



Strategy, Execution and Results

**We are in the business of solving
our customers' complex,
critical problems.**

Dynamics Research Corporation is an innovative solutions provider that partners with its customers in government and commercial sectors to apply proven processes and technology. DRC delivers engineering, logistics and information technology services and precision manufactured products that enhance the performance and cost effectiveness of its customers' mission critical systems.

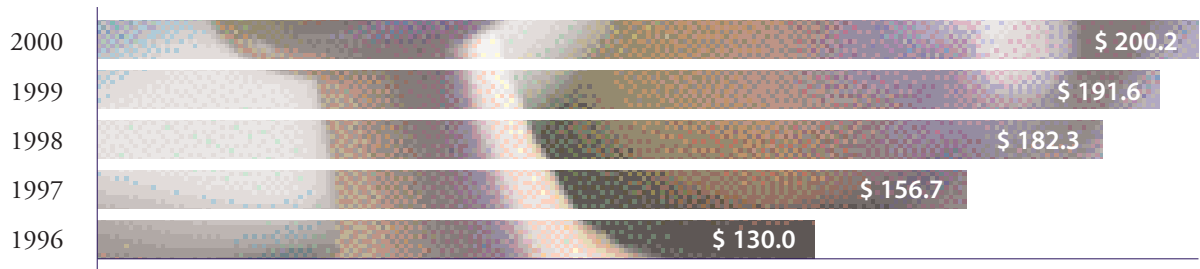
2000 Highlights:

- Developing and beginning implementation of a five-year strategic plan
- Organizationally aligning the company to achieve its strategic objectives
- Launching employee-centered initiatives, including an enterprise-wide human resources planning system and an employee stock purchase plan
- Reaching the highest levels of revenue and net income in the company's 46-year history
- Achieving profitability across all business segments
- Generating \$4.7 million in cash flow from operations
- Strengthening the balance sheet, reducing debt by 21 percent
- Winning \$206 million in new and repeat orders
- Receiving ISO 9001 certification for the Encoder Division
- Successfully completing pilot implementation of the State of Colorado child welfare system, followed by the commencement of statewide rollout shortly after the end of the year

(in millions of dollars, except per share data)

	2000	1999	1998	1997	1996
Revenue	\$ 200.2	\$ 191.6	\$ 182.3	\$ 156.7	\$ 130.0
Operating income (loss)	9.2	(11.4)	2.5	7.8	4.3
Net income (loss)	4.6	(7.5)	(6.0)	4.1	1.7
Income (loss) per share - diluted	.59	(1.02)	(.77)	.53	.22
Total assets	78.7	75.2	88.1	77.6	71.0
Total debt	15.5	19.7	26.8	10.0	12.1
Stockholders' equity	29.3	23.8	31.2	39.1	35.2

Revenue



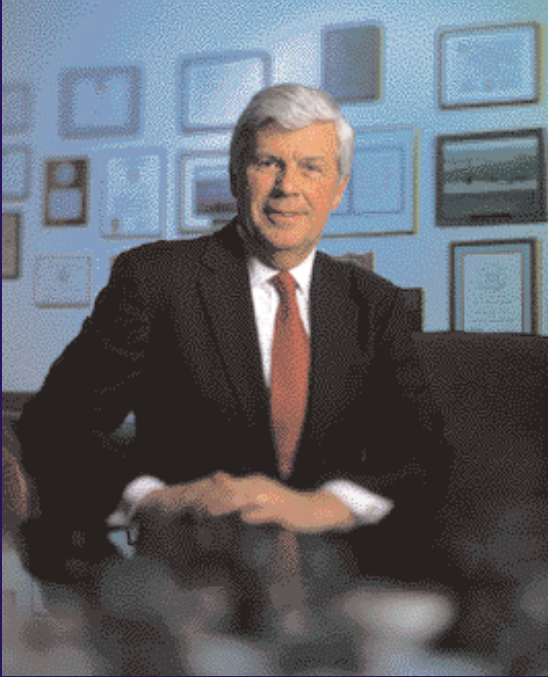
Net Income (Loss)



Stockholders' Equity



To Our Shareholders



The year 2000 was a period of tremendous progress and improvement for Dynamics Research Corporation (DRC). The company achieved profitability in all four quarters. Revenue and net income for the year were the highest in company history, and the balance sheet was greatly strengthened. These impressive results were due to the teamwork, focus and hard work of DRC's dedicated employees.

We began the year by implementing a game plan to dramatically improve operational performance. We established clear goals to guide operations. We set out to improve profitability, strengthen and energize our workforce, invest in technologies to improve operations and enhance customer satisfaction. Actions were assigned, and schedules established, to drive performance toward goal achievement. We faced considerable challenges and had considerable success.

Looking ahead, our strategy and vision for the future are clear. We have specific long-term objectives and know where we are going. Having successfully returned to profitability, we are now focused on cultivating new business opportunities that will result in consistent and sustainable profit growth.

Strategic Plan

In assessing our long-range prospects, senior management developed a five-year strategic plan to guide long-term growth. In forming the plan, we critically assessed all aspects of DRC's business operations and capabilities. We evaluated products and services, markets served, corporate values and culture, infrastructure support systems and shareholder value. This analysis resulted in a cohesive strategic plan supported by four breakthrough objectives that ultimately guide everyday decisions. These are to:

Continuously improve DRC's financial value. While I am extremely pleased we were able to achieve strong operating results in 2000, there is much more to be done. Our long-term expectation is that DRC can reach a sustainable revenue growth rate of at least 20 percent, roughly half organic and half through acquisition. From a profitability viewpoint, we expect the company to develop a sustainable operating income margin of 8 percent or higher, and achieve returns on invested capital in excess of 15 percent.

Grow DRC's business in selected markets. We are focused on expanding our presence in markets where DRC already possesses recognized expertise. We plan to do this by expanding sales and marketing programs, winning new customers and continuously measuring and improving customer satisfaction. While DRC's defense business, currently annualized at \$150 million, will continue to grow, we expect our business in federal civil, state government and commercial markets to grow more rapidly.

Create a culture that makes DRC an employer of choice. We aspire to make DRC a place where employees are excited about their work and proud of their affiliation with the company. The continued, sustained success of our company and each of its operating units, along with the recognition of our employees in this achievement, will provide the foundation for realizing this goal. We also want to provide an environment in which their skills and talents can flourish. We are moving toward this goal by continuously measuring and improving employee satisfaction, and by implementing best-in-class human resource support practices and compensation programs—including broad employee stock ownership.

Establish DRC as a leader in operational effectiveness. Long recognized by our customers for our technical expertise, we will further enhance customer satisfaction through the deployment of continuous process improvement methodologies and integrated enterprise business systems.

Financial Results

Returning to profitability while instituting a stable capital structure was our chief objective for 2000. By all measures we made excellent progress. For the year ended December 31, 2000, DRC posted net income of \$4.6 million, or \$.59 per diluted share. Revenue for the year was \$200.2 million, up 4.5 percent over 1999. The company generated \$4.7 million in cash from operations for the year, reducing debt from 45 percent of invested capital at the beginning of the year to 35 percent at year end.

Customer Satisfaction

Our customers repeatedly expressed satisfaction with DRC's products and services by placing new and repeat orders totaling \$206 million in 2000. Over the past year I have had the opportunity to visit many of DRC's customers to hear directly from them just how we are doing. I found their views on the quality and value of DRC's services and products very encouraging. Renewals of contract tasking from longstanding Department of Defense customers and expanded contracts from key customers in our state health and human services business made a large contribution to 2000 results, and will provide benefits in 2001 and beyond.

Noteworthy has been the progress made in delivering a new child welfare information system project for the State of Colorado. Now reorganized under new internal management, this large system development project successfully completed pilot testing in two counties and recently commenced statewide rollout. Colorado placed additional multi-year information technology service contracts consisting of both new business as well as the expansion of existing contracts, which will provide approximately \$6.5 million of incremental revenue to DRC in 2001.

Employer of Choice

Making DRC a stimulating and rewarding workplace so we can retain and attract valued employees is a key management objective, and we made a great deal of progress toward this goal in 2000. Specifically, we launched several employee-centered initiatives, including new training programs, an employee satisfaction survey, more flexible benefits, and a system of rewards and recognition for employee excellence. In addition, we awarded stock options to 20 percent of employees as part of their compensation packages and have initiated an employee stock purchase plan. We bolstered our management capabilities by adding new senior executives who have the experience to manage future growth. On January 1, 2001, we formally realigned the management structure around core expertise, markets and strategic plan requirements. Each employee now knows how he or she can personally contribute to DRC's success.

Operational Effectiveness

In our quest to improve operational effectiveness, we applied our expertise in business process re-engineering to some of our internal operations. Initial outcomes include implementation of the company's first enterprise-wide business system—for human resource management—and the kick-off of a formal continuous process improvement program. In our Precision Manufactured Products group, we received ISO 9001 certification—an internationally recognized standard of manufacturing system excellence—for the Encoder Division, which manufactures electro-mechanical devices for calibrating and controlling motion in sensitive machinery.

2001 Outlook and Objectives

The outlook for profitable growth in 2001 is bright, and we will be applying a much heavier emphasis on overall business growth. Last year we retooled internal processes to support the pursuit and capture of new business. For 2001, our operating plan includes increased investment in business development resources and activities. Prospects are excellent for continued growth in defense and state systems and services businesses. In the commercial sector, we are closely watching the general slowdown in manufacturing for signs of a possible negative impact on our Precision Manufactured Products business.

We are on a mission to increase DRC's enterprise value by focusing on five broad areas in 2001:

- Commitment to enhanced quality and customer satisfaction;
- Improved bookings, revenue and profitability across all lines of business;
- Initiatives to improve employee development and satisfaction;
- Application of continuous process improvement principles to critical business processes; and
- Investment in technology enablers to improve operational effectiveness.

Additionally, we plan to take a careful, selective approach to acquisition opportunities. We are looking to make small acquisitions that expand sales channels and/or provide greater access to markets consistent with DRC's strategic interests. Our intent is to add up to \$20 million in incremental annualized revenue, with acquired operations becoming accretive to earnings within a year.

With a well-defined growth strategy and focus, a strengthened management team and a full year of strong financial results there is a renewed sense of enthusiasm and confidence toward future prospects throughout DRC. Above all, I appreciate the enthusiasm and energy with which employees have adapted to a new pace and more disciplined operations. We are also grateful for our shareholders' loyalty and support.

Sincerely,



James P. Regan
President and Chief Executive Officer

Game Plan for Growth

With insight and expertise built on decades of success, Dynamics Research Corporation provides its customers with the strategies and tools they need to analyze options, make masterful moves and achieve organizational objectives. The pages that follow highlight DRC's primary capabilities and competencies for solving complex, mission-critical problems.


**We help customers achieve their goals,
whatever their game.**

In early 2000 DRC forged a long-range strategic plan, which serves as a game plan for guiding the corporation's growth and evolution through 2004. Within that timeframe, DRC aims to attain four primary, yet interrelated goals. These are to:

- Increase shareholder value
- Grow in selected markets
- Be an employer of choice
- Achieve operational excellence

The plan specifies a combination of building upon existing customer business—some of which has spanned nearly five decades; launching business development initiatives that extend unique, valuable competencies into new markets; and revitalizing and updating internal resources and infrastructure.

Logistics



Determining how to accomplish more with fewer dollars is a prime mandate for the U.S. military. One of the first places to improve cost efficiencies is in logistics—the procurement, supply and maintenance of equipment—which accounts for 60-70 percent of the cost of operating an aircraft. DRC provides logistics and supply chain management expertise to the U.S. Air Force, Army and Navy aviation operations. DRC engineers and logistics experts have developed a specialized software program that tracks and forecasts aircraft fuel and ammunition requirements, the location and availability of parts, and the availability of repair bays—as well as managing the scheduling of repairs. DRC staff also works on site at customer operations in a classic management consultant role, establishing supply chain management systems and evaluating and performing logistics operations.



Managing Air Force Logistics

DRC performs logistics analyses and operations for the U.S. Air Force's three domestic Air Logistics Centers located at Tinker Air Force Base (AFB) in Oklahoma, Robins AFB in Georgia and Hill AFB in Utah. Working on base and in company offices, DRC employees provide logistics support, information technology management and analysis, custom database development, system engineering and technical services.

Minimizing Maintenance Costs

DRC is developing an analytical simulation model that will enable Tinker Air Force Base to determine ways to more efficiently conduct depot repairs on aircraft engines, especially for the F-16's 100-220 engine. A key program objective is minimizing the lifecycle costs of maintaining major weapons systems.



Manpower Analysis

DRC is developing an analytical tool for the Chief of Naval Education & Training that simulates the training pipeline for new recruits and helps the Navy analyze and predict demand for basic and advanced training programs. The system will enable the Navy to ascertain the costs and risks of potential changes to training programs before they are made.

Tracking Fleet Assets

A simulation program created by DRC for the U.S. Air Force, using data collected from a variety of sources, models the availability and capacity of aircraft and other assets fleet-wide. Designed to provide key information for planning missions, the system enables commanders to determine aircraft availability and location, and the number of pilots, mechanics, electricians, hydraulics specialists and other technicians required to operate them.

Modeling and Simulation

Software models that simulate complex organizational and human processes are important tools for streamlining workflow, improving performance, controlling material costs and reducing the number of people required to perform a job. DRC combines expertise in software engineering with knowledge of organizational requirements and processes to customize off-the-shelf, object-oriented software for modeling and reengineering customer operations. DRC's systems have been deployed in a range of environments and applications—from improving workflow and efficiencies at aircraft repair and maintenance shops to assessing manpower requirements for major military operations. DRC simulation systems are also used to create realistic scenarios for training on usage of specialized computer applications for situations that require rapid decision making.

Custom Engineering



Semiconductor Processing Equipment

The number of semiconductor devices used in computer, telecommunications, medical and consumer products is proliferating rapidly. DRC encoders are used to enhance the precision and operating speed of semiconductor processing equipment, a market that has strong growth potential.

Medical Electronics

Recent innovations in medical technology are leading to the use of miniaturized electronics in a variety of devices including body probes, hearing aids, pacemakers, intra-vascular catheters and blood and body fluid analysis equipment. This trend represents a major market opportunity for DRC's Metrigraphics products. The company's flexible circuits are now used to diagnose the electrical properties of blood and in electronics embedded in heart catheters for angioplasty procedures.

Avalanche Detection

DRC integrated an inertial measurement device and a receiver board incorporating the Global Positioning System for Swiss scientists at the École Polytechnique Fédérale de Lausanne. Used from a helicopter to help measure landforms and snow mass, the system enables scientists to more accurately predict the time and location of potential avalanches.

DRC's ability to rapidly design and manufacture customized components enables its customers to get their products to market sooner and at lower cost, creating a strong demand for custom engineering services. The company's Metrigraphics Division designs and produces high density, multi-layer flexible miniature circuits, micro-miniature mechanical parts, disks and screens with tolerances as fine as one micron. These products are manufactured through a process known as electroforming, whereby a thin composite metal film is deposited in a precise pattern. The Encoder Division designs and assembles electro-mechanical devices that provide precise position feedback in a wide range of capital equipment, enabling machines such as semiconductor processing equipment to operate faster and with greater precision. DRC's Test Equipment Division also offers custom engineering services, developing specialized components for aircraft navigation systems, for example.

Managing Lifecycle Requirements

Trident II Missile System

DRC builds specialized equipment that tests and validates the accuracy and operability of gyroscopes and other navigational equipment for Trident II

Reverse Engineering

DRC's Test Equipment Division has longstanding expertise in the reverse engineering of electronics, a capability that can greatly extend aircraft and other weapons systems' operating life spans—especially when crucial parts are no longer in mass production. DRC has reverse engineered electronics equipment for military aircraft that are 15-20 years old.

Maintaining the accuracy and advanced functionality of major weapons systems is a key priority for the Department of Defense, thereby requiring constant testing and evaluation. With its expertise in engineering and running and maintaining mammoth databases, DRC has participated in the upkeep of several legacy systems, including the U.S. Navy's Polaris, Poseidon and Trident missile programs. DRC provides "cradle-to-grave" data capture, management and analysis for missile guidance systems and components. DRC employees both understand legacy system operations and know how to incorporate new technological developments to improve system capability and efficiency. For the Trident II missile program, DRC's engineering staff performs complicated mathematical analyses to set navigational algorithms, and conducts software validation and verification procedures to ensure navigation systems are accurate and functioning correctly. DRC also develops new software and reengineers and replaces obsolete circuits by generating models of semiconductor devices.

te Information Technology Services

Infrastructure Maintenance & Support

DRC is providing large-scale infrastructure support in the states of Colorado and Ohio. In Ohio, DRC provides direct maintenance and help desk support for a statewide local area network (LAN) consisting of approximately 16,500 workstations. DRC's staff consists of certified engineers and technicians providing real-time support. In Colorado, the company recently received amendments worth \$5.5 million to its children, youth and family (CYF) contract, consolidating maintenance efforts for another statewide LAN, and providing support to three different automated systems for the CYF department in 2001.

Job Performance Support System

DRC has developed a state-of-the-art computer-based training and job performance support system for the State of Colorado that combines online learning capabilities with direct access to policies and procedures via an intranet. Scaled to accommodate individual user's varying knowledge of computer systems, it prompts social workers on the day-to-day use of business process system software applications. This system recently won first place and "best-in-show" for its online instruction and computer-based training capability in a national competition.

Federal legislation requiring states to automate systems for tracking and monitoring child welfare cases has opened up a major market for state information technology services. Leveraging its expertise in large, complex information systems, DRC moved into the state arena in 1995 beginning with the State of New Hampshire. The company has since helped automate child welfare and other information technology systems for health and human service agencies in Ohio and Colorado. DRC's work has ranged from customizing existing software to building an entire information technology and computer communications infrastructure. The company has won repeat business from its state customers—most recently expanding its work with the State of Colorado. One of these new awards has DRC assisting with the development and implementation of a new statewide benefits management system for Colorado's Departments of Human Services and Health Care Policy and Financing. The new system will integrate eligibility determination across major benefits programs. DRC will design, develop and deliver training, online policies and procedures, computer-based training and help desk services.

Hospital Medical Teamwork

An outgrowth of a highly successful program DRC created for improving teamwork and reducing accident rates for U.S. Army helicopter crews, MedTeams instills a teamwork ethic among emergency room staff in civilian and military hospitals. The program instructs medical staff in techniques for interacting more effectively and minimizing error under high-stakes, high-stress situations.

Military Training Exercises

Military training exercises in various world theaters involve thousands of people, as well as the supplies, vehicles and equipment to support them. Such exercises require coordination among various branches of the service to prevent scheduling and resource conflicts. DRC is developing a Web-based system for the Joint Chiefs of Staff that allows authorized personnel to log on and obtain or add real-time updates on planned training exercises.

DRC helps customers achieve mission objectives and reduce risk of error by developing training programs—both computer-based and in actual job environments—to improve individual and team performance. Working in conjunction with internal and external subject-matter experts, DRC's multidisciplinary teams of training analysts, instructional designers, graphics specialists and technical writers collaborate to create computerized course materials to be used in distance learning or classroom situations. DRC has created a range of computer-based training programs—from systems that teach pilots and sensor operators to use special equipment on U.S. Customs Service aircraft to online systems that coach social workers on the use of special computer applications. Behavioral scientists at DRC have also created programs that reduce accident and error rates by improving teamwork in high-risk situations that require immediate decision making.

Selected Financial Information

Five Year Summary	2000	1999	1998	1997	1996
<i>(in thousands of dollars, except share, per share and employee data)</i>					
Revenue	\$ 200,175	\$ 191,621	\$ 182,344	\$ 156,733	\$ 129,997
Operating income (loss)	9,203	(11,378)	2,459	7,807	4,283
Income (loss) from continuing operations	4,353	(8,888)	491	5,177	2,311
Net income (loss)	4,559	(7,526)	(5,971)	4,129	1,729
Income (loss) from continuing operations per common share - basic	.57	(1.21)	.07	.69	.31
Income (loss) from continuing operations per common share - diluted	.56	(1.21)	.06	.66	.30
Net income (loss) per common share - basic	.60	(1.02)	(.80)	.55	.23
Net income (loss) per common share - diluted	.59	(1.02)	(.77)	.53	.22
Total assets	78,702	75,188	88,067	77,629	70,950
Total debt	15,534	19,700	26,800	10,000	12,101
Stockholders' equity	29,289	23,805	31,246	39,147	35,239
Return on invested capital	12.0%	(13.8)%	2.4%	10.6%	6.2%
Stockholders' equity per share	3.85	3.23	4.24	5.19	4.69
Return on stockholders' equity	15.6%	(31.6)%	(19.1)%	10.6%	4.9%
Backlog	89,843	83,549	105,427	110,001	73,200
Cash flow from operations	4,735	10,985	(11,406)	7,980	1,035
Research and development expense	150	1,478	2,739	1,249	2,189
Capital expenditures	3,120	2,702	3,171	5,104	9,266
Depreciation and amortization	3,746	6,060	6,219	5,240	4,910
Number of shares outstanding at end of year	7,601,519	7,363,324	7,369,190	7,546,646	7,515,630
Number of employees	1,504	1,613	1,557	1,455	1,349

Quarterly Information (Unaudited)

(in thousands of dollars, except share and per share data)

	1st Qtr	2nd Qtr	3rd Qtr	4th Qtr
2000				
Revenue	\$ 47,790	\$ 54,440	\$ 48,376	\$ 49,569
Gross margin	5,556	7,215	6,257	5,733
Operating income	1,512	2,981	2,701	2,009
Income from continuing operations	556	1,436	1,350	1,011
Gain on discontinued operations	171	35	-	-
Net income	727	1,471	1,350	1,011
Income from continuing operations per common share - diluted ⁽¹⁾	.07	.19	.17	.13
Gain on discontinued operations per common share - diluted ⁽¹⁾	.02	-	-	-
Net income per common share - diluted ⁽¹⁾	.09	.19	.17	.13
1999				
Revenue	\$ 46,549	\$ 48,810	\$ 48,241	\$ 48,021
Gross margin	6,659	(5,367)	4,041	753
Operating income (loss)	2,563	(9,545)	(200)	(4,196)
Income (loss) from continuing operations	1,182	(6,075)	(602)	(3,393)
Gain on discontinued operations	-	1,362	-	-
Net income (loss)	1,182	(4,713)	(602)	(3,393)
Income (loss) from continuing operations per common share - diluted ⁽¹⁾	.16	(.83)	(.08)	(.46)
Gain on discontinued operations per common share - diluted ⁽¹⁾	-	.19	-	-
Net income (loss) per common share - diluted ⁽¹⁾	.16	(.64)	(.08)	(.46)

(1) Quarterly per share amounts may not equal annual amounts due to rounding.

See consolidated financial statements and related notes thereto included in the Company's Annual Report on form 10-K for the year ended December 31, 2000.

Consolidated Statements of Operation

For the years ended December 31, <i>(in thousands of dollars, except share and per share data)</i>	2000	1999	1998
Revenue			
Contract revenue	\$ 172,774	\$ 164,766	\$ 154,336
Product sales	27,401	26,855	28,008
<u>Total revenue</u>	<u>200,175</u>	<u>191,621</u>	<u>182,344</u>
Costs and expenses			
Cost of contract revenue	156,327	164,278	140,653
Cost of product sales	19,087	21,257	22,029
Selling, engineering and administrative expenses	15,558	17,464	17,203
<u>Total operating costs and expenses</u>	<u>190,972</u>	<u>202,999</u>	<u>179,885</u>
Operating income (loss)	9,203	(11,378)	2,459
Interest expense, net	1,842	2,255	1,612
Income (loss) from continuing operations before provision (benefit) for income taxes	7,361	(13,633)	847
Provision (benefit) for income taxes	3,008	(4,745)	356
Income (loss) from continuing operations	4,353	(8,888)	491
Gain (loss) from discontinued operations, net of tax benefit of \$1,989 in 1998	-	-	(3,890)
Gain (loss) on disposal of discontinued operations, net of tax expense of \$143 in 2000, \$835 in 1999 and tax benefit of \$1,576 in 1998	206	1,362	(2,572)
Gain (loss) from discontinued operations	206	1,362	(6,462)
Net income (loss)	\$ 4,559	\$ (7,526)	\$ (5,971)
Earnings (Loss) Per Share			
Per common share - basic			
Income (loss) from continuing operations	\$.57	\$ (1.21)	\$.07
Gain (loss) from discontinued operations	.03	.19	(.87)
<u>Net income (loss)</u>	<u>\$.60</u>	<u>\$ (1.02)</u>	<u>\$ (.80)</u>
Per common share - diluted			
Income (loss) from continuing operations	\$.56	\$ (1.21)	\$.06
Gain (loss) from discontinued operations	.03	.19	(.83)
<u>Net income (loss)</u>	<u>\$.59</u>	<u>\$ (1.02)</u>	<u>\$ (.77)</u>
Weighted Average Shares Outstanding			
Weighted average shares outstanding - basic	7,541,376	7,360,548	7,501,604
Dilutive effect of options	151,780	-	269,711
<u>Weighted average shares outstanding - diluted</u>	<u>7,693,156</u>	<u>7,360,548</u>	<u>7,771,315</u>

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Consolidated Balance Sheets

December 31, <i>(in thousands of dollars, except share and per share data)</i>	2000	1999
Assets		
Current assets		
Cash and cash equivalents	\$ 527	\$ 2,267
Receivables, net of allowances of \$1,096 in 2000 and \$790 in 1999	31,967	34,917
Unbilled expenditures and fees on contracts in process	24,633	18,609
Inventories	3,208	2,735
Prepaid expenses and other current assets	3,926	1,593
<u>Total current assets</u>	<u>64,261</u>	<u>60,121</u>
Net property, plant and equipment	14,441	15,067
<u>Total assets</u>	<u>\$ 78,702</u>	<u>\$ 75,188</u>
Liabilities and Stockholders' Equity		
Current liabilities		
Notes payable	\$ 5,784	\$ 19,700
Current portion of long term debt	500	-
Accounts payable	12,843	11,641
Accrued payroll and employee benefits	9,901	9,435
Other accrued expenses	5,711	7,840
Current deferred income taxes	4,575	1,575
Net liabilities of discontinued operations	-	273
<u>Total current liabilities</u>	<u>39,314</u>	<u>50,464</u>
Long term debt	9,250	-
Deferred income taxes	849	919
Commitments and contingencies		
Stockholders' equity		
Preferred stock, par value, \$.10 per share, 5,000,000 shares authorized, none issued	-	-
Common stock, par value, \$.10 per share:		
Authorized - 30,000,000 shares		
Issued - 8,980,945 shares in 2000 and 8,742,750 in 1999	898	874
Treasury stock - 1,379,426 shares in 2000 and 1999	(138)	(138)
Capital in excess of par value	28,461	27,560
Retained earnings (accumulated deficit)	68	(4,491)
<u>Total stockholders' equity</u>	<u>29,289</u>	<u>23,805</u>
<u>Total liabilities and stockholders' equity</u>	<u>\$ 78,702</u>	<u>\$ 75,188</u>

See consolidated financial statements and related notes thereto included in the company's Annual Report on Form 10-K for the year ended December 31, 2000.

Consolidated Statements of Cash Flows

For the years ended December 31, (in thousands of dollars)	2000	1999	1998
Cash Provided By (Used For) Operations			
Net income (loss)	\$ 4,559	\$ (7,526)	\$ (5,971)
Adjustments to reconcile net income (loss) to net cash provided by (used for) operating activities:			
(Gain) loss from discontinued operations	(206)	(1,362)	6,462
Non-cash stock compensation expense	114	116	–
Provision for impairment of investment in Empresa, Inc.	–	1,424	–
Depreciation and amortization	3,746	6,060	6,219
Deferred income tax provision	2,930	(5,043)	(1,347)
	11,143	(6,331)	5,363
Cash Provided By (Used For) Working Capital			
Receivables	2,950	(1,901)	(15,916)
Unbilled expenditures and fees on contracts in process	(6,024)	13,560	128
Inventories	(473)	(88)	730
Prepaid expenses and other current assets	(2,333)	(626)	1,568
Accounts payable	1,202	1,341	1,945
Accrued payroll and employee benefits	466	1,653	(199)
Other accrued expenses	(2,129)	5,210	(1,810)
	(6,341)	19,149	(13,554)
Net cash provided by (used for) continuing operations	4,802	12,818	(8,191)
Net cash used for discontinued operations	(67)	(1,833)	(3,215)
Net cash provided by (used for) operating activities	4,735	10,985	(11,406)
Cash Used For Investing Activities			
Additions to property, plant and equipment related to continuing operations	(3,120)	(2,702)	(2,874)
Additions to property, plant and equipment related to discontinued operations	–	–	(297)
Investments and acquisitions	–	(682)	(742)
Proceeds from the sale of discontinued operations	–	1,700	–
Net cash used for investing activities	(3,120)	(1,684)	(3,913)
Cash Provided By (Used For) Financing Activities			
Net borrowings (repayments) under revolving credit agreement	5,784	(7,100)	16,800
Repayment of working capital agreement	(19,700)	–	–
Proceeds from mortgage agreements	17,500	–	–
Repayment of interim mortgage	(7,500)	–	–
Principal payment under 10-year mortgage	(250)	–	–
Proceeds from the exercise of stock options	811	28	346
Purchase of treasury stock	–	(59)	(2,272)
Net cash provided by (used for) financing activities	(3,355)	(7,131)	14,874
Net increase (decrease) in cash and cash equivalents	(1,740)	2,170	(445)
Cash and cash equivalents at the beginning of the year	2,267	97	542
Cash and cash equivalents at the end of the year	\$ 527	\$ 2,267	\$ 97
Supplemental Information			
Cash paid for interest	\$ 2,055	\$ 2,451	\$ 1,640
Cash paid for taxes	\$ 2,893	\$ 199	\$ 150
Cashless options exercised	\$ –	\$ –	\$ 245

See consolidated financial statements and related notes thereto included in the company's Annual Report on Form 10-K for the year ended December 31, 2000.

Management's Responsibility for Financial Statements

The financial statements included in the company's Annual Report on Form 10-K for the year ended December 31, 2000, are the responsibility of the management of Dynamics Research Corporation and have been prepared in conformity with accounting principles generally accepted in the United States. The financial statements reflect judgments which management believes are appropriate to the circumstances. All other financial information in this report has been presented on a basis consistent with the information included in the financial statements.

Management of the company is responsible for maintaining a system of internal controls which provides reasonable assurance that the assets of the company are protected and that the financial statements present fairly the financial position and results of operations of the company. The internal control system is tested, monitored and revised when necessary.

The Audit Committee of the Board of Directors is composed of three directors of the company who are not members of management. The Audit Committee meets with management and the company's independent public accountants several times a year to review the results of external audits and to discuss plans for future audits. At these meetings the Audit Committee also meets privately with the independent public accountants.

The company's independent public accountants, Arthur Andersen LLP, audited the financial statements prepared by the management of Dynamics Research Corporation. Their report on these statements is included in the Annual Report on Form 10-K for the year ended December 31, 2000.



James P. Regan
President and Chief Executive Officer



David Keleher
Vice President and Chief Financial Officer

Report of Independent Public Accountants on Condensed Financial Statements

To Dynamics Research Corporation:

We have audited, in accordance with auditing standards generally accepted in the United States, the consolidated balance sheets of Dynamics Research Corporation (a Massachusetts Corporation) and subsidiaries as of December 31, 2000 and 1999, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the three years in the period ended December 31, 2000, appearing in the company's Annual Report on Form 10-K for the year ended December 31, 2000 (not presented herein). In our report dated February 5, 2001, also appearing in the Annual Report on Form 10-K, we expressed an unqualified opinion on those consolidated financial statements.

In our opinion, the information set forth in the accompanying consolidated balance sheets as of December 31, 2000 and 1999, and the related consolidated statements of operations and cash flows for each of the three years in the period ended December 31, 2000, is fairly stated, in all material respects, in relation to the consolidated financial statements from which it has been derived.



Arthur Andersen LLP
Boston, Massachusetts
February 5, 2001

Directors

John S. Anderegg, Jr.
Chairman
Dynamics Research Corporation

Dr. Francis J. Aguilar*
Professor of Business Administration, Emeritus
Harvard University, Graduate School of Business Administration

Martin V. Joyce, Jr.**
Vice President
A.T. Kearney, Inc.

Kenneth F. Kames*
Vice President (Retired), New Business Development,
The Gillette Company

General James P. Mullins*
USAF (Retired)

James P. Regan
President and Chief Executive Officer
Dynamics Research Corporation

* Member of the Audit Committee.
+ Member of the Compensation Committee.

Officers

James P. Regan
President and Chief Executive Officer

Barry L. Aldrich
Vice President and General Manager, Contracts

Richard Basque
Vice President and Director of Federal Information
Systems and Services

William G. Clautice
Vice President, Strategic Programs, Test Equipment Group

Richard A. Covel
Vice President and General Counsel

Chester Ju
Vice President and General Manager, Precision Manufacturing Group

David Keleher
Vice President and Chief Financial Officer

Thomas J. Kelly
Vice President and General Manager
Information Systems and Service Group

Lawrence O'Brien
Vice President and General Manager, Systems Engineering Group

David C. Proctor
Treasurer, Assistant Clerk

Richard P. Rappaport
Vice President and General Manager, Test Equipment Group

Robert Smith
Vice President and General Manager, Integrated Field Services Group

Robert D. Sykes
Vice President and Chief Information Officer

John L. Wilkinson
Vice President and General Manager, Human Resources

Auditors

Arthur Andersen LLP
225 Franklin Street Boston, Massachusetts 02110

Legal Counsel

Ropes & Gray
One International Place Boston, Massachusetts 02110

Transfer Agent

American Stock Transfer & Trust Company
59 Maiden Lane
New York, New York 10038
Telephone: (800) 937-5449

Stock Prices

	2000		1999	
	High	Low	High	Low
First quarter	\$ 8.38	\$ 6.94	\$ 7.19	\$ 2.88
Second quarter	8.63	7.00	6.63	4.25
Third quarter	8.53	6.75	6.25	3.50
Fourth quarter	9.25	7.13	9.50	3.94

The bid and ask prices of the company's common stock on February 13, 2001 were \$8.38 and \$8.44, respectively. Prices shown reflect inter-dealer prices, without retail mark-up, mark-down, or commission and may not necessarily represent actual transactions. Source: Monthly Statistical Report of the National Association of Securities Dealers, Inc. (NASDAQ).

Common Stock

The company's stock is traded on the NASDAQ Stock Market. The ticker symbol for the company's stock is DRCO. The company's common stock is commonly listed in newspapers as DynamR, DynRsh. or DynRsearch.

Number of Shareholders

The number of shareholders of record at February 13, 2001 was 787. As of February 13, 2001 there were 7,601,519 common shares outstanding.

Form 10-K

A copy of the company's Form 10-K, which is filed annually with the Securities and Exchange Commission, will be sent without charge to any shareholder requesting it in writing to the Treasurer's office, Dynamics Research Corporation, 60 Frontage Road, Andover, Massachusetts 01810-5498.

Annual Meeting

The 2001 Annual Meeting of Shareholders will be held at 1:30 PM on April 24, 2001 at the State Street Bank and Trust Building, 33rd floor, 225 Franklin Street, Boston, Massachusetts 02110.

Corporate Headquarters

60 Frontage Road
Andover, Massachusetts 01810-5498
Telephone: (978) 475-9090
Fax: (978) 475-8205
Internet: www.drc.com

Safe harbor statements under the Private Securities Litigation Reform Act of 1995: Some statements contained or implied in this annual report which are not historical fact such as financial forecasts contain forward-looking information. These statements may be identified by forward-looking words such as "expect," "look," "believe," "anticipate," "may," "will" and other forward-looking terminology. Such statements are subject to risks and uncertainties that could cause actual results to differ materially, including uncertainties regarding contractual requirements, actions by customers and actual costs to complete; federal budget matters; government contracting risks, competitive market conditions; customer requirements, schedules and related funding; technological change; uncertainty of future financing; overall economic factors; ability to successfully complete and integrate acquisitions and other matters discussed in the company's filings with the SEC. These factors are discussed in more detail in the company's most recent Annual Report on Form 10-K. The Company assumes no obligation to update any forward-looking information.

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Other Company Offices

Alabama

Madison (256) 772-6509
Daleville (334) 503-1748
Enterprise (334) 308-5361
Montgomery (334) 271-5558

Arkansas

Little Rock (501) 682-2094

California

San Diego (619) 523-3660

Colorado

Denver (303) 376-3200
Colorado Springs (719) 574-0350

Florida

Orlando (407) 380-1200
Shalimar (850) 651-8155

Georgia

Warner Robins (912) 918-0268

Illinois

Scott AFB (618) 744-9412

Kansas

Leavenworth (913) 758-1551

Maryland

California (301) 737-7699

Massachusetts

Technical Services Group

Bedford (781) 687-9603

Test Equipment Group

West Newton (617) 965-1346

Precision Manufacturing Group, Metrigraphics and Encoder Divisions

Wilmington (978) 658-6100

Missouri

St. Ann (314) 291-7522

New Hampshire

Concord (603) 271-0947

New Mexico

Albuquerque (505) 292-5562

New York

Mitchel Field (516) 228-1614

Ohio

Fairborn (937) 429-0055
Columbus (614) 294-1731

Oklahoma

Midwest City (405) 741-7775

Texas

San Antonio (210) 375-1350

Utah

Layton (801) 775-0900

Virginia

Arlington (703) 412-2812
Alexandria (703) 329-7888
Hampton (757) 838-9075



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