FREQUENCY ELECTRONICS INC
Form 10-Q
December 15, 2010

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

(Mark one)

x QUARTERLY REPORT PURSUANT TO SECTION 13 or 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the Quarterly Period ended October 31, 2010

OR

o TRANSITION REPORT PURSUANT TO SECTION 13 or 15 (d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the transition period from __________ to __________

Commission File No. 1-8061

FREQUENCY ELECTRONICS, INC.
(Exact name of Registrant as specified in its charter)

Delaware (State or other jurisdiction of incorporation or organization)	11-1986657 (I.R.S. Employer Identification No.)
55 CHARLES LINDBERGH BLVD., MITCHEL FIELD, N.Y. (Address of principal executive offices)	11553 (Zip Code)

Registrant's telephone number, including area code: 516-794-4500

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

Indicate by check mark whether the registrant has submitted electronically and posted on its corporate Web site, if any, every Interactive Data File required to be submitted and posted pursuant to Rule 405 of Regulation S-T during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files). Yes o No o

Indicate by check mark whether the registrant is a large accelerated filer, an accelerated filer, a non-accelerated filer or a smaller reporting company. See the definitions of “large accelerated filer,” “accelerated filer” and smaller reporting company in Rule 12b-2 of the Exchange Act. (Check one):

Large accelerated filer o Accelerated filer o Non-accelerated filer o Smaller Reporting Company x
(do not check if a smaller reporting company)

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

The number of shares outstanding of Registrant's Common Stock, par value $1.00 as of December 10, 2010 – 8,256,350

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

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FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES
Condensed Consolidated Balance Sheets

	October 31, 2010 (UNAUDITED)	April 30, 2010 (AUDITED) (NOTE A)
	(In thousands except share data)	
ASSETS:		
Current assets:		
Cash and cash equivalents	$ 7,384	$ 9,954
Marketable securities	11,577	10,418
Accounts receivable, net of allowance for doubtful accounts of $258 at October 31, 2010 and $266 at April 30, 2010	11,855	10,504
Costs and estimated earnings in excess of billings, net	2,466	1,667
Inventories, net	28,954	26,975
Prepaid income taxes	255	-
Prepaid expenses and other	1,141	1,122
Total current assets	63,632	60,640
Property, plant and equipment, at cost, less accumulated depreciation and amortization	6,811	7,015
Goodwill and other intangible assets	218	218
Cash surrender value of life insurance and cash held in trust	9,181	8,917
Investment in and loans receivable from affiliates	3,841	3,813
Other assets	817	817
Total assets	$ 84,500	$ 81,420
LIABILITIES AND STOCKHOLDERS' EQUITY:		
Current liabilities:		
Short-term credit and lease obligations	$ 254	$ 246
Accounts payable - trade	2,496	1,720
Income taxes payable	-	295
Accrued liabilities	5,043	5,047
Total current liabilities	7,793	7,308
Lease obligation- noncurrent	313	441
Deferred compensation	9,737	9,624
Deferred rent and other liabilities	703	664
Total liabilities	18,546	18,037
Commitments and contingencies		
Stockholders' equity:		
Preferred stock - $1.00 par value	-	-
Common stock - $1.00 par value	9,164	9,164
Additional paid-in capital	49,763	49,580
Retained earnings	6,106	5,271
	65,033	64,015
	(4,379)	(4,651)

Common stock reacquired and held in treasury - at cost (907,590 shares at October 31, 2010 and 946,172 shares at April 30, 2010)				
Accumulated other comprehensive income		5,300		4,019
Total stockholders' equity		65,954		63,383
Total liabilities and stockholders' equity	$	84,500	$	81,420

See accompanying notes to condensed consolidated financial statements.

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

Condensed Consolidated Statements of Operations

Six Months Ended October 31,
(Unaudited)

	2010		2009	
	(In thousands except per share data)			
Revenues	$	24,652	$	23,836
Cost of revenues		15,102		15,141
Gross margin		9,550		8,695
Selling and administrative expenses		5,560		5,340
Research and development expense		2,389		2,454
Operating profit		1,601		901
Other income (expense):				
Investment income		179		253
Equity income (loss)		28		(195)
Impairment of investment in affiliate		-		(200)
Interest expense		(64)		(78)
Other expense, net		(89)		(156)
Income before provision for income taxes		1,655		525
Provision for income taxes		820		-
Net income	$	835	$	525
Net income per common share				
Basic	$	0.10	$	0.06
Diluted	$	0.10	$	0.06
Weighted average shares outstanding				
Basic		8,242,481		8,172,643
Diluted		8,302,405		8,184,764

See accompanying notes to consolidated condensed financial statements.

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

Condensed Consolidated Statements of Operations

Three Months Ended October 31,
(Unaudited)

	2010	2009
	(In thousands except per share data)	
Revenues	$ 12,528	$ 11,395
Cost of revenues	7,724	7,001
Gross margin	4,804	4,394
Selling and administrative expenses	2,765	2,773
Research and development expense	1,227	1,379
Operating profit	812	242
Other income (expense):		
Investment income	99	125
Equity loss	(1)	(145)
Impairment of investment in affiliate	-	(200)
Interest expense	(29)	(34)
Other expense, net	(83)	(117)
Income (loss) before provision for income taxes	798	(129)
Provision for income taxes	470	-
Net income (loss)	$ 328	$ (129)
Net income (loss) per common share		
Basic	$ 0.04	$ (0.02)
Diluted	$ 0.04	$ (0.02)
Weighted average shares outstanding		
Basic	8,251,391	8,180,659
Diluted	8,323,303	8,180,659

See accompanying notes to condensed consolidated financial statements.

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

Condensed Consolidated Statements of Cash Flows

Six Months Ended October 31,
(Unaudited)

	2010	2009
	(In thousands)	
Cash flows from operating activities:		
Net income	$ 835	$ 525
Non-cash charges to earnings and non-operating income or loss, net	1,988	2,541
Net changes in operating assets and liabilities	(4,665)	(406)
Net cash (used in) provided by operating activities	(1,842)	2,660
Cash flows from investing activities:		
Proceeds from sale of marketable securities and investments	1,500	-
Purchase of marketable securities	(2,500)	-
Purchase of fixed assets	(694)	(280)
Net cash used in investing activities	(1,694)	(280)
Cash flows from financing activities:		
Payment of short-term credit and lease obligations	(120)	(1,243)
Net cash used in financing activities	(120)	(1,243)
Net (decrease) increase in cash and cash equivalents before effect of exchange rate changes	(3,656)	1,137
Effect of exchange rate changes on cash and cash equivalents	1,086	(349)
Net (decrease) increase in cash and cash equivalents	(2,570)	788
Cash and cash equivalents at beginning of period	9,954	4,911
Cash and cash equivalents at end of period	$ 7,384	$ 5,699
Supplemental disclosures of cash flow information:		
Cash paid during the period for:		
Interest	$ 60	$ 40
Income Taxes	$ 1,370	-

See accompanying notes to condensed consolidated financial statements.

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements
(Unaudited)

NOTE A - CONSOLIDATED FINANCIAL STATEMENTS

In the opinion of management of Frequency Electronics, Inc. (“the Company”), the accompanying unaudited condensed consolidated interim financial statements reflect all adjustments (which include only normal recurring adjustments) necessary to present fairly, in all material respects, the consolidated financial position of the Company as of October 31, 2010 and the results of its operations and cash flows for the six and three months ended October 31, 2010 and 2009. The April 30, 2010 condensed consolidated balance sheet was derived from audited financial statements. Certain information and footnote disclosures normally included in financial statements prepared in accordance with generally accepted accounting principles have been condensed or omitted. These condensed consolidated financial statements should be read in conjunction with the financial statements and notes thereto included in the Company's April 30, 2010 Annual Report to Stockholders on Form 10-K. The results of operations for such interim periods are not necessarily indicative of the operating results for the full fiscal year.

NOTE B - EARNINGS PER SHARE

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

	Six months		Three months	
	Periods ended October 31,			
	2010	2009	2010	2009
Weighted average shares outstanding:				
Basic	8,242,481	8,172,643	8,251,391	8,180,659
Effect of dilutive securities	59,924	12,121	71,912	***
Diluted	8,302,405	8,184,764	8,323,303	8,180,659

*** Dilutive securities are excluded for the three month period ended October 31, 2009 since the inclusion of such shares would be antidilutive due to the net loss for the period then ended.

Dilutive securities consist of unexercised stock options and stock appreciation rights (“SARS”). The computation of diluted shares outstanding excludes those options and SARS with an exercise price in excess of the average market price of the Company’s common shares during the periods presented. The inclusion of such options and SARS in the computation of earnings per share would have been antidilutive. The number of excluded options and SARS were:

	Six months		Three months	
	Periods ended October 31,			
	2010	2009	2010	2009
Outstanding options and SARS excluded	966,775	869,213	966,775	869,213

NOTE C – COSTS AND ESTIMATED EARNINGS IN EXCESS OF BILLINGS, NET

At October 31, 2010 and April 30, 2010, costs and estimated earnings in excess of billings, net, consist of the following:

	October 31, 2010	April 30, 2010
	(In thousands)	
Costs and estimated earnings in excess of billings	$ 3,814	$ 2,917
Billings in excess of costs and estimated earnings	(1,348)	(1,250)
Net asset	$ 2,466	$ 1,667

Such amounts represent revenue recognized on long-term contracts that had not been billed at the balance sheet dates or represent a liability for amounts billed in excess of the revenue recognized. Amounts are billed to customers pursuant to contract terms. In general, the recorded amounts will be billed and collected or revenue recognized within twelve months of the balance sheet date. Revenue on these long-term contracts is accounted for on the percentage of completion basis. During the six and three months ended October 31, 2010, revenue recognized under percentage of completion contracts was approximately $10.5 million and $5.5 million, respectively. For the six and three months ended October 31, 2009, such revenue was approximately $9.7 million and $5.1 million, respectively.

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements
(Unaudited)

NOTE D - INVENTORIES

Inventories, which are reported at the lower of cost or market at October 31, 2010 and April 30, 2010, respectively, consist of the following:

	October 31, 2010	April 30, 2010
	(In thousands)	
Raw Materials and Component Parts	$ 11,679	$ 13,192
Work in Progress	14,224	11,039
Finished Goods	3,051	2,744
	$ 28,954	$ 26,975

As of October 31, 2010 and April 30, 2010, approximately $18.6 million and $18.2 million, respectively, of total inventory is located in the United States, approximately $9.6 million and $7.9 million, respectively, is located in Belgium and approximately $800,000 and $900,000, respectively, is located in China.

NOTE E – COMPREHENSIVE INCOME

For the six and three months ended October 31, 2010 and 2009, comprehensive income is composed of (in thousands):

	Six months		Three months	
	Periods ended October 31,			
	2010	2009	2010	2009
Net income (loss)	$ 835	$ 525	$ 328	$ (129)
Foreign currency translation adjustment	1,082	644	2,012	272
Change in market value of marketable securities	199	834	113	511
Comprehensive income	$ 2,116	$ 2,003	$ 2,453	$ 654

NOTE F – SEGMENT INFORMATION

The Company operates under three reportable segments based on the geographic locations of its subsidiaries:

(1) FEI-NY – operates out of New York and its operations consist principally of precision time and frequency control products used in three principal markets- communication satellites (both commercial and U.S. Government-funded); terrestrial cellular telephone or other ground-based telecommunication stations and other components and systems for the U.S. military.

(2) Gillam-FEI - operates out of Belgium and France and primarily sells wireline synchronization and network management systems in non-U.S. markets. All sales from Gillam-FEI to the United States are to other segments of the Company.

(3) FEI-Zyfer – operates out of California and its products incorporate Global Positioning System (GPS) technologies into systems and subsystems for secure communications, both government and commercial, and other locator applications. This segment also provides sales and support for the Company's wireline telecommunications family of products, including US5G, which are sold in the United States market.

The FEI-NY segment also includes the operations of the Company's wholly-owned subsidiary, FEI-Asia. FEI-Asia functions primarily as a manufacturing facility for the FEI-NY segment.

The Company's Chief Executive Officer measures segment performance based on total revenues and profits generated by each geographic location rather than on the specific types of customers or end-users. Consequently, the Company determined that the segments indicated above most appropriately reflect the way the Company's management views the business.

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements
(Unaudited)

The table below presents information about reported segments with reconciliation of segment amounts to consolidated amounts as reported in the statement of operations or the balance sheet for each of the periods (in thousands):

	Six months		Three months	
	Periods ended October 31,			
	2010	2009	2010	2009
Revenues:				
FEI-NY	$ 15,168	$ 14,014	$ 7,527	$ 6,949
Gillam-FEI	5,203	4,975	2,230	2,501
FEI-Zyfer	5,657	6,828	3,160	2,579
less intersegment revenues	(1,376)	(1,981)	(389)	(634)
Consolidated revenues	$ 24,652	$ 23,836	$ 12,528	$ 11,395
Operating profit (loss):				
FEI-NY	$ 1,465	$ 624	$ 565	$ 538
Gillam-FEI	40	(5)	(76)	14
FEI-Zyfer	290	485	451	(171)
Corporate	(194)	(203)	(128)	(139)
Consolidated operating profit	$ 1,601	$ 901	$ 812	$ 242

	October 31, 2010	April 30, 2010
Identifiable assets:		
FEI-NY (approximately $3.6 million in China)	$ 35,854	$ 35,462
Gillam-FEI (all in Belgium or France)	21,345	19,594
FEI-Zyfer	7,741	7,413
less intersegment balances	(13,365)	(14,655)
Corporate	32,925	33,606
Consolidated identifiable assets	$ 84,500	$ 81,420

NOTE G – RELATED PARTY TRANSACTIONS

The Company has equity interests in two strategically important companies: Elcom Technologies, Inc. ("Elcom") and Morion Inc. ("Morion"), accounted for on the equity and cost basis, respectively. During the six and three month periods ended October 31, 2010 and 2009, the Company acquired technical services from Elcom, purchased crystal oscillator products from Morion and sold certain of its products to both companies. The Company also receives interest from Elcom under two notes receivable. The table below summarizes these transactions:

	Six months		Three months	
	Periods ended October 31,			
	2010	2009	2010	2009
	(in thousands)			
Purchases from:				
Elcom	$ 314	$ 6	$ 279	$ -
Morion	37	212	20	16
Sales to:				

Elcom	$	133	$	1	$	75	$	1
Morion		200		32		72		11
Interest on Elcom notes receivable	$	47	$	24	$	22	$	12

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements
(Unaudited)

The Company measures the current market value of Elcom based on comparisons to comparable companies as well as Elcom's forecasts of future financial results. For the year ended April 30, 2010, in addition to its equity share in the income or loss of Elcom during the year, the Company determined that its investment was impaired and recorded impairment charges in the amount $550,000 for fiscal year 2010, of which $200,000 was recorded during the six and three months ended October 31, 2009. No impairment charges were recorded during the six and three months ended October 31, 2010.

NOTE H – FAIR VALUE OF FINANCIAL INSTRUMENTS

The cost, gross unrealized gains, gross unrealized losses and fair market value of available-for-sale securities at October 31, 2010 and April 30, 2010 are as follows (in thousands):

	October 31, 2010			
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Market Value
Fixed income debt securities	$ 10,566	$ 354	$ (24)	$ 10,896
Equity securities	450	231	-	681
	$ 11,016	$ 585	$ (24)	$ 11,577

	April 30, 2010			
	Cost	Gross Unrealized Gains	Gross Unrealized Losses	Fair Market Value
Fixed income debt securities	$ 9,606	$ 261	$ (90)	$ 9,777
Equity securities	450	191	-	641
	$ 10,056	$ 452	$ (90)	$ 10,418

The following table presents the fair value and unrealized losses, aggregated by investment type and length of time that individual securities have been in a continuous unrealized loss position:

	Less than 12 months		12 Months or more		Total	
	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses	Fair Value	Unrealized Losses
October 31, 2010						
Fixed income debt securities	$ 1,515	$ (4)	$ 980	$ (20)	$ 2,495	$ (24)
Equity securities	-	-	-	-	-	-
	$ 1,515	$ (4)	$ 980	$ (20)	$ 2,495	$ (24)
April 30, 2010						
Fixed income debt securities	$ -	$ -	$ 3,438	$ (90)	$ 3,438	$ (90)
Equity securities	-	-	-	-	-	-
	$ -	$ -	$ 3,438	$ (90)	$ 3,438	$ (90)

The Company regularly reviews its investment portfolio to identify and evaluate investments that have indications of possible impairment. The Company does not believe that its investments in marketable securities with unrealized losses at October 31, 2010 are other-than-temporary due to market volatility of the security's fair value, analysts' expectations and the Company's ability to hold the securities for a period of time sufficient to allow for any anticipated recoveries in market value.

During the six months ended October 31, 2010, the Company redeemed an available-for-sale security in the amount of $1,500,000 and realized a loss of $27,800 on the transaction which is included in the determination of net income for the period. During the six and three months ended October 31, 2009, the Company did not sell or redeem any available-for-sale securities. Accordingly, there were no realized gains or losses included in the determination of net income for that period.

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements
(Unaudited)

Maturities of fixed income debt securities, which include corporate and government agency debt securities classified as available-for-sale at October 31, 2010 are as follows, at cost (in thousands):

Current	$ 1,000
Due after one year through five years	7,066
Due after five years through ten years	2,500
	$ 10,566

The fair value accounting framework provides a fair value hierarchy that prioritizes the inputs to valuation techniques used to measure fair value. The hierarchy gives the highest priority to unadjusted quoted prices in active markets for identical assets or liabilities (level 1 measurements) and the lowest priority to unobservable inputs (level 3 measurements). The three levels of the fair value hierarchy are described below:

Level 1 Inputs to the valuation methodology are unadjusted quoted prices for identical assets or liabilities in active markets that the Company has the ability to access.

Level 2 Inputs to the valuation methodology include:
- Quoted prices for similar assets or liabilities in active markets;
- Quoted prices for identical or similar assets or liabilities in inactive markets
- Inputs other than quoted prices that are observable for the asset or liability;
- Inputs that are derived principally from or corroborated by observable market data by correlation or other means.

Level 3 Inputs to the valuation methodology are unobservable and significant to the fair value measurement.

The asset's or liability's fair value measurement level within the fair value hierarchy is based on the lowest level of any input that is significant to the fair value measurement. Valuation techniques used need to maximize the use of observable inputs and minimize the use of unobservable inputs. All of the Company's investments in marketable securities are Level 1 assets whereby fair value has been determined from quoted market prices.

NOTE I - RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

In June 2009, the FASB issued standards which modified how a company determines when an entity that is insufficiently capitalized or is not controlled through voting (or similar rights) should be consolidated. These standards clarify that the determination of whether a company is required to consolidate an entity is based on, among other things, an entity's purpose and design and a company's ability to direct the activities of the entity that most significantly impact the entity's economic performance. These standards require an ongoing reassessment of whether a company is the primary beneficiary of a variable interest entity. These standards also require additional disclosures about a company's involvement in variable interest entities and any significant changes in risk exposure due to that involvement. These standards are effective for fiscal years beginning after November 15, 2009 and were effective for the Company on May 1, 2010. The adoption of these standards did not have a material impact on the financial condition, results of operations, cash flows and disclosures of the Company.

NOTE J – INCOME TAXES

The Company has established a valuation allowance against all the deferred tax assets of its domestic and foreign subsidiaries. Because of the full valuation allowance, the provision for income taxes consists solely of taxes currently due to taxing authorities in the United States. Any tax provision or benefit realized from temporary tax differences is offset by increases or decreases in the valuation allowance thus creating a difference from a normally expected effective tax rate. For the six and three months ended October 31, 2010, the deferred tax asset valuation allowance increased by approximately $100,000 to $8.2 million. In future periods, the valuation allowance may be reduced if the Company's current positive earnings are sufficient to offset past losses for purposes of predicting future utilization of deferred tax assets.

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES

Notes to Condensed Consolidated Financial Statements
(Unaudited)

NOTE K – TREASURY STOCK TRANSACTIONS

During the six month period ended October 31, 2010, the Company made a contribution of 38,582 shares of its common stock held in treasury to the Company's profit sharing plan and trust under section 401(k) of the Internal Revenue Code. Such contribution is in accordance with the Company's discretionary match of employee voluntary contributions to this plan.

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

"Safe Harbor" Statement under the Private Securities Litigation Reform Act of 1995:

The statements in this quarterly report on Form 10-Q regarding future earnings and operations and other statements relating to the future constitute "forward-looking" statements pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. The words "believe," "may," "will," "could," "should," "would," "anticipate," "estimate," "expect," "project," "intend," "objective," "seek," "strive," "might," "likely result," "build," "grow," "plan," "goal," "expand," "position," or similar words, or the negatives of these words, or similar terminology, identify forward-looking statements. These statements are based on assumptions that the Company believes are reasonable, but are subject to a wide range of risks and uncertainties, and a number of factors could cause the Company's actual results to differ materially from those expressed in the forward-looking statements referred to above. Factors that would cause or contribute to such differences include, but are not limited to, continued acceptance of the Company's products in the marketplace, competitive factors, new products and technological changes, product prices and raw material costs, dependence upon third-party vendors, competitive developments, changes in manufacturing and transportation costs, changes in contractual terms, the availability of capital, and other risks detailed in the Company's periodic report filings with the Securities and Exchange Commission. Readers are cautioned not to place undue reliance on these forward-looking statements, which relate only to events as of the date on which the statements are made and which reflect management's analysis, judgments, belief, or expectation only as of such date. By making these forward-looking statements, the Company undertakes no obligation to update these statements for revisions or changes after the date of this report.

Critical Accounting Policies and Estimates

The Company's significant accounting policies are described in Note 1 to the consolidated financial statements included in the Company's April 30, 2010 Annual Report to Stockholders. The Company believes its most critical accounting policies to be the recognition of revenue and costs on production contracts and the valuation of inventory. Each of these areas requires the Company to make use of reasoned estimates including estimating the cost to complete a contract, the realizable value of its inventory or the market value of its products. Changes in estimates can have a material impact on the Company's financial position and results of operations.

Revenue Recognition

Revenues under larger, long-term contracts which generally require billings based on achievement of milestones rather than delivery of product, are reported in operating results using the percentage of completion method. On fixed-price contracts, which are typical for commercial and U.S. Government satellite programs and other long-term U.S. Government projects, and which require initial design and development of the product, revenue is recognized on the cost-to-cost method. Under this method, revenue is recorded based upon the ratio that incurred costs bear to total estimated contract costs with related cost of sales recorded as the costs are incurred. Each month management reviews estimated contract costs through a process of aggregating actual costs incurred and updating estimated costs to completion based upon the current available information and status of the contract. The effect of any change in the estimated gross margin percentage for a contract is reflected in revenues in the period in which the change is known. Provisions for anticipated losses on contracts are made in the period in which they become determinable.

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES
(Continued)

On production-type orders, revenue is recorded as units are delivered with the related cost of sales recognized on each shipment based upon a percentage of estimated final program costs. Changes in job performance may result in revisions to costs and income and are recognized in the period in which revisions are determined to be required. Provisions for anticipated losses on contracts are made in the period in which they become determinable.

For customer orders in the Company's Gillam-FEI and FEI-Zyfer segments or smaller contracts or orders in the FEI-NY segment, sales of products and services to customers are reported in operating results based upon (i) shipment of the product or (ii) performance of the services pursuant to terms of the customer order. When payment is contingent upon customer acceptance of the installed system, revenue is deferred until such acceptance is received and installation completed.

Costs and Expenses

Contract costs include all direct material, direct labor costs, manufacturing overhead and other direct costs related to contract performance. Selling, general and administrative costs are charged to expense as incurred.

Inventory

In accordance with industry practice, inventoried costs contain amounts relating to contracts and programs with long production cycles, a portion of which will not be realized within one year. Inventory write downs are established for slow-moving and obsolete items and are based upon management's experience and expectations for future business. Any changes arising from revised expectations are reflected in cost of sales in the period the revision is made.

Marketable Securities

Marketable securities consist of investments in common stocks, corporate debt securities and debt securities of U.S. government agencies which trade on public markets with current prices readily available (Level 1 securities in the fair value hierarchy). Investments in debt and equity securities are categorized as available for sale and are carried at fair value, with unrealized gains and losses excluded from income and recorded directly to stockholders' equity. The market value of these investments may temporarily decline due to economic conditions, but the Company's own financial strength enables it to wait for such securities to recover their value or to mature such that any interim unrealized losses are deemed to be temporary. The Company recognizes gains or losses when securities are sold using the specific identification method.

FREQUENCY ELECTRONICS, INC. and SUBSIDIARIES
(Continued)

RESULTS OF OPERATIONS

The table below sets forth for the respective periods of fiscal years 2011 and 2010 the percentage of consolidated revenues represented by certain items in the Company's consolidated statements of operations:

	Six months		Three months	
	Periods ended October 31,			
	2010	2009	2010	2009
Revenues				
FEI-NY	61.5%	58.8%	60.1%	61.0%
Gillam-FEI	21.1	20.9	17.8	21.9
FEI-Zyfer	22.9	28.6	25.2	22.6
Less intersegment revenues	(5.5)	(8.3)	(3.1)	(5.5)
	100.0	100.0	100.0	100.0
Cost of revenues	61.3	63.5	61.6	61.4
Gross Margin	38.7	36.5	38.4	38.6
Selling and administrative expenses	22.5	22.4	22.1	24.4
Research and development expenses	9.7	10.3	9.8	12.1
Operating Profit	6.5	3.8	6.5	2.1
Other income (expense), net	0.2	(1.6)	(0.1)	(3.2)
Pretax Income (Loss)	6.7	2.2	6.4	(1.1)
Provision for income taxes	3.3	-	3.8	-
Net Income (Loss)	3.4%	2.2%	2.6%	(1.1)%

(Note: All dollar amounts in following tables are in thousands, except Revenues which are in millions)

Revenues (in millions)

	Six months				Three months			
	Periods ended October 31,							
Segment	2010	2009	Change		2010	2009	Change	
FEI-NY	$ 15.2	$ 14.0	$ 1.2	8%	$ 7.5	$ 6.9	$ 0.6	8%
Gillam-FEI	5.2	5.0	0.2	5%	2.2	2.5	(0.3)	(11)%
FEI-Zyfer	5.6	6.8	(1.2)	(17)%	3.2	2.6	0.6	22%
Intersegment revenues	(1.4)	(2.0)	0.6		(0.4			