determined compensation cost based on the fair value at the grant date for its stock options under Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation," the Company's net earnings and related per share amounts would have been reduced to the pro forma amounts indicated below:

Year Ended June 30	2004	2003	2002
Net income, as reported	$ 65,020,000	$ 46,581,000	$ 38,417,000
Add: Stock-based employee compensation expense included in reported net income, net of related tax effects	–	–	–
Deduct: Total stock-based employee compensation expense determined under fair value based method for all awards, net of related tax effects	(6,702,000)	(5,301,000)	(5,106,000)
Pro forma net income	$ 58,318,000	$ 41,280,000	$ 33,311,000
Earnings per share:			
Basic – as reported	$ 1.89	$ 1.39	$ 1.24
Basic – pro forma	$ 1.70	$ 1.23	$ 1.07
Diluted – as reported	$ 1.84	$ 1.36	$ 1.20
Diluted – pro forma	$ 1.66	$ 1.21	$ 1.04

Novametrix also had in place, prior to its merger with the Company, warrants outstanding to purchase shares of its common stock. At the date of the merger, the outstanding Novametrix warrants were converted into a total of 71,956 warrants to purchase Respironics common stock with exercise prices ranging from $10.33 per share to $29.52 per share. The warrants expire at various dates through March 2005. As of June 30, 2004, 67,427 warrants remain outstanding, and are all currently exercisable.

In August 2001, the Company adopted the 2002 Employee Stock Purchase Plan (the "2002 Plan") under which employees can purchase common stock of the Company through payroll deductions during each Plan year beginning in 2002 through 2006. The purchase price under each Plan is the lesser of 85% of the market value of the Company's common stock on either the first or last day of the Plan year. The maximum amount employees can purchase currently under the 2002 Plan is equal to 20% of their annual compensation. There are no charges or credits to income in connection with the Plans. Shares are purchased at the end of each Plan year with the funds set aside through payroll deductions.

In June 1996, the Company adopted a shareholders' rights plan under which existing and future shareholders received a right for each share outstanding entitling such shareholders to purchase shares of the Company's common stock at a specified exercise price. The right to purchase such shares is not currently exercisable, but would become exercisable in the future if certain events occurred relating to a person or group (the "acquirer") acquiring or attempting to acquire 20% or more of the Company's outstanding shares of common stock. In the event the rights become exercisable, each right would entitle the holder (other than the acquirer) to purchase shares of the Company's common stock having a value equal to two times the specified exercise price.

> NOTE N: INDUSTRY SEGMENT, FINANCIAL INFORMATION BY GEOGRAPHIC AREAS AND MAJOR CUSTOMERS

The Company conducts its operations in one reportable industry segment: the design, development, manufacture, and sale of medical devices used primarily for the treatment of patients suffering from sleep and respiratory disorders. Sales by product within this segment are as follows:

Year Ended June 30	2004	2003	2002
Net Sales			
Domestic homecare products	$471,645,000	$388,516,000	$339,339,000
Domestic hospital products	95,876,000	79,427,000	57,468,000
International products	192,029,000	161,874,000	98,112,000
NET SALES	$759,550,000	**$629,817,000**	**$494,919,000**

The Company is a Delaware corporation, with its corporate offices located in Murrysville, Pennsylvania. Its principal manufacturing operations are currently located in Pennsylvania, California, Georgia, Connecticut, China and Ireland. Other major distribution and sales sites are located throughout the United States, Germany, France, Hong Kong and Japan. With the acquisition of Profile on July 1, 2004, the Company added manufacturing, sales and distribution operations in the United Kingdom. See Note T to these Consolidated Financial Statements for additional information about Profile.

Financial information about the Company by geographic area is presented below:

Year Ended June 30	2004	2003	2002
Net Sales			
Domestic	$567,521,000	$467,943,000	$396,807,000
International:			
Europe, Africa, and Middle East	95,001,000	74,441,000	61,193,000
Latin America	11,012,000	9,272,000	8,005,000
Far East/Asia Pacific	86,016,000	78,161,000	28,914,000
NET SALES	$759,550,000	**$629,817,000**	**$494,919,000**

June 30	2004	2003
Long-Lived Assets		
United States	$109,394,000	$111,906,000
International:		
Europe	5,177,000	710,000
Far East/Asia Pacific	33,952,000	21,005,000
TOTAL LONG-LIVED ASSETS	$148,523,000	**$133,621,000**

The Company develops, manufactures and markets medical devices primarily for the treatment of patients suffering from sleep and respiratory disorders. Its products are used primarily in the home and in hospitals, as well as emergency medical settings and alternative care facilities. The Company sells and rents primarily to providers and distributors in the healthcare industry and closely monitors the extension of credit to both domestic and foreign customers, including obtaining and analyzing credit applications for all new accounts and maintaining an active program to contact customers promptly when invoices become past due. The Company generally does not require collateral for the extension of credit. During the fiscal years ended June 30, 2003 and 2002, one customer accounted for 10% of net sales. During the fiscal year ended June 30, 2004, that same customer accounted for over 9% of net sales.

> NOTE O: RETIREMENT PLANS

The Company has a Retirement Savings Plan ("the Plan") that is available to all U.S. employees. Employees may contribute up to 30% (to a defined maximum) of their compensation to the Plan. The Company matches employee contributions (up to 3% of each employee's compensation) at a 100% rate, and may make discretionary contributions to the Plan. Total Company contributions to the plan were $2,368,000, $2,204,000, and $1,774,000 for the years ended June 30, 2004, 2003, and 2002, respectively.

> NOTE P: RESTRUCTURING

On October 23, 2002, the Company announced the relocation of several of its smaller product lines and related support functions from the Company's Kennesaw, Georgia manufacturing facility to its Murrysville, Pennsylvania location. This relocation allowed the Company to standardize its manufacturing support, engineering and marketing functions as well as improve the overall efficiency of its manufacturing operations in Kennesaw. Approximately 134 employees were involuntarily terminated and six were relocated as a result of the restructuring actions, primarily from manufacturing and manufacturing support, engineering, purchasing and marketing. In conjunction with these actions, the Company incurred $180,000 of restructuring expenses during the year ended June 30, 2004 and $9,531,000 during the year ended June 30, 2003, related primarily to involuntary termination benefits accruing to employees affected by the restructuring plan, employee transition and relocation benefits, idle facility rent obligations, and certain asset write-offs related to products that were discontinued as a result of the restructuring plan. The transition of products and manufacturing processes from Kennesaw to Murrysville was completed during the quarter ended September 30, 2003, and both facilities are currently operating at capacity levels that reflect the changes brought about by the facility consolidation. Substantially all of the restructuring obligations have been paid as of June 30, 2004, except for $1,752,000 of remaining idle facility costs that will be paid over the remaining term of the lease.

During the year ended June 30, 2003, $9,176,000 of the restructuring charge was included in restructuring and acquisition-related expenses, and $355,000 was included in cost of goods sold in the Consolidated Statement of Operations.

> NOTE Q: ACQUISITIONS

Novametrix: On April 12, 2002, the Company completed its previously announced acquisition of 100% of the outstanding common stock of Novametrix Medical Systems Inc. (now known as "Respironics Novametrix, LLC" and referred to herein as "Novametrix"), a leading cardiorespiratory monitoring company that develops, manufactures and markets proprietary state-of-the-art noninvasive monitors, sensors and disposable accessories. The acquisition of Novametrix was consummated pursuant to an Agreement and Plan of Merger ("Merger") dated as of December 17, 2001, pursuant to which Respironics Holdings, Inc., a wholly owned subsidiary of the Company, was merged with and into Novametrix. The Company made this acquisition for various reasons, including: (a) the Novametrix monitoring products complement the Company's therapeutic products used in the hospital environment, (b) the Novametrix developmental care products complement the Company's infant management products and programs, (c) the Novametrix cardiac output monitoring technologies have the potential to support the Company's initiatives in the congestive heart failure area, and with the acquisition, (d) the Company's "critical mass" of products, revenues, profits and assets in these markets increased, and (e) the Company expects to reduce costs by integrating Novametrix's business functions and processes. The results of operations of Novametrix are included in the Company's Consolidated Statements of Operations beginning on the acquisition date, April 12, 2002.

Upon consummation of the Merger, 2,400,000 shares of the Company's common stock were issued to the former stockholders of Novametrix, reflecting an exchange ratio of .2541 shares of the Company's common stock for each share of Novametrix common stock. The exchange ratio was determined based on the weighted-average selling price of $31.48 for the Company's common stock for the 20-day trading period from March 11 through April 8, 2002. Novametrix stockholders received the Company's stock in an amount equal to $8.00 per Novametrix share based upon the weighted-average selling price. In addition, 509,000 shares of the Company's common stock were reserved for issuance upon exercise of options and warrants issued in exchange for Novametrix options and warrants that were not exercised prior to the consummation of the Merger. As of the close of trading on April 12, 2002, Novametrix common stock ceased to be traded on the NASDAQ National Market.

The total value of the Company's shares issued and reserved for issuance in the transaction was $80,996,000 based on the average fair market value of the Company's common stock during the three-day periods both before and after the first day the number of shares issued became fixed, plus the fair market value of the Company's common stock reserved for issuance. In addition, the Company incurred approximately $4,153,000 in transaction costs directly related to the acquisition (consisting primarily of investment banking and other professional fees), bringing the total acquisition cost to approximately $85,149,000.

The following table summarizes the fair value of the assets acquired and liabilities assumed at the date of acquisition. The allocation of the purchase price was final as of June 30, 2003.

At April 12	2002
Current assets, primarily consisting of accounts receivable and inventories	$ 24,564,000
Property, plant and equipment	2,571,000
Intangible assets	17,478,000
Other non-current assets	1,355,000
Goodwill	51,680,000
Total assets acquired	**$ 97,648,000**
Current liabilities, primarily consisting of accounts payable, accrued expenses, and current portion of debt	12,499,000
NET ASSETS ACQUIRED	**$ 85,149,000**

The amounts assigned to major classes of intangible assets are shown below:

Product-related intellectual property, primarily patents	$ 17,101,000
Employee contracts	377,000
TOTAL INTANGIBLE ASSETS	**$ 17,478,000**

The weighted-average amortization period is approximately 14 years for the product-related intangible assets, approximately one year for the employee contracts, and approximately 14 years in total.

Approximately $3,900,000 of goodwill is expected to be deductible for tax purposes.

In fiscal year 2002, after consummating the acquisition, the Company began to integrate Novametrix's products and programs, employees, systems and processes with its own. In connection with these integration actions, the Company incurred severance and related costs of $1,647,000 for the separation of approximately 50 employees, of which $1,336,000 represented costs of the acquisition and were included in the purchase price allocation for Novametrix, and $311,000 was recorded as restructuring and acquisition-related expenses during the fourth quarter of fiscal year 2002. Restructuring and acquisition-related expenses incurred during the fourth quarter of fiscal year 2002 also included $1,977,000 related to eliminating and centralizing certain corporate services functions, and were primarily comprised of employee transition payments and consulting fees.

In fiscal year 2003, the Company incurred additional restructuring and acquisition-related expenses of $6,205,000 (excluding the impact of the facility changes described below), primarily related to the elimination and centralization of certain corporate services functions and certain compensation-related payments associated with the acquisition and related integration activities. These costs are classified in restructuring and acquisition-related expenses in the Consolidated Statement of Operations for the year ended June 30, 2003.

On April 11, 2003, the Company announced that it would be consolidating product manufacturing activities and other support functions from the Company's Wallingford, Connecticut plant to its Carlsbad, California location. This action represents the final step in the Company's integration of Novametrix. The relocation will allow the Company to standardize its manufacturing support and engineering functions at the Carlsbad plant, will enable the Wallingford facility to concentrate on new product research and development, and will improve the overall efficiency of the Company. Approximately 60 employees are being involuntarily terminated as a result of the restructuring actions, primarily from manufacturing and manufacturing support, purchasing, and certain administrative support functions. During the years ended June 30, 2004 and 2003, the Company recorded $10,380,000 and $1,441,000 of restructuring and acquisition-related expenses, respectively, related to the Wallingford facility restructuring. These costs relate primarily to employee retention and transition benefits and other costs associated with the relocation and transition process. Additionally, approximately $1,911,000 of costs associated with employees' involuntary termination and relocation benefits and idle facility rent obligations was accrued as of April 11, 2003, the date the Company finalized the restructuring plan. These $1,911,000 of costs represent costs of the Novametrix acquisition and were recorded as additional goodwill in the Consolidated Balance Sheet as of June 30, 2003.

Following is a summary of the restructuring and acquisition-related liabilities related to the Novametrix acquisition that were recorded during the year ended June 30, 2004, the payments made against the obligations, and the remaining obligations as of June 30, 2004. This table only includes employee and facility rent obligations, and does not include expenses directly related to the Wallingford facility restructuring that are recorded to restructuring and acquisition-related expenses as they are incurred.

	Accrued Employee Costs	Accrued Facility Costs
BALANCE AT JUNE 30, 2003	**$ 1,668,000**	**$ 1,075,000**
Restructuring and acquisition-related expenses	3,366,000	–
Liability adjustment – costs of acquired business	(270,000)	–
Cash payments	(2,707,000)	(32,000)
BALANCE AT JUNE 30, 2004	**$ 2,057,000**	**$ 1,043,000**

Substantially all of the accrued obligations (including amounts that will be accrued during the quarter ended June 30, 2004 and during the 2005 fiscal year) are expected to be paid by January 31, 2005, except for the idle facility costs that will be paid over the remaining term of the lease. As previously announced in February 2004, the Company received a warning letter from the U.S. Food & Drug Administration regarding the Carlsbad, California manufacturing facility. The Company temporarily delayed certain aspects of the facility restructuring until the warning letter matters are resolved. Consequently, the Company will incur additional restructuring and acquisition-related expenses during the first half of the 2005 fiscal year to complete the facility consolidation.

In the fourth quarter of fiscal year 2002, the Company ceased work on an oxygen monitoring technology development project based in part on the results of a review of that technology by engineers from Novametrix that was conducted after the acquisition. This decision resulted in an impairment charge totaling $2,006,000 in the fourth quarter representing the write-off of intangible assets, inventory and fixed assets related to the project. This amount is included in restructuring and acquisition-related expenses in the Consolidated Statement of Operations for the year ended June 30, 2002.

The following unaudited pro forma summary presents the Company's results of operations as if the acquisition had occurred at the beginning of the period indicated and does not purport to be indicative of what would have occurred had the acquisition been made as of that date, or of results that may occur in the future. These pro forma results of operations do not reflect the positive impact of cost reductions and other synergies that were realized as a result of the merger, nor do they include non-recurring restructuring and acquisition-related expenses incurred following the merger.

Year Ended June 30	2002
Pro forma sales	$531,606,000
Pro forma net income	37,857,000
Pro forma earnings per share	1.12

Novametrix had an April fiscal year-end, which differed from the Company's June year-end. In order to develop the fiscal year 2002 pro forma information, the Company's income statement for the year ended June 30, 2002 (which included Novametrix's results of operations effective April 12, 2002) was combined with Novametrix's unaudited income statement for the period July 1, 2001 through April 12, 2002. Earnings per share data are based on the Company's weighted-average number of common shares outstanding plus the total number of the Company's common shares and equivalents delivered to Novametrix stockholders as part of the acquisition.

Fuji: In May 2002, the Company acquired a 60% controlling interest in Fuji RC Kabushiki Kaisha (now known as "Fuji Respironics Kabushiki Kaisha" and referred to herein as "Fuji"), a leading provider of homecare and hospital products and services for respiratory-impaired patients in Japan, and entered into an agreement to purchase all of the remaining outstanding shares of Fuji in four annual installments of $1,433,000, the last of which is due on December 31, 2006 (before the amendment described below). As of June 30, 2004 and 2003, the net present value of the Company's remaining obligation under the fixed-price forward contract, $2,709,000 and $5,455,000, respectively, is accounted for as a financing of the Company's purchase of the minority interest and is classified with other non-current liabilities in the consolidated balance sheets. Including the fixed-price forward contract and costs directly associated with the acquisition, the base cash purchase price for all of the outstanding shares is approximately $12,662,000 with provisions for additional payments to one of the shareholders of Fuji to be made based on the operating performance of Fuji over four years, payable on December 31, 2006. These additional payments are being accrued as compensation over the four-year period as they are earned by the shareholder during his post-acquisition employment period. As of June 30, 2004 and 2003, $8,344,000 and $2,036,000, respectively, is accrued in the Consolidated Balance Sheets and classified with other non-current liabilities pertaining to this obligation. The liability balances as of June 30, 2004 are net of amounts paid in conjunction with the October 29, 2003 amendment to the stock purchase agreement described below. No amounts of the purchase price were assigned to goodwill or other intangible assets since the initial purchase price equaled the fair market value of the net tangible assets acquired.

On October 29, 2003, the Company and the 40% shareholder of Fuji entered into an amendment to the stock purchase agreement described above, whereby the Company acquired 20% of the outstanding shares of Fuji for $5,090,000 on the closing date of the amendment. The Company will acquire the remaining outstanding shares of Fuji on December 31, 2005 and 2006 for a total of $3,431,000. Provisions for the additional payments based on the operating performance of Fuji described above remain in effect. The Company does not expect the total of the payments due under the amended purchase agreement to be different than the total of those payments under the original purchase agreement described previously.

BiliChek: On March 6, 2003, the Company acquired certain assets related to the BiliChek Non-invasive Bilirubin Analyzer product line from SpectRx, Inc. for a base purchase price of $4,000,000 and up to $7,250,000 of additional future payments based on the achievement of various performance milestones following the acquisition through December 31, 2007. During the year ended June 30, 2004, the Company accrued $1,993,000 for milestones achieved during the period (of which $1,655,000 was paid as of June 30, 2004). The acquisition expands the Company's involvement with the acquired product line from U.S. marketing and sales under a prior exclusive license agreement, to worldwide marketing and sales and also to the future development and manufacturing of the product. The acquisition did not materially impact the Company's net sales or net income during the years ended June 30, 2004 or 2003. In connection with the acquisition and subsequent milestone payments, the Company recorded $4,370,000 of intangible assets, representing the fair market value of acquired product-related intellectual property and employee contracts. The weighted-average amortization period for these intangible assets is approximately 14 years.

Caradyne: On February 27, 2004, the Company acquired 100% of the outstanding capital stock of Western Biomedical Technologies (WBT), an Ireland-based company, which owns 100% of the outstanding capital stock of Caradyne Limited [now known as "Respironics (Ireland) Limited"] for a base purchase price of $5,970,000 (including transaction costs), of which $4,470,000 was paid at closing and up to $1,500,000 is scheduled to be paid at the end of a two-year retention period. The Company may also be required to make up to $2,500,000 of additional future payments based on the achievement of various performance milestones following the acquisition through July 1, 2005. Subsequent to June 30, 2004, the Company paid $1,000,000 as a result of the successful achievement of a performance milestone. WBT and Caradyne Limited are collectively referred to herein as "Caradyne." Caradyne is involved in the development, manufacturing and marketing of unique technologies that are complementary with the Company's ventilation product portfolio, primarily used in hospital settings and pre-hospital applications. The acquisition did not materially impact the Company's net sales or net income during the year ended June 30, 2004. In connection with the acquisition, the Company recorded $3,751,000 of intangible assets, representing the fair market value of acquired product-related intellectual property and employee contracts. The weighted-average amortization period for these intangible assets is approximately 15 years.

> NOTE R: EARNINGS PER SHARE

The following table sets forth the computation of basic and diluted earnings per share:

Year Ended June 30	2004	2003	2002
Numerator:			
Net income	$ 65,020,000	$ 46,581,000	$ 38,417,000
Denominator:			
Denominator for basic earnings per share – weighted-average shares	34,377,000	33,585,000	31,079,000
Effect of dilutive securities – stock options and warrants	932,000	759,000	929,000
Denominator for diluted earnings per share – adjusted weighted-average shares and assumed conversions	35,309,000	34,344,000	32,008,000
Basic earnings per share	$ 1.89	$ 1.39	$ 1.24
Diluted earnings per share	$ 1.84	$ 1.36	$ 1.20

> NOTE S: QUARTERLY RESULTS OF OPERATIONS (UNAUDITED)

Following are the unaudited quarterly results of operations for the fiscal years ended June 30, 2004 and 2003:

Three Months Ended	September 30	December 31	March 31	June 30
2004				
Net sales	$164,058,000	$192,318,000	$196,732,000	$206,442,000
Gross profit	84,056,000	101,479,000	106,486,000	110,903,000
Restructuring and acquisition-related expenses	3,345,000	2,545,000	2,885,000	2,167,000
Contribution to foundation	–	1,500,000	–	1,344,000
Net income	11,150,000	15,902,000	18,194,000	19,674,000
Basic earnings per share	0.33	0.47	0.53	0.56
Diluted earnings per share	0.32	0.45	0.51	0.55

Three Months Ended	September 30	December 31	March 31	June 30
2003				
Net sales	$138,642,000	$151,881,000	$161,858,000	$177,436,000
Gross profit	68,136,000	76,330,000	82,727,000	92,239,000
Restructuring and acquisition-related expenses	3,165,000	7,043,000	3,182,000	4,398,000
Net income	8,886,000	9,213,000	13,917,000	14,566,000
Basic earnings per share	0.27	0.28	0.41	0.43
Diluted earnings per share	0.26	0.27	0.41	0.42

> NOTE T: SUBSEQUENT EVENT

On July 1, 2004, the Company's previously announced offer to acquire Profile Therapeutics plc (referred to herein as "Profile") was declared unconditional, and the Company paid 50.9 British Pence for each share of Profile. The total purchase price was 25,140,000 British Pounds (or approximately $46,057,000). Profile is a UK-based company that distributes, develops and commercializes specialty products to improve the treatment of sleep and respiratory patients. The acquisition of Profile expands the Company's presence in the global sleep and respiratory markets, and enhances the breadth of its products and services with Profile's new innovative technologies for respiratory drug delivery.

Report of Independent Registered Public Accounting Firm

Board of Directors and Shareholders
Respironics, Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheets of Respironics, Inc. and subsidiaries as of June 30, 2004 and 2003, and the related consolidated statements of operations, shareholders' equity, and cash flows for each of the three years in the period ended June 30, 2004. 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 the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Respironics, Inc. and subsidiaries as of June 30, 2004 and 2003, and the consolidated results of their operations and their cash flows for each of the three years in the period ended June 30, 2004, in conformity with U.S. generally accepted accounting principles.

As discussed in Note A to the consolidated financial statements, the Company adopted Statement of Financial Accounting Standards No. 142, "Goodwill and Other Intangible Assets," effective July 1, 2002.

Ernst & Young LLP

Pittsburgh, Pennsylvania
July 20, 2004

Five-Year Summary

(amounts in thousands except per share data)

Year Ended June 30	2004	2003	2002	2001	2000
Per Share Data					
Net income	$ 1.84[1]	$ 1.36[2]	$ 1.20[3]	$ 1.09	$ 0.19[4]
Book value at year end	14.84	12.57	11.04	7.75	6.49
Results of Operations					
Net sales	$ 759,550	$ 629,817	$ 494,919	$ 422,438	$ 368,184
Cost of goods sold	356,625	310,385	260,795[5]	224,087	205,230[5]
Income before income taxes	105,234[1]	74,890[2]	64,036[3]	55,908	8,576[4]
Net income	65,020[1]	46,581[2]	38,417[3]	33,571	5,752[4]
Financial Position at Year End					
Working capital	$ 301,032	$ 212,787	$ 198,966	$ 171,985	$ 155,095
Property, plant, and equipment (net)	111,057	98,680	99,935	69,147	66,785
Total assets	711,139	582,196	550,911	367,295	352,577
Long-term obligations	26,897	16,513	59,502	80,055	108,095
Shareholders' equity	519,053	426,869	367,720	235,268	191,106
Other Data					
Capital expenditures	51,391	42,075	39,830	28,236	27,304
Depreciation and amortization	44,556	46,952	34,232	28,338	26,706
Number of employees at year end	3,032	2,698	2,589	2,056	1,940
Diluted shares outstanding	35,309	34,344	32,008	30,886	30,004
Selected Financial Ratios					
Gross profit as a percent of sales	53%	51%	47%[5]	47%	44%[5]
Income before income taxes as a percent of sales	14%[1]	12%[2]	13%[3]	13%	2%[4]
Effective income tax rate	38%	38%	40%	40%	33%[6]
Net income as a percent of sales	9%[1]	7%[2]	8%[3]	8%	2%[4]
Return on average equity	14%[1]	12%[2]	13%[3]	16%	3%[4]
Debt to equity ratio	5%	4%	16%	34%	57%
Current ratio	2.99x	2.67x	2.79x	4.31x	3.91x

[1] *Includes the impact of restructuring and acquisition-related expenses related primarily to the restructuring of operations at the Wallingford, Connecticut manufacturing facility. These costs reduced net income by $10,942 ($0.19 per share) in fiscal year 2004.*

[2] *Includes the impact of restructuring and acquisition-related expenses related to the integration of Novametrix Medical Systems Inc. ("Novametrix") and restructuring of operations at the Kennesaw, Georgia and Wallingford, Connecticut manufacturing facilities, and other acquisition-related costs. These costs reduced pre-tax income by $18,144, and net income by $11,286 ($0.32 per share) in fiscal year 2003.*

[3] *Includes the impact of a non-recurring purchase accounting adjustment related to reversing acquisition date inventory fair market value adjustments as inventory was sold subsequent to the acquisition of Novametrix, restructuring and acquisition-related expenses related to the integration of Novametrix, and an asset impairment charge. These costs reduced pre-tax income by $5,947, and net income by $3,853 ($0.12 per share) in fiscal year 2002.*

[4] *Includes the impact of restructuring expenses related to the Company's July 1999 restructuring, a specific addition to the allowance for doubtful accounts due to a customer bankruptcy, and a one-time reduction in income tax expense. These costs reduced pre-tax income by $33,696, and net income by $19,611 ($0.66 per share) in fiscal year 2000.*

[5] *Includes the impact of the restructuring expenses described above of $8,710 in fiscal year 2000 and the non-recurring purchase accounting adjustment described above of $1,653 in fiscal year 2002.*

[6] *Includes the impact of the one-time reduction in income tax expense described above.*

Shareholder Information

Corporate Headquarters

1010 Murry Ridge Lane
Murrysville, PA 15668-8525
P: 724-387-5200

Annual Meeting of Shareholders

The annual meeting of shareholders will be held at Two Mellon Bank Center at 501 Grant Street, Pittsburgh, Pennsylvania on Tuesday, November 16, 2004 at 5:00 p.m., in the Auditorium on the Tenth Floor.

Market for the Company's Common Stock and Related Shareholder Matters

The Company's shares are traded on the over-the-counter market and are reported on the NASDAQ National Market System under the symbol RESP. The Company began trading on the national over-the-counter market on May 12, 1988. As of October 4, 2004, there were 2,356 shareholders of record of the Company's common stock.

The Company has never paid a cash dividend with respect to its common stock and does not intend to pay cash dividends in the foreseeable future.

High and low price information for the Company's common stock for the applicable quarter is shown below:

Fiscal Year Ended June 30	1st Quarter	2nd Quarter	3rd Quarter	4th Quarter
2004				
High	$43.57	$47.00	$54.74	$58.75
Low	$37.96	$40.00	$43.88	$50.53
2003				
High	$35.21	$34.07	$34.72	$40.00
Low	$26.50	$28.76	$28.73	$34.31

Form 10-K

Copies of the Respironics, Inc. Annual Report on Form 10-K can be found on the Company's website as filed with the Securities and Exchange Commission; otherwise copies will be mailed without charge upon request. Address requests to Dorita Pishko, Corporate Secretary, Respironics, Inc. 1010 Murry Ridge Lane, Murrysville, PA 15668-8525.

Shareholder Inquiries/Financial Data

Shareholders, analysts or others seeking information about the company are encouraged to contact Daniel Bevevino, Vice President and Chief Financial Officer, or James Woll, Vice President and Corporate Controller at Respironics, Inc. 1010 Murry Ridge Lane, Murrysville, PA 15668-8525 or by calling 724-387-5200.

Market Makers

Adams, Harkness & Hill, Inc.
Archipelago Exchange (The)
Bank of America Securities
Boston Stock Exchange
BrokerageAmerica, LLC
Cantor, Fitzgerald & Co.
Citigroup Global Markets, Inc.
Credit Suisse First Boston
Crown Financial Group
Deutsche Bank Alex Brown
Fidelity Capital Markets
First Albany Capital Inc.
Goldman, Sachs & Co.
GVR Company LLC
Harris Nesbitt Corp.
Jefferies & Company, Inc.
Knight Equity Markets, L.P.
Leerink Swann & Co.
Lehman Brothers, Inc.
McDonald Investments Inc.
Merrill Lynch, Pierce, Fenner
Morgan Stanley & Co., Inc.
National Stock Exchange
Parker/Hunter Inc.
Prudential Equity Group, Inc.
Schwab Capital Markets
SG Cowen Securities
Susquehanna Capital Group
The Robinson Humphrey Co.
Timber Hill Inc.
Wachovia Capital Markets
Wells Fargo Van Kasper

Research Coverage

Banc of America Securities
First Albany Corporation
Harris Nesbitt Gerard
LJR Great Lakes Review
Parker/Hunter Inc.
Wachovia Securities

Transfer Agent and Registrar

Mellon Investor Services LLC,
85 Challenger Road, Ridgefield Park, NJ 07660
or www.melloninvestor.com

General Counsel

Steven P. Fulton

Independent Registered Public Accounting Firm

Ernst & Young LLP, Pittsburgh, PA 15222

Design: Mizrahi Design Associates, Inc. www.mizrahidesign.com

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