



2011
Annual
Report

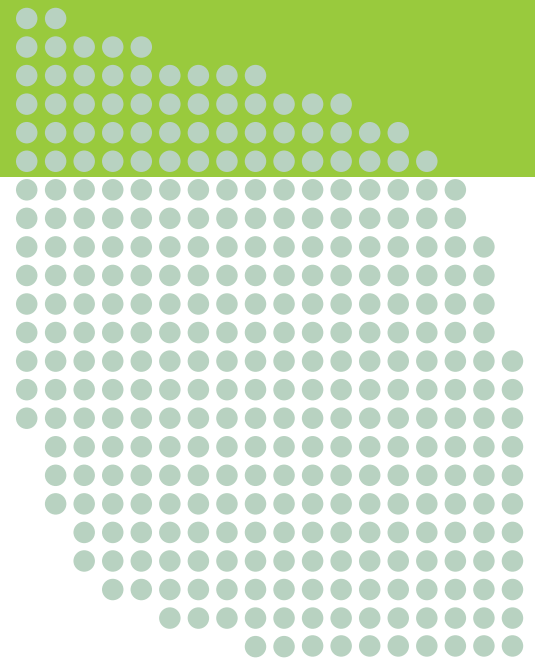
Growth & Innovation

SONO•TEK Corporation

A pictorial history of Sono-Tek ultrasonic nozzle technology shows one of our earliest nozzles (far left), followed by several generations of titanium nozzle designs, ending on the right with our latest addition, the Gold Series nozzle, engineered with a new proprietary chemically resistant material.

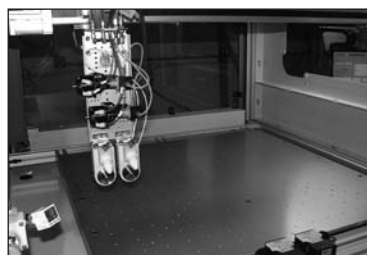


Company Profile: Sono-Tek is a green technology company, manufacturing precision ultrasonic nozzle systems since 1975. The Company's headquarters are in Milton, NY USA, with distributors in dozens of countries worldwide. Our coating systems serve a wide variety of industries and applications, including printed circuit board manufacturing, advanced energy coatings for fuel cell and solar cell technologies, precision medical device coatings, float glass and panel glass manufacturing, and food and food packaging. Our ultrasonic nozzles produce soft, atomized spray patterns ranging from half a millimeter wide to six hundred millimeters wide with a single nozzle. Unlimited width spray patterns are achieved with multiple nozzle systems. Our customers benefit from up to eighty percent reduction in sprayed liquids with more uniform spray patterns than conventional spraying systems. Reduced exhaust and cleanup requirements from overspray enable our customers to achieve immediate, significant cost savings while improving functional coatings.



2011 Corporate Highlights

- Strongest growth in Company's history, up 37% to nearly \$10m in sales
- Over seven fold increase in net profit, to almost \$600k and \$.04 per share
- Record backlog heading into new fiscal year
- Purchase of the Industrial Park where we were leasing to insure space for current and future growth
- Significant growth in alternative energy coating applications, both fuel cells and solar energy
- Continued success and growth in implantable medical device coating sales
- Maintained minimal debt levels and grew cash balance
- Expansion of glass line coating applications into new markets
- Strong recovery in electronics printed circuit board fluxing applications
- Continued balance sheet strength



Recent press releases: *June 6, 2011* - Sono-Tek Corporation announced expansion of customer services with new laboratory facilities in China, Korea, Germany and Taiwan. Available laboratory equipment will include fully enclosed 3 axis programmable coating systems with a multitude of fixturing, heating and vacuum options, and a variety of different nozzle configurations. Sono-Tek's new labs in Asia and Europe will be staffed and managed by the local Sono-Tek distributors, with the added advantage of native language support and geographic proximity. The addition of these new laboratories extends Sono-Tek's global reach and ability to provide superior customer service, while still offering a full range of testing services in their New York laboratory. The new labs will be up and running at all locations by mid 2011.

May 23, 2011 - Sono-Tek Corporation (OTCQB: SOTK) announced record sales of \$9,914,312 for the fiscal year ended February 28, 2011, compared to sales of \$7,242,324 for the previous fiscal year, an increase of 37%. Sales increased versus last year due to growth in the advanced energy markets involving coating systems for fuel cells and solar energy devices, sales of coating systems for glass and non-woven fabric manufacturers, and the resurgence and increase of our spray fluxing business worldwide. The Company also announced net income of \$593,945 or \$.04 per share for the year, versus \$81,676 for the previous year, an increase of \$512,269 or 627%.

According to Dr. Christopher L. Coccio, Sono-Tek's Chairman and CEO, "Looking ahead, based on our existing backlog, we expect to see similar continued sales growth and profitability in the new fiscal year. In addition, we are in the process of making a major purchase of a new CNC lathe machine to handle our greater production volume in house, rather than outsourcing it. We expect this purchase to lead to greater profitability, timeliness, and quality control in our manufacturing operation."

December 17, 2010 - Sono-Tek Corporation announced it purchased the Milton Industrial Park. The Milton Industrial Park, located in Milton, NY, is an improved 3.13 acre parcel of land comprised of five buildings of office/industrial space, with 50,000 square feet of gross leasable floor area. Sono-Tek currently occupies approximately 19,000 square feet of the industrial park. The acquisition of the park was financed with a cash down-payment of \$400,000 and the balance of \$2,100,000 in seller financing to be repaid over 20 years.

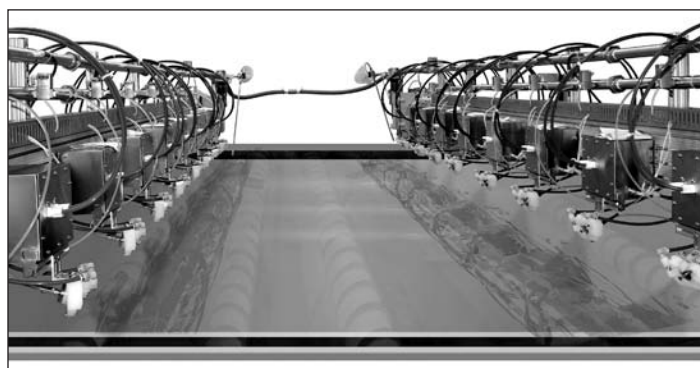


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2011 Financial Highlights

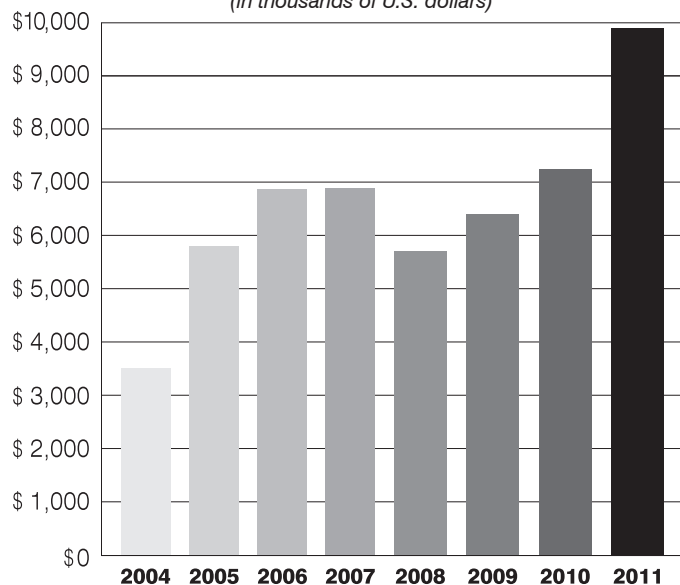
We had our strongest year ever in terms of growth, showing gains in providing coating systems for printed circuit board fabrication, implantable medical devices, glass manufacturing, and advanced energy applications involving solar cells and fuel cells. We added staff and manufacturing space, and then purchased the industrial park we have resided in for two decades to insure space for future growth without a disruptive move. Our products and the benefits of our ultrasonic atomization spraying and coating systems are winning increasing acceptance as the smart way to reduce the use and cost of expensive liquid coatings, dramatically reduce environmental impact, and produce a more precise and uniform coating. We are now achieving our goal of seeing significant repeat business in a number of these markets, which promises continued growth going forward.

SALES - Our sales this year were up by \$2.7m or 37%, which follows double digit growth in our last two fiscal years. This result was largely due to the success of our diversification program of two years ago which allowed us to sell new products into new market segments and global geographies. This latest annual sales level sets a new and significant record for the Company, as it has been achieved as a result of a multiyear investment in sales and engineering resources and programs rather than a market recovery in existing markets. We expect to see continued returns on the investments we made—and continue to make—in terms of further sales growth in the current fiscal year. Nearly a quarter of our sales were attributable to the new areas of organic growth that we developed in the past two years.

INCOME - We reported a profit of \$594k this year, in contrast to \$82k for the previous fiscal year. This dramatic improvement was due to a combination of increased sales from the diversification program combined with strong recovery and growth into new markets in our electronics segment. We made significant investments for the future of the Company two years ago during FY 2009, rather than taking a more cautious approach during the recession. The exciting turnaround in the result shown on the income chart speaks for itself, and we expect a further increase in net income during the present fiscal year.

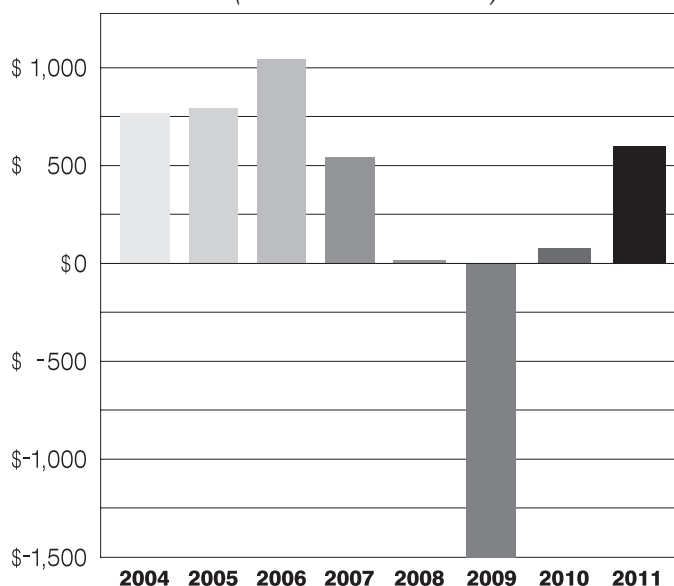
SALES CHART FY 2004 - 2011

(in thousands of U.S. dollars)



INCOME CHART FY 2004 - 2011

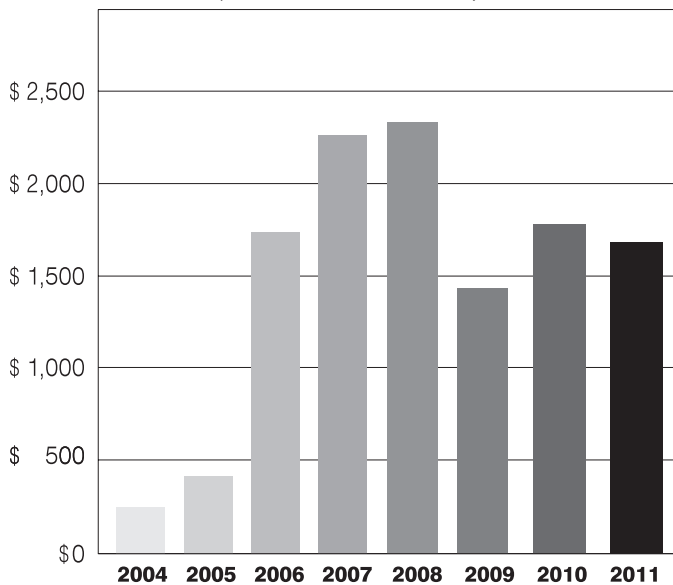
(in thousands of U.S. dollars)





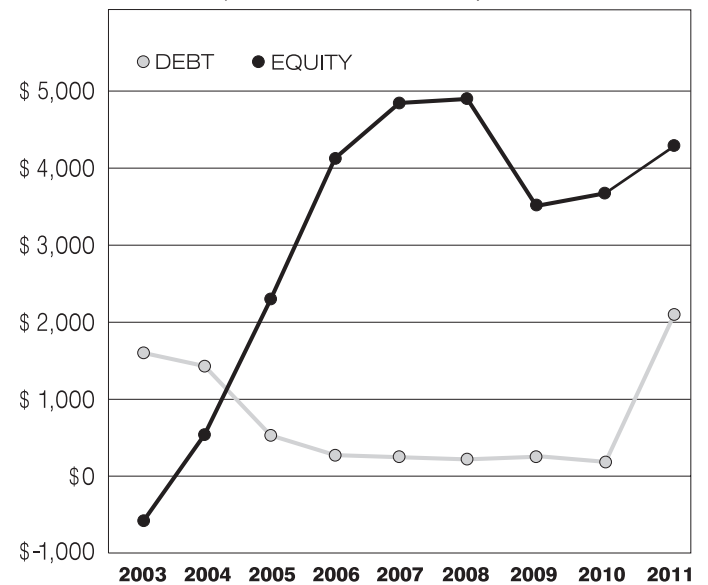
CASH - We maintained our cash this year as a result of improving profitable operations even though we used some cash as down payment for the purchase of the industrial park, and fully paid down our line of credit. At this point, we plan to continue to reinvest a portion of our positive cash flow back into the business, while also increasing our cash reserves to allow us to take advantage of future opportunities as they arise.

CASH CHART FY 2004 - 2011
(in thousands of U.S. dollars)



DEBT & EQUITY - A company's ratio of debt to equity is considered to be more important than either debt or equity alone. Typically, companies strive to have a debt to equity ratio of less than 50%. Sono-Tek's ratio is less than this benchmark, as seen in the debt to equity chart. Sono-Tek has a simple balance sheet that reflects our philosophy of making our financial statements and reports straightforward and transparent.

DEBT to EQUITY CHART FY 2003 - 2011
(in thousands of U.S. dollars)



Chairman's Message



Sono-Tek's sales continued a strong growth trend this past fiscal year ending February 2011, with record increases in sales and income. Our sales grew by 37% to just under \$10M, and our income grew from \$82k to nearly \$600k, or \$.04 per share. Our share price also reflected the dramatic increases in sales and income, and doubled from \$.50 per share at the end of February 2009 to over a dollar per share in February 2011 at the close of the fiscal year. We found that we needed more office and manufacturing space to accommodate the increased business and new employees, which led us to first increase our rented space in our industrial park setting, and then later in the calendar year to purchase it outright to insure that we have further room to grow without a costly and disruptive move.

The largest contributors to our record sales have been in the Advanced Energy and Electronics segments. We achieved strong growth in solar energy cell coating applications, utilizing a number of new ultrasonic spraying and coating products based on our Exactacoat and Flexicoat platforms. Our fuel cell coating systems also continued to be strong, utilizing other versions of the Exactacoat and Flexicoat platforms. We also saw strong sales in the electronics printed circuit board fluxing side of the business, in fact larger orders than we have ever experienced in past years. We believe part of the strong showing here is related to the growth of consumer markets for electronic products in the emerging markets—a factor that has not been present before. Our success here has been accelerated because we now offer a more fully developed product line which provides electronics customers with a choice from simpler, less expensive fluxers to more complex and costlier ones.

The other segments of our business including medical device coaters and glass product coaters have also grown over the past year. We enjoy a strong position in providing MediCoat drug eluting stent coating platforms for cardiac implantables. This market continues to evolve and use our equipment to coat ever more sophisticated cardiac stents, and has branched out into coatings for other implantable applications now. In addition, we have promising trials under way in both food and other new coating segments that could open additional marketing niches in the current fiscal year.

Once again, the majority of our business has come from the international markets of Europe, Asia, and Latin America. Our successful globalizing of the business is providing us stability and growth, since other countries have been experiencing infrastructure growth and consumer product demand, by virtue of their younger and growing populations, in contrast to the US with its aging baby boom cohort and slower economic recovery. We are very familiar with working and selling in China, India, Southeast Asia, and European markets, and we have developed a strong set of distributor relationships to serve these markets with us.

The next section will give shareholders more details on our performance this past year, a performance that has been the best ever in the Company's history.

Our ultrasonic nozzle technology produces an atomized spray output that provides key conservation and cost reduction benefits to various product coating applications. Most of these applications involve incorporating one or more of our ultrasonic nozzles in a sophisticated engineered spraying system that provides our customers in these industries with the precision and performance they want from an applied coating.

We are continuing our successful strategy of introducing ultrasonic atomization spraying and coating technology to new markets. These are markets where customers are using old fashioned pressure based spraying and coating systems with their wasteful overspray, harmful environmental impacts, and associated excessive cost of materials and the need for clean-up and collection systems. The brief summary below will provide shareholders with some additional information regarding these applications and our technology and products.



Printed Circuit Board Manufacturing—served by SonoFlux Spray Fluxers and EVS Solder Recovery Systems

Spray fluxing has been at the core of our business for nearly two decades. This market usually follows the overall economy, because our equipment is used in the manufacture of consumer electronics. Over the past two years, we added two new spray fluxing systems to our successful SonoFlux 2000 product. One, the SonoFlux EZ, enhances our ability to compete for simpler application needs and is our lowest cost offering. Our second addition was the SonoFlux Servo, which combines features of both wide area and selective fluxing in one programmable device, and is our highest cost offering. These new fluxers have added significantly to our sales to the electronics printed circuit segment, and have opened up opportunities to growth in emerging markets that did not exist for us before. Besides contributing to our success this year, we expect this family of ultrasonic spray fluxers to continue to contribute to the Company's growth and profitability in the next several fiscal years. Our competitive advantage in this market is providing fluxing systems that offer the manufacturer greater process control combined with lower material and environmental costs than other methods of flux application.

We also offer a related product to our US and Canadian printed circuit board customers, one that offers them an additional opportunity to save on material costs and reduce manufacturing environmental impacts similar to what our spray fluxer line does for them. This is the EVS Solder Recovery System, which allows manufacturers to recycle their used solder to recover reusable solder from a large part of the oxidized dross in their own facility, rather than scrapping the used solder and buying replacement material. The cost savings of recycling typically provides a payback time on our equipment of well under a year at current metal commodity prices.

Fuel Cell Membrane Coatings—served by ExactaCoat and FlexiCoat Platforms

Concerns regarding global warming and the cost and availability of foreign oil supplies has led many governments to sponsor R&D programs in fuel cell technology. We have had customers from all parts of the world visit our laboratory facilities to work with us in specifying which of our equipment platforms best serves their needs. In addition, a number of manufacturers have now purchased our ExactaCoat and FlexiCoat fuel cell coating systems as their R&D work evolves into production work. The material used to coat fuel cell membranes typically includes costly precious metals, and Sono-Tek's ultrasonic atomization offers manufacturers a method to apply precision thin coatings that both cost less and perform better than alternative methods available.

Solar Energy Applications—served by ExactaCoat / FlexiCoat Platforms and the HyperSonic High Speed Coating System

Solar energy development is the key story this year, as many governments and companies around the world compete to develop and provide solar energy systems that offer the best cost and performance. Our ultrasonic coating systems have demonstrated their inherent advantage in creating high performance solar energy conversion cells, and we have seen significant market penetration and growth this year. Solar energy development is being driven by oil prices and availability and global warming concerns, so we expect this market to continue to strengthen over the next several years and beyond. We now offer a series of products to serve the different solar manufacturing applications such as silicon solar, phosphoric doping equipment, and thin film solar coatings such as cadmium sulfide, and other exotic materials.

Implantable Medical Devices—served by MediCoat and Specialty Coating Platforms

We continue to see increasing sales to manufacturers of implanted medical devices such as drug eluting stents for cardiac applications, peripheral vascular applications, sinus applications, diabetic monitoring applications, and others. This business continues to grow as more device manufacturers seek a coating method that is precise and repeatable, and as manufacturers move from the use of our products in development trials to full scale production. The medical device market is one where a great deal of R&D continues as customers here and abroad seek to develop proprietary implantable devices aimed at a variety of diseases. Sono-Tek ultrasonic atomization nozzles and systems have been proven by many customers to be the best way of applying precisely dosed coatings on a variety of these devices, and our sales growth has followed the growth our reputation in this market. In an offshoot of our work in the textile industry, we also have provided systems to medical manufacturers to coat bandages with antimicrobial solutions.

Glass Manufacturing—served by our WideTrack Coating Platforms

Several years ago, we introduced our WideTrack platform which consists of multiple nozzles arranged on a beam over a production line. Included in this platform are integrated pumping and valving, and a computerized control cabinet to provide customers with a complete solution for their production needs. The WideTrack Platform is flexible in that it can accommodate varying lines widths and speeds by using different nozzles and numbers of nozzles, depending on the application. Our greatest success with this platform has been in the glass manufacturing industry, where we have sold dozens of WideTracks to customers who are replacing their older pressure spray platforms due to the cost and waste of this older technology—and implementing new lines with our systems. The main application has been for applying protective coatings at the end of the production line, but our success here is leading to new applications involving anti-reflective and other performance coatings for architectural, automotive, and electronic device manufacturers.

Food and Newer Coating Applications—served by our WideTrack Coating Platforms

We initiated an aggressive program to develop food and food packaging applications two years ago, after receiving several previous orders for coating food products. Conventional air pressure spraying systems are in use in the food industry, with their typical limitations of nozzle clogging, waste and extra cost due to overspray. Beyond that, we believe that we can offer the food industry better ways of providing antimicrobial protection to food products, based on accurate surface coatings rather than incorporating artificial preservatives throughout the food product itself. Progress in penetrating this very large potential market has been slower than we anticipated. However, we are presently working with a major baking company and their oil provider in a newly coordinated attempt to provide the customer with a robust and reliable replacement to the present pressure based systems with their many cost and operational disadvantages. We also have established a laboratory testing relationship with major food manufacturers who are seeking process technology that will enable them to lower their cost of goods sold by accurately and uniformly applying expensive antimicrobials, flavorings and nutraceutical coatings to their products.

Looking Forward

Will the past be prologue? We believe it will be in this case, based on the extensive work we have done to move the Company forward on a new trajectory. It has taken time, money, and the efforts of a talented and committed team of people at Sono-Tek to make the past years success a reality, but we believe that we now have the team, the facility, and the business structure to continue our success into the coming and subsequent years. We are a very unusual small cap company in terms of recent growth, profitability, capital structure, and diversity of geographical and niche end markets. We have a high gross margin based on unique and proprietary technology that makes a significant difference to our customer's success, with little competition. We look forward to continued engagement and expansion in the markets where we have been successful, and to creating new successes around our strong technology core in other markets that can benefit from our ultrasonic atomization spraying and coating systems.

Sincerely,



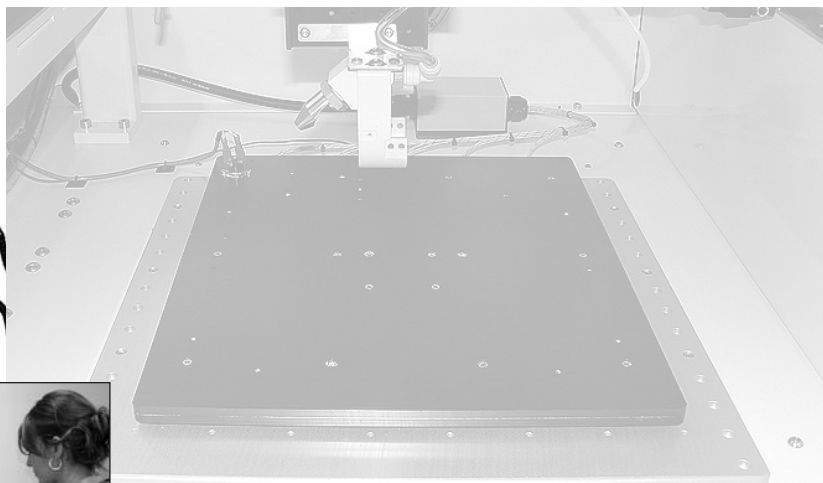
Christopher L. Coccio, PhD

Chairman and CEO

July 8, 2011



Officers and Management Team (left to right): Ed Bozydaj, Robb Engle, Luis Abarca, Christopher Coccio, Joseph Riemer, Steve Harshbarger, Stephen Bagley





MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Forward-Looking Statements

We discuss expectations regarding our future performance, such as our business outlook, in our annual and quarterly reports, press releases, and other written and oral statements. These “forward-looking statements” are based on currently available competitive, financial and economic data and our operating plans. They are inherently uncertain, and investors must recognize that events could turn out to be significantly different from our expectations. These factors include, among other considerations, general economic and business conditions; political, regulatory, competitive and technological developments affecting our operations or the demand for our products; timely development and market acceptance of new products; adequacy of financing; capacity additions, the ability to enforce patents and the ability to achieve increased sales volume and continued profitability.

We undertake no obligation to update any forward-looking statement.

Overview

We have developed a unique and proprietary series of ultrasonic atomizing nozzles, which are being used in an increasing variety of electronics, advanced energy (solar and fuel cells), medical device, glass, textiles and food applications. These nozzles are electrically driven and create a fine, uniform, low velocity spray of atomized liquid particles, in contrast to common pressure nozzles. These characteristics create a series of commercial applications that benefit from the precise, uniform, thin coatings that can be achieved. When combined with significant reductions in liquid waste and less overspray than can be achieved with ordinary pressure nozzle systems, there is lower environmental impact and lower energy use.

Market Diversity

In the past two years we have invested significant time, monies and efforts to enhance our market diversity. Based on our core ultrasonic coating technology, we increased our portfolio of products, the industries we serve and the countries in which we operate.

Today we serve six major industries: electronics, advanced energy (solar and fuel cells), medical device, glass, textiles and food.

Most of our sales now originate outside the USA, and we are geographically present directly and through distributors and trade representatives in North and Latin America, Europe and Asia. The infrastructure upon which this diversified market approach is based, includes a newly equipped process development laboratory, a strengthened sales organization with application engineers, an engineering team with additional talent and the latest, most sophisticated design software tools, as well as an expanded, highly trained installation and service organization.

The new products which were introduced, the new markets that were penetrated, and the regions in which we now operate, are a strong foundation for the company's future sales growth and enhanced profitability.

Liquidity and Capital Resources

Working Capital - Our working capital increased \$247,000 from a working capital of \$3,075,000 at February 28, 2010 to \$3,322,000 at February 28, 2011. The increase in working capital is primarily a result of the current year's net income. Our current ratio is 3.1 to 1 at February 28, 2011, as compared to 3 to 1 at February 28, 2010.

Stockholders' Equity - Stockholders' equity increased \$647,000 from \$3,670,000 at February 28, 2010 to \$4,317,000 at February 28, 2011. The increase in stockholders' equity is the result of the current year's net income of \$594,000, stock based compensation of \$49,000 and the exercise of stock options for \$3,000.

Operating Activities - Our operating activities provided \$1,158,000 of cash for the year ended February 28, 2011 as compared to providing \$494,000 for the year ended February 28, 2010. During the year ended February 28, 2011, we had net income of \$594,000, accounts receivable increased \$12,000, inventories increased \$111,000, prepaid expenses increased \$74,000 and accounts payable, accrued expenses and customer deposits increased \$389,000. In addition, we incurred non-cash expenses of \$313,000 for depreciation and amortization, \$49,000 for stock based compensation expense and an increase in our allowance for doubtful accounts of \$10,000.

Investing Activities - For the year ended February 28, 2011, we used \$2,993,000 in our investing activities as compared to using \$255,000 for the year ended February 28, 2010. In 2011 we used \$2,540,000 for the purchase of land, buildings and improvements and \$249,000 for the purchase of marketable securities. In 2011 and 2010, we used \$195,000 and \$290,000, respectively, for the purchase or manufacture of equipment, furnishings and building improvements. In addition, in 2011 and 2010 we used \$9,000 and \$26,000, respectively, for patent application costs. The purchases of equipment and patent costs were offset by the sale of depreciable equipment of \$61,000 during the year ended February 28, 2010.

Financing Activities - Our financing activities provided \$1,731,000 of cash for the year ended February 28, 2011 as compared to providing \$76,000 for the year ended February 28, 2010. During the year ended February 28, 2011, we had proceeds of a note payable for \$2,100,000 for the purchase of land, buildings and improvements. We repaid the outstanding balance of our line of credit of \$350,000. We had proceeds of \$3,000 for stock option exercises and repayments of notes payable of \$22,000.

Net Decrease in Cash - For the year ended February 28, 2011, our cash balance decreased by \$104,000 as compared to an increase of \$315,000 for the year ended February 28, 2010. During the year ended February 28, 2011, our operations provided \$1,158,000 of cash, we used \$2,993,000 in investing activities and our financing activities provided \$1,731,000 of cash.

We currently have a revolving credit line of \$750,000 and a \$250,000 equipment purchase facility, both of which are with a bank. The revolving credit line is collateralized by all of the assets of the Company and requires a 30 day annual payoff. As of February 28, 2011, we had no outstanding borrowings under the line of credit as compared to \$350,000 at February 28, 2010.

We had outstanding borrowings of \$3,000 under the equipment facility at February 28, 2011. The borrowings have repayment terms which vary from 36 – 60 months and bear interest at rates from 5.2% to 6.6%.

We had outstanding borrowings under a note payable of \$2,095,000 at February 28, 2011. The note is payable over 20 years and bears interest at 5.5%. The note payable is secured by a mortgage on our land and buildings.

Results of Operations

For the year ended February 28, 2011, our sales increased by \$2,672,000 to \$9,914,000 as compared to \$7,242,000 for the year ended February 28, 2010, an increase of 37%. For the year ended February 28, 2011, we experienced an increase in sales in all of our product lines except for stent coater units and HyperSonic units. Noteworthy increases took place in SonoFlux EZ units, WideTrack units and our FlexiCoat and ExactaCoat (XYZ) Platform units. Our sales to customers located in Asian countries increased by \$1,537,000 or 67% for the year ended February 28, 2011. Our sales to US based customers increased by \$1,781,000 or 71% for the year ended February 28, 2011.

Our gross profit increased \$1,098,000, to \$4,772,000 for the year ended February 28, 2011 from \$3,674,000 for the year ended February 28, 2010. Our gross margin percentage was 48% for the year ended February 28, 2011 compared to 51% for the year ended February 28, 2010. For the year ended February 28, 2011, our gross profit margin was impacted by a shift in the mix of products sold during the year. Compared to the year ended February 28, 2010, there was a decline in the number of stent coater units sold and an increase in our XYZ Platform units sold. Historically, our XYZ units have a lower gross profit margin when compared to our stent coater units. In addition, we experienced a lower gross profit margin on our Widetrack units this year as we utilized the resources of a subcontractor for the manufacture of some of these units. The outsourced units were manufactured in the United States under our supervision.

Research and product development costs increased \$105,000 to \$823,000 for the year ended February 28, 2011 as compared to \$718,000 for the year ended February 28, 2010. The increase is due to increased engineering personnel and engineering materials required by additional research and development and product development. The increase in these expenses was offset by a decrease depreciation expense.

Marketing and selling costs increased \$378,000 to \$2,180,000 for the year ended February 28, 2011 from \$1,802,000, for the year ended February 28, 2010. During the year ended February 28, 2011, our trade show and travel expenses increased by approximately \$129,000 when compared to the prior year. In addition, we also saw an increase in salaries, commissions, insurance and depreciation expenses.

General and administrative expense increased \$95,000 to \$1,167,000 for the year ended February 28, 2011 from \$1,072,000, for the year ended February 28, 2010. During the year ended February 28, 2011, we saw an increase in salaries, insurance, consulting and corporate expenses. The increase in these expenses was offset by in decrease in bad debt expense and stock based compensation expense.

Interest income remained flat at \$2,000 for the years ended February 28, 2011 and 2010. Our present investment policy is to invest excess cash in short term cash equivalents with an S & P rating of at least A1+.

Interest expense decreased \$2,000 to \$8,000 for the year ended February 28, 2011 as compared to \$10,000 for the year ended February 28, 2010. The decrease in interest expense is due to decreased borrowing under our line of credit.

Income from real estate operations is the net income from the Company's operation of the Milton Industrial Park which was purchased in December 2010 and began operating January 2011.

Income tax expense was \$14,500 for the year ended February 28, 2011 as compared to a benefit of \$2,000 for the year ended February 28, 2010.

For the year ended February 28, 2011, we had net income of \$594,000 compared to \$82,000 for the year ended February 28, 2010. The improvement in our net income is due primarily to an increase in sales.

Critical Accounting Policies

The discussion and analysis of the Company's financial condition and results of operations are based upon the Company's consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in the United States of America. The preparation of these financial statements requires the Company to make estimates and judgments that affect the reported amount of assets and liabilities, revenues and expenses, and related disclosure on contingent assets and liabilities at the date of the financial statements. Actual results may differ from these estimates under different assumptions and conditions.

Critical accounting policies are defined as those that are reflective of significant judgments and uncertainties, and may potentially result in materially different results under different assumptions and conditions. The Company believes that its critical accounting policies are limited to those described below. For a detailed discussion on the application of these and other accounting policies, please see the notes to the Company's consolidated financial statements.

Accounting for Income Taxes

As part of the process of preparing the consolidated financial statements, the Company is required to estimate income taxes. Management judgment is required in determining the provision for the deferred tax asset.

Stock-Based Compensation

The computation of the expense associated with stock-based compensation requires the use of a valuation model. ASC 718 is a complex accounting standard, the application of which requires significant judgment and the use of estimates, particularly surrounding Black-Scholes assumptions such as stock price volatility, expected option lives, and expected option forfeiture rates, to value equity-based compensation. We currently use a Black-Scholes option pricing model to calculate the fair value of stock options. We primarily use historical data to determine the assumptions to be used in the Black-Scholes model and have no reason to believe that future data is likely to differ materially from historical data. However, changes in the assumptions to reflect future stock price volatility and future stock award exercise experience could result in a change in the assumptions used to value awards in the future and may result in a material change to the fair value calculation of stock-based awards. ASC 718 requires the recognition of the fair value of stock compensation in net income. Although every effort is made to ensure the accuracy of our estimates and assumptions, significant unanticipated changes in those estimates, interpretations and assumptions may result in recording stock option expense that may materially impact our financial statements for each respective reporting period.

Impact of New Accounting Pronouncements

Accounting pronouncements issued but not yet effective have been deemed to be not applicable or the adoption of such accounting pronouncement is not expected to have a material impact on the financials.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Stockholders and Board of Directors

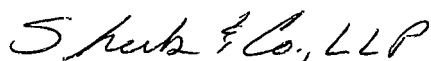
Sono-Tek Corporation

Milton, New York

We have audited the accompanying consolidated balance sheets of Sono-Tek Corporation as of February 28, 2011 and 2010, and the related consolidated statements of operations, stockholders' equity and cash flows for each of the years ended February 28, 2011 and 2010. 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 auditing standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audits to obtain reasonable assurance about whether the financial statements are free of material misstatement. 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 financial position of Sono-Tek Corporation, as of February 28, 2011 and 2010 and the results of their operation and their cash flows for each of the years then ended February 28, 2011 and 2010 in conformity with accounting principles generally accepted in the United States.



SHERB & CO., LLP

Certified Public Accountants

New York, New York

May 16, 2011

CONSOLIDATED BALANCE SHEETS

	February 28,	
	2011	2010
ASSETS		
Current Assets:		
Cash and cash equivalents	\$ 1,683,801	\$ 1,787,516
Marketable Securities	249,100	-
Accounts receivable (less allowance of \$26,000 and \$16,000, respectively)	976,339	974,429
Inventories, net	1,868,144	1,757,153
Prepaid expenses and other current assets.....	131,404	57,775
Total current assets	4,908,788	4,576,873
Land	250,000	-
Buildings, net.....	2,280,175	-
Equipment, furnishings and building improvements, net	414,210	514,623
Intangible assets, net	79,150	76,913
Other assets	6,542	7,171
TOTAL ASSETS	\$ 7,938,865	\$ 5,175,580
LIABILITIES AND STOCKHOLDERS' EQUITY		
Current Liabilities:		
Accounts payable	\$ 643,315	\$ 595,174
Accrued expenses	507,517	466,656
Customer Deposits	373,577	73,954
Line of credit – Bank	-	350,000
Current maturities of long term debt.....	62,247	15,727
Total current liabilities.....	1,586,656	1,501,511
Long term debt, less current maturities	2,035,579	3,622
Total Liabilities	3,622,235	1,505,133
Commitments and Contingencies	-	-
Stockholders' Equity		
Common stock, \$.01 par value; 25,000,000 shares authorized, 14,441,511 and 14,437,511 issued and outstanding, respectively	144,416	144,376
Additional paid-in capital	8,599,122	8,546,924
Accumulated deficit	(4,426,908)	(5,020,853)
Total stockholders' equity.....	4,316,630	3,670,447
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	\$ 7,938,865	\$ 5,175,580

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF OPERATIONS

	Years Ended February 28,	
	2011	2010
Net Sales	\$ 9,914,312	\$ 7,242,324
Cost of Goods Sold	5,142,229	3,568,174
Gross Profit	4,772,083	3,674,150
Operating Expenses		
Research and product development	823,089	717,816
Marketing and selling	2,180,268	1,801,941
General and administrative.....	1,166,690	1,071,636
Total Operating Expenses.....	4,170,047	3,591,393
Operating Income	602,036	82,757
Other Income (Expense):		
Interest Expense.....	(7,921)	(10,214)
Interest Income.....	1,870	1,929
Other Income	-	5,661
Income from real estate operations	12,460	-
Income before Income Taxes	608,445	80,133
Income Tax Expense (Benefit).....	14,500	(1,543)
Net Income	<u>\$ 593,945</u>	<u>\$ 81,676</u>
Basic Earnings Per Share	<u>\$.04</u>	<u>\$.01</u>
Diluted Earnings Per Share	<u>\$.04</u>	<u>\$.01</u>
Weighted Average Shares – Basic	<u>14,439,166</u>	<u>14,414,969</u>
Weighted Average Shares – Diluted	<u>15,028,047</u>	<u>14,524,417</u>

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF STOCKHOLDERS' EQUITY

YEARS ENDED FEBRUARY 28, 2011 AND 2010

	Common Stock Par Value \$.01		Additional	Accumulated	Total
	Shares	Amount	Paid – In Capital	Deficit	Stockholders' Equity
Balance – February 28, 2009	14,414,714	\$ 144,148	\$ 8,490,071	\$ (5,102,529)	\$ 3,531,690
Exercise of stock options	22,797	228	(18)	-	210
Stock based compensation expense	-	-	56,871	-	56,871
Net Income	-	-	-	81,676	81,676
Balance – February 28, 2010	14,437,511	144,376	8,546,924	(5,020,853)	3,670,447
Exercise of stock options	4,000	40	2,920	-	2,960
Stock based compensation expense	-	-	49,278	-	49,278
Net Income	-	-	-	593,945	593,945
Balance – February 28, 2011	14,441,511	\$ 144,416	\$ 8,599,122	\$ (4,426,908)	\$ 4,316,630

See notes to consolidated financial statements.

CONSOLIDATED STATEMENTS OF CASH FLOWS

	Years Ended February 28,	
	2011	2010
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net Income	\$ 593,945	\$ 81,676
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	312,823	309,575
Stock based compensation expense.....	49,278	56,871
Allowance for doubtful accounts.....	10,000	(2,500)
(Increase) Decrease in:		
Accounts receivable	(11,910)	(170,639)
Inventories	(110,991)	(93,579)
Prepaid expenses and other current assets.....	(73,629)	41,030
(Decrease) Increase in:		
Accounts payable and accrued expenses.....	89,002	271,546
Customer deposits	299,623	-
Net Cash Provided by Operating Activities ...	<u>1,158,141</u>	<u>493,980</u>
CASH FLOWS FROM INVESTING ACTIVITIES:		
Purchase of equipment, furnishings and building improvements	(195,035)	(290,301)
Purchase of land, buildings and improvements.....	(2,539,716)	-
Purchase of marketable securities	(249,100)	-
Sale of equipment.....	-	60,862
Patent application costs	(9,442)	(25,785)
Net Cash (Used In) Investing Activities	<u>(2,993,293)</u>	<u>(255,224)</u>
CASH FLOWS FROM FINANCING ACTIVITIES:		
Proceeds from exercise of options.....	2,960	210
Proceeds from note payable	2,100,000	-
Proceeds from line of credit – Bank	-	350,000
Repayment of line of credit – Bank.....	(350,000)	(250,000)
Repayment of long term debt.....	(21,523)	(23,504)
Net Cash Provided by Financing Activities	<u>1,731,437</u>	<u>76,706</u>
NET (DECREASE) INCREASE IN CASH AND CASH EQUIVALENTS	(103,715)	315,462
CASH AND CASH EQUIVALENTS:		
Beginning of year.....	<u>1,787,516</u>	<u>1,472,054</u>
End of year.....	<u><u>\$1,683,801</u></u>	<u><u>\$1,787,516</u></u>

See notes to consolidated financial statements.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
YEARS ENDED FEBRUARY 28, 2011 AND FEBRUARY 28, 2010

NOTE 1: BUSINESS DESCRIPTION

The Company was incorporated in New York on March 21, 1975 for the purpose of engaging in the development, manufacture, and sale of ultrasonic liquid atomizing nozzles, which are sold world-wide. Ultrasonic nozzle systems atomize low to medium viscosity liquids by converting electrical energy into mechanical motion in the form of high frequency ultrasonic vibrations that break liquids into minute drops that can be applied to surfaces at low velocity.

Based on its core technology of ultrasonic liquid atomizing nozzles, the Company has developed intellectual property in the area of precision spray coating of liquids. The Company is presently engaged in the development, manufacture, sales, installation and servicing of diverse ultrasonic coating equipment for various manufacturing industries worldwide.

NOTE 2: SIGNIFICANT ACCOUNTING POLICIES

Consolidation - The accompanying consolidated financial statements of Sono-Tek Corporation, a New York corporation (the "Company"), include the accounts of the Company and its wholly owned subsidiaries, Sono-Tek Cleaning Systems Inc. and Sono-Tek Industrial Park, LLC. Sono-Tek Cleaning Systems, Inc., a New Jersey Corporation ("SCS"), ceased operations during the Fiscal Year Ended February 28, 2002. Sono-Tek Industrial Park, LLC ("SIP"), operates as a real estate holding company for the Company's real estate operations and started operating in December 2010.

Reclassifications - Where appropriate, prior year's financial statements reflect reclassifications to conform to the current year's presentation.

Cash and Cash Equivalents - Cash and cash equivalents consist of money market mutual funds, short term commercial paper and short-term certificates of deposit with original maturities of 90 days or less.

Supplemental Cash Flow Disclosure -

	Years Ended February 28,	
	2011	2010
Interest paid	\$ 14,546	\$ 10,214
Income taxes paid	\$ 216	\$ -

Inventories - Inventories are stated at the lower of cost or market. Cost is determined using the first-in, first-out (FIFO) method for raw materials, subassemblies and work-in-progress and the specific identification method for finished goods.

Allowance for doubtful accounts - The Company records a bad debt expense/allowance based on management's estimate of uncollectible accounts. All outstanding accounts receivable accounts are reviewed for collectability on an individual basis. The bad debt expense recorded for the years ended February 28, 2011 and 2010 was \$10,000 and \$32,470, respectively.

Equipment, Furnishings and Building Improvements - Equipment, furnishings and building improvements are stated at cost. Depreciation of equipment and furnishings is computed by use of the straight-line method based on the estimated useful lives of the assets, which range from three to five years.

Land and Buildings - Land and buildings are stated at cost. Buildings are being depreciated by use of the straight-line method based on an estimated useful life of forty years.

Product Warranty - Expected future product warranty expense is recorded when the product is sold.

Intangible Assets - Include costs of patent applications which are deferred and charged to operations over seventeen years for domestic patents and twelve years for foreign patents and the unamortized portion of deferred financing costs. The accumulated amortization of patents is \$78,058 and \$70,852 at February 28, 2011 and 2010, respectively. Annual amortization expense of such intangible assets is expected to be \$6,700 per year for the next five years.

Research and Product Development Expenses - Research and product development expenses represent engineering and other expenditures incurred for developing new products, for refining the Company's existing products and for developing systems to meet unique customer specifications for potential orders or for new industry applications and are expensed as incurred. Engineering costs directly applicable to the manufacture of existing products are included in cost of goods sold.

Income Taxes - The Company accounts for income taxes under the asset and liability method. Under this method, deferred income taxes are recognized for the tax consequences of "temporary differences" by applying enacted statutory tax rates applicable to future years to differences between the financial statement carrying amounts and the tax basis of existing assets and liabilities. If it is more likely than not that some portion or all of a deferred tax asset will not be realized, a valuation allowance is recognized.

Earnings Per Share - Basic earnings per share ("EPS") is computed by dividing net income by the weighted-average number of common shares outstanding for the period. Diluted EPS reflects the potential dilution that could occur if securities or other contracts to issue common stock were exercised or converted into common stock.

Shipping and Handling Costs - Shipping and handling costs are included in cost of sales in the accompanying consolidated statements of operations.

Advertising Expenses - The Company expenses the cost of advertising in the period in which the advertising takes place. Advertising expense for the years ended February 28, 2011 and 2010 was \$206,271 and \$138,676, respectively.

Long-Lived Assets - The Company periodically evaluates the carrying value of long-lived assets, including intangible assets, when events and circumstances warrant such a review. The carrying value of a long-lived asset is considered impaired when the anticipated undiscounted cash flow from such asset is separately identifiable and is less than its carrying value. In that event, a loss is recognized based on the amount by which the carrying value exceeds the fair market value of the long-lived asset. Fair market value is determined primarily using the anticipated cash flows discounted at a rate commensurate with the risk involved.

Recognition of Revenue - Sales are recorded at the time title passes to the customer, which, based on shipping terms, generally occurs when the product is shipped to the customer. Based on prior experience, the Company reasonably estimates its sales returns and warranty reserves. Sales are presented net of discounts and allowances. Discounts and allowances are determined when a sale is negotiated. The Company does not grant its customers or independent representatives the ability to return equipment nor does it grant price adjustments after a sale is complete.

Concentration of Credit Risk - The Company does not believe that it is subject to any unusual or significant risks, in the normal course of business. The Company also had one customer, which accounted for 8.5% of sales during the year ended February 28, 2011. Two customers accounted for 21.9% of the outstanding accounts receivables at February 28, 2011.

Fair Value of Financial Instruments - Effective June 1, 2008, the Company adopted the guidance in the Fair Value Measurements and Disclosure Topic of the Accounting Standards Codification for assets and liabilities measured at fair value on a recurring basis. This guidance establishes a common definition for fair value to be applied to existing generally accepted accounting principles that require the use of fair value measurements, establishes a framework for measuring fair value and expands disclosure about such fair value measurements. The adoption of this guidance did not have an impact on the Company's financial position or operating results, but did expand certain disclosures. The guidance defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date. Additionally, the guidance requires the use of valuation techniques that maximize the use of observable inputs and minimize the use of unobservable inputs. These inputs are prioritized below:

Level 1: Quoted prices in active markets.

Level 2: Observable market-based inputs or unobservable inputs that are corroborated by market data.

Level 3: Unobservable inputs for which there is little or no market data, which require the use of the reporting entity's own assumptions.

The fair values of financial assets of the Company were determined using the following categories at February 28, 2011:

	<u>Quoted prices in active markets (Level 1)</u>
Marketable Securities	<u>\$ 249,100</u>

Marketable Securities include mutual funds of \$249,100, that are considered to be highly liquid and easily tradeable as of February 28, 2011. These securities are valued using inputs observable in active markets for identical securities and are therefore classified as Level 1 within the Company's fair value hierarchy.

In addition, the guidance of the Fair Value Option for Financial Assets and Financial Liabilities Topic of the Codification was effective for June 1, 2008. The guidance expands opportunities to use fair value measurements in financial reporting and permits entities to choose to measure many financial instruments and certain other items at fair value.

Management Estimates - The preparation of financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

New Accounting Pronouncements-

Accounting pronouncements issued but not yet effective have been deemed to be not applicable or the adoption of such accounting pronouncement is not expected to have a material impact on the financials.

NOTE 3: SEGMENT INFORMATION

The Company currently operates in one business segment, ultrasonic spray coating systems and is primarily engaged in the business of developing, manufacturing, selling, installing and servicing ultrasonic spray coating equipment.

NOTE 4: STOCK-BASED COMPENSATION

The Company adopted ASC 718, "Share Based Payments," which requires companies to expense the value of employee stock options and similar awards.

The weighted-average fair value of options has been estimated on the date of grant using the Black-Scholes options-pricing model. The weighted-average Black-Scholes assumptions are as follows:

	2011	2010
Expected life	4 years	4 years
Risk free interest rate57% - 1.17%	1.39% - 2.7%
Expected volatility	37% - 53%	66% - 96%
Expected dividend yield.....	0%	0%

In computing the impact, the fair value of each option is estimated on the date of grant based on the Black-Scholes options-pricing model utilizing certain assumptions for a risk free interest rate; volatility; and expected remaining lives of the awards. The assumptions used in calculating the fair value of share-based payment awards represent management's best estimates, but these estimates involve inherent uncertainties and the application of management judgment. As a result, if factors change and the Company uses different assumptions, the Company's stock-based compensation expense could be materially different in the future. In addition, the Company is required to estimate the expected forfeiture rate and only recognize expense for those shares expected to vest. In estimating the Company's forfeiture rate, the Company analyzed its historical forfeiture rate, the remaining lives of unvested options, and the number of vested options as a percentage of total options outstanding. If the Company's actual forfeiture rate is materially different from its estimate, or if the Company reevaluates the forfeiture rate in the future, the stock-based compensation expense could be significantly different from what the Company has recorded in the current period.

For the years ended February 28, 2011 and February 28, 2010, net income and earnings per share reflect the actual deduction for stock-based compensation expense. The impact of applying ASC 718 approximated \$49,278 and \$56,871 in additional compensation expense for the years then ended, respectively. Such amount is included in general and administrative expenses on the statement of operations. The expense for stock-based compensation is a non-cash expense item.

NOTE 5: INVENTORIES

Inventories consist of the following:

	February 28,	
	2011	2010
Raw Materials.....	\$ 799,355	\$ 477,845
Work-in-process.....	594,744	527,553
Consignment.....	7,861	9,042
Finished Goods	729,142	951,671
Totals	2,131,102	1,966,111
Less: Allowance	(262,958)	(208,958)
	<u>\$ 1,868,144</u>	<u>\$ 1,757,153</u>

NOTE 6: BUILDINGS, EQUIPMENT, FURNISHINGS AND BUILDING IMPROVEMENTS

Equipment, furnishings and building improvements consist of the following:

	February 28,	
	2011	2010
Buildings	\$ 2,289,716	\$ -
Laboratory equipment	423,286	414,112
Machinery and equipment	376,518	363,167
Building improvements	138,810	126,529
Tradeshow and demonstration equipment	721,246	621,561
Furniture and fixtures	579,369	540,786
Totals	4,528,945	2,066,155
Less: accumulated depreciation	(1,834,560)	(1,551,532)
	<u>\$ 2,694,385</u>	<u>\$ 514,623</u>

Depreciation expense for the years ended February 28, 2011 and February 28, 2010 was \$305,618 and \$302,290, respectively.

NOTE 7: ACCRUED EXPENSES

Accrued expenses consist of the following:

	February 28,	
	2011	2010
Accrued compensation	\$ 288,929	\$ 235,980
Estimated warranty costs	28,050	21,900
Accrued commissions	126,092	168,831
Professional fees	14,850	25,014
Other accrued expenses	49,596	14,931
	<u>\$ 507,517</u>	<u>\$ 466,656</u>

NOTE 8: REVOLVING LINE OF CREDIT

The Company has a \$750,000 revolving line of credit at prime which was 3.25% at February 28, 2011. The loan is collateralized by all of the assets of the Company. The line of credit is payable on demand and must be retired for a 30 day period once annually. As of February 28, 2011 and February 28, 2010, the Company had outstanding borrowings of \$0 and \$350,000, respectively, under the revolving line of credit.

NOTE 9: LONG-TERM DEBT

Long-term debt consists of the following:

	February 28,	
	2011	2010
Note payable, individual, collateralized by land and buildings, payable in monthly installments of principal and interest of \$14,446 through January 2031. Interest rate 5.5%. 20 year term.....	\$ 2,095,179	\$ 0
Equipment loan, bank, collateralized by related production equipment, payable in monthly installments of principal and interest of \$832 through March 2010. Interest rate 6.51%. 60 month term.....	0	830
Equipment loan, bank, collateralized by related office equipment, payable in monthly installments of principal and interest of \$529 through September 2011. Interest rate 5.22%. 36 month term.....	2,647	9,632
Equipment loan, bank, collateralized by related engineering equipment, payable in monthly installments of principal and interest of \$770 through February 2011. Interest rate 6.54%. 60 month term.....	0	8,887
Total long term debt	2,097,826	19,349
Due within one year	62,247	15,727
Due after one year	<u>\$ 2,035,579</u>	<u>\$ 3,622</u>

Long-term debt is payable as follows:

Fiscal Year ending February 28,	
2012	\$ 62,247
2013	62,962
2014	66,514
2015	70,265
2016	74,229
Thereafter	1,761,609

NOTE 10: COMMITMENTS AND CONTINGENCIES

Leases – Total rent expense was approximately \$116,321 and \$142,094, for the years ended February 28, 2011 and 2010, respectively.

NOTE 11: INCOME TAXES

The annual provision (benefit) for income taxes differs from amounts computed by applying the maximum U.S. Federal income tax rate of 35% to pre-tax income as follows:

	February 28,	
	2011	2010
Expected federal income tax (benefit)	\$ 212,880	\$ 28,587
State tax, net of federal	36,494	3,430
Permanent timing difference	53,721	22,748
(Decrease) in valuation allowance	(288,595)	(56,308)
Income tax expense (benefit)	\$ 14,500	\$ (1,543)

The net deferred tax asset is comprised of the following:

	February 28,	
	2011	2010
Inventory	\$ 135,000	\$ 110,000
Accrued expenses and other	60,000	34,000
Net operating losses	541,000	870,000
Deferred tax asset	736,000	1,014,000
Deferred tax liability	(152,000)	(141,000)
Valuation allowance	(584,000)	(873,000)
Net deferred tax asset	\$ -	\$ -

The change in the valuation allowance was \$289,000 for the year ended February 28, 2011. This represents a \$289,000 decrease in the net operating loss valuation allowance and includes an \$11,000 change in depreciable timing differences.

At February 28, 2011, the Company has available net operating loss carryforwards of approximately \$1,300,000 for income tax purposes, which expire between fiscal 2019 and fiscal 2029. The net operating loss carryforwards generated by a subsidiary are subject to limitations under Section 382 of the Internal Revenue Code.

NOTE 12: STOCKHOLDERS' EQUITY

Stock Options – The Company has two stock option plans, the 1993 Stock Incentive Plan, as Amended (“1993 Plan”) and the 2003 Stock Incentive Plan (“2003 Plan”). Under each Plan, options can be granted to officers, directors, consultants and employees of the Company and its subsidiaries to purchase up to 1,500,000 of the Company’s common shares. Options granted under the 1993 Plan expire on various dates through 2013. The 1993 Plan expired in October 2003 and no further options can be granted under the 1993 Plan. A total of 40,000 options remain outstanding under the 1993 Plan. Under the 2003 Plan options expire at various dates through 2020. A total of 1,321,268 options are outstanding under the 2003 Plan.

During Fiscal Year 2011, the Company granted options for 125,000 shares exercisable at \$1.04 to an officer of the Company, options for 20,000 shares exercisable at \$.95 to a director of the Company and options for 43,500 shares exercisable at prices from \$.88 to \$.97 to employees of the Company.

During Fiscal Year 2010, the Company granted options for 50,000 shares exercisable at \$1.04 to an officer of the Company, options for 5,500 shares exercisable at prices from \$.53 to \$1.04 to independent consultants and options for 17,500 shares exercisable at prices from \$.54 to \$1.03 to employees of the Company.

Under both the 1993 Plan and the 2003 Plan, options are granted at prices that are at least 100% of the fair market value of the common stock at time of grant. For qualified employees, except under certain circumstances specified in both Plans or unless otherwise specified at the discretion of the Board of Directors, no option may be exercised prior to one year after date of grant, with the balance becoming exercisable in cumulative installments over a three year period during the term of the option, and terminate at a stipulated period of time after an employee's termination of employment.

A summary of the activity of both plans for the years ended February 28, 2011 and February 28, 2010 is as follows:

	Stock Options		Weighted Average Exercise Price		Fair Value Vested
	Outstanding	Exercisable	Outstanding	Exercisable	
Balance – February 29, 2009.....	1,205,565	920,906	\$ 1.10	\$ 1.08	\$.33
Granted	73,000		.98		
Exercised	(47,797)		(.74)		
Cancelled	(1,000)		(.42)		
Balance – February 28, 2010.....	1,229,768	1,018,418	1.11	1.06	.34
Granted	191,000		1.01		
Exercised	(4,000)		(.74)		
Cancelled	(55,500)		(1.11)		
Balance – February 28, 2011.....	<u>1,361,268</u>	<u>1,104,293</u>	<u>\$ 1.11</u>	<u>\$ 1.06</u>	<u>\$.34</u>

The intrinsic value of the Company's options exercised during the years ended February 28, 2011 and 2010 was \$1,560 and \$31,356, respectively.

Information, at date of issuance, regarding stock option grants for the years ended February 28, 2011:

	Shares	Weighted Average Exercise Price	Weighted Average Fair Value
Year ended February 28, 2011:			
Exercise price exceeds market price	-	-	-
Exercise price equals market price	191,000	\$ 1.01	\$.50
Exercise price is less than market price.....	-	-	-

The aggregate intrinsic value of the Company's outstanding options at February 28, 2011 was \$137,440.

The following table summarizes information about stock options outstanding and exercisable at February 28, 2011:

	Number Outstanding	Weighted- Average Remaining Life in Years	Weighted Average Exercise Price	Number Exercisable
Range of exercise prices:				
\$.25 to \$.50	87,000	5.5	\$.39	81,000
\$.51 to \$1.00	647,893	6.8	\$.83	556,393
\$1.01 to \$1.75	553,875	8.3	\$ 1.49	394,400
\$1.76 to \$2.30	65,000	3.9	\$ 2.15	65,000
\$2.31 to \$3.00	7,500	4.1	\$ 2.58	7,500

NOTE 13: EARNINGS PER SHARE

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

	February 28,	
	2011	2010
Numerator for basic and diluted earnings per share.....	\$ 593,945	\$ 81,676
Denominator:		
Denominator for basic earnings per share- weighted average shares	14,439,166	14,414,969
Effects of dilutive securities:		
Stock options for employees, directors and outside consultants.....	588,881	109,448
Denominator for diluted earnings per share	15,028,047	14,524,417
Basic Earnings Per Share	\$.04	\$.01
Diluted Earnings Per Share.....	\$.04	\$.01

NOTE 14: SIGNIFICANT CUSTOMERS AND FOREIGN SALES

Export sales to customers located outside the United States were approximately as follows:

	February 28,	
	2011	2010
Western Europe	\$ 1,252,000	\$ 1,324,000
Far East	3,841,000	2,304,000
Other	531,000	1,108,000
	<u>\$ 5,624,000</u>	<u>\$ 4,736,000</u>

During Fiscal Years 2011 and 2010, sales to foreign customers accounted for approximately \$5,624,000 and \$4,736,000, or 57% and 65% respectively, of total revenues.

One customer accounted for 8.5% of our sales for Fiscal Year ended February 28, 2011.

NOTE 15: SUBSEQUENT EVENTS

The Company has evaluated subsequent events for disclosure purposes.

COMMON STOCK

Prior to February 21, 2011, our Common Stock traded in the over-the-counter market on the OTC Bulletin Board. Since February 22, 2011 our common stock has been traded on the over-the-counter QB platform. The following table sets forth the range of high and low closing bid quotations for our Common Stock for the periods indicated.

	YEAR ENDED FEBRUARY 28,			
	2011		2010	
	HIGH	LOW	HIGH	LOW
First Quarter	\$ 1.13	\$ 0.95	\$ 0.55	\$ 0.40
Second Quarter	1.00	0.86	0.72	0.42
Third Quarter	1.05	0.70	1.25	0.62
Fourth Quarter	1.06	0.92	1.40	0.97

The above quotations are believed to represent inter-dealer quotations without retail markups, markdowns or commissions and may not represent actual transactions.

As of May 2, 2011, there were 206 shareholders of record of our Common Stock, according to our stock transfer agent. We estimate that we have between 1,000 and 1,400 beneficial shareholders of our common stock. The difference between the shareholders of record and the total shareholders is due to stock being held in street names at our transfer agent.

We have not paid any cash dividends on our Common Stock since inception. We intend to retain earnings, if any, for use in our business and for other corporate purposes.

Directors

Christopher L. Coccio, Ph.D. - Chairman and CEO

Joseph Riemer, Ph.D. - President

Samuel Schwartz - Chairman Emeritus and former Chairman of the Board, retired Chairman and CEO of Krystinel Corporation.

Edward J. Handler, Esq. - Compensation and Audit Committees, retired partner from Kenyon and Kenyon intellectual property law firm, President and COO of The Bronx Project, Inc., past President of the West Point Society of New York.

Philip A. Strasburg, CPA - Certified Public Accountant in New York State, retired partner from Anchin Block and Anchin accounting firm, Chairman of the Audit Committee.

Donald F. Mowbray, Ph.D. - Chairman of Compensation Committee, Independent Consultant, Retired head of General Electric's Corporate R&D Mechanical Engineering Laboratory.

Eric Haskell, CPA - Compensation Committee, former Executive Vice President and Chief Financial Officer of SunCom Wireless Holdings, Inc., former Chief Financial Officer of Systems & Computer Technology Corp.

Executive Officers

Christopher L. Coccio, Ph.D. - Chairman and CEO

Joseph Riemer, Ph.D. - President

Stephen J. Bagley, CPA - Chief Financial Officer

R. Stephen Harshbarger - Vice President and Director of Electronics & Advanced Energy

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