

SERVOTRONICS, INC.

Creating Waves of Leading Edge Technology



2011 ANNUAL REPORT

Annual Message



The year 2011 was a period of improved operational performance as a result of a successful business development and cost containment opportunity capture. Servotronics, Inc.'s ("Company") net income increased 23.4% to \$2,626,000 (or \$1.31 per share Basic and \$1.24 Diluted) on an 8.0% revenue increase to \$34,181,000 for the year ended December 31, 2011 as compared to a net income of \$2,128,000 on revenues of \$31,659,000 for the corresponding twelve month period a year earlier. The Company also paid out two dividends totaling \$0.30 per share,



double prior year levels. This is the first time Servotronics has distributed cash dividends to shareholders twice in a single year. Despite these distributions, the balance sheet continued to strengthen with cash increasing by approximately 11% to almost \$5,000,000. Such dividend payments do not indicate that the Company will continue to pay similar dividends on a regular or scheduled basis. Improved performance was driven by increased demand, product enhancements, and improved mix in the Company's Advanced Technology Group ("ATG") partially offset by margin pressure and start-up costs related to business development activities at the Consumer Products Group ("CPG"). In many ways, this performance is a reflection of what is occurring in the global economy at large.

The year ended December 31, 2011 marks the completion of a challenging ten-year period that included many domestic and global record-breaking events that had significant adverse impacts on domestic and international economies. There have been a growing number of reports and opinions indicating that the ongoing recession remains in a slow, possibly unstable, state of recovery. Vacillating scenarios are now being advanced which vary from those which claim that the World and U.S. economies are poised for a "double-dip" recession, to the more positive observations that claim the worst is over and the trend is now upward. No matter which negative or positive bias is proven to be right, there are substantial margins for error in the interim. National and regional economies around the world remain fragile and precarious. Fiscal irresponsibility in the European Union and elsewhere has created a significant risk factor that could delay or derail any potential recovery. Further, the increased money supply and continued deficit spending that bolstered the United States economy in recent years could foster inflation or adversely impact market confidence. Finally, conflicts that arise from unforeseen acts of terrorism or failure of international diplomacy issues, such as those focusing on nuclear weapons in Iran, could dramatically impact world-wide economic growth. These factors appear to be weighing heavily on the recovery, impacting decision making at large corporations, financial institutions, and Government agencies in the United States and abroad.

Of course, recovery dynamics remain specific to the market segments in which one competes. The Company's ATG designs and manufactures servo-control and other products for the domestic and foreign aerospace markets. These products are utilized in large airplanes by the commercial travel and cargo shipping markets as well as in specialty aircraft for military applications. Beyond this, there are numerous additional applications for the Company's ATG products including use on Government aircraft, helicopters, missiles, ground vehicles, and medical equipment. Servotronics' CPG also designs and manufactures edged products. Those products include propriety specialty tools, cutlery, bayonets, machetes, and knives used for combat, survival, sporting, and agricultural applications. Each of these sectors has specific dynamics that impact business performance.

In recent months, aircraft manufacturers in the commercial sector have forecasted more robust aircraft production driven by growing customer demand due to a need to address capacity constraints and improve economic efficiencies by replacing aging fleets. This is occurring primarily in the delivery of jetliners to both domestic and foreign markets and is supported by the underlying return of this business segment to profitability. Conversely, the Department of Defense continues to lower expenditures in order to address budget constraints, thereby reallocating funds in response to changing geo-political issues. Government procurements are expected to continue to be volatile and have resulted in fluctuating demand and delivery requirements. The impact of these changes on the American Aerospace industry remains a concern and will, hopefully, be strongly supported in spite of possible alternatives. The United States maintains a strong international trade surplus which adds support for the U.S. Aerospace Industry.

Unlike aerospace, the edged products industry remains more fragmented and diverse. Products are sold to a wide range of customers for use in a broad range of industries both domestically and abroad. Value-added design and product innovations continue to provide a challenge to low-cost competitors manufacturing overseas. Price competition continues to be aggressive and demand is soft. The primary driver is industry overcapacity combined with a reduction in consumption stemming from a wind-down in international military engagements by U.S. forces. The impact of these dynamics is, optimistically, expected to stabilize in the future, providing an opportunity for top-line growth and margin expansion.

While the Company's ATG and CPG have distinctly different product lines, in certain circumstances, the variables affecting Government procurement of our Company's products are similar. These include shifts in military and/or Government funding priorities, funding availabilities, as well as political determinations that form the role the U.S. will play in known international affairs and yet unknown geo-political developments. All of this is made more precarious as the upcoming year is an election period where the future administration, and its resulting focus, remains unclear. Deficit spending, the inability to create a budget for several years, and general congressional gridlock further complicate the situation. Specifically, automatic budget cuts across-the-board, if implemented, could reduce military expenditures in ways that may be strategically adverse both for U.S. military requirements and for the resulting near-term demand. All of these variables will affect the types and amount of Government items produced and delivery schedule demands. As military sales comprise a material component of Servotronics business, this makes forecasting a challenge. Fortunately in 2011, declines in Government sales were offset by increases in commercial and international demand. However, these military unknowns, in combination with the ongoing economic challenges, continue to result in uncertain projections for the future.

To address this, Servotronics continues to manage what it can control and plan around what it cannot. The Company has strategically positioned itself by consistently designing and developing new products for new applications and programs across multiple industries. Product application diversity provides a foundation for multi-market opportunities that aggressive propriety design efforts can selectively and efficiently convert to new income producing products. Servotronics continues to expand its capabilities by adding product lines and resources to the Company's inventory of skills and product offerings. Ontario Knife Company's recent receipt of the "Best of the Best" award from Field and Stream Magazine for innovative new product introductions reflects this. Servotronics' many product developments and expanded capabilities are expected to benefit from the continuing cost improvements through manufacturing enhancement and consolidation as the Company converts each challenge into an opportunity. Although there is always a certain degree of uncertainty with all planned courses of action, the ability to respond quickly is a carefully cultivated Company skill that has substantial value when implementing strategic and tactical plans of action. Our receipt of the top Defense Logistic Agency (DLA) Supplier Gold Excellence Award for operational excellence again in 2011 is a continuing reflection of our core competency. It is anticipated that over the near-term the operating result for certain of the Company's products will be responsive to the volatility of certain of the Government's procurement procedures and other unexpected market events.

These ongoing proactive efforts and the ever-evolving systems and processes that support them are directly attributed to our recent performance successes. The 8% increase in 2011 revenues is the result of increased product sales at both ATG and CPG. The 23% increase in net income is the result of new higher product margins and improved product mix at ATG which offset a small decline at CPG due to product mix, write-off, and start-up costs. Collectively, these revenue gains were achieved in spite of continuing investments related to the introduction of new products and product lines, facility improvements, and ramp-up costs to meet customers' forecasted increase in product requirements. Cost containment efforts, operational consolidation evaluations, equipment updating, procurement cost reductions, outsourcing, and other front-end expense-producing activities also continue to bear fruit while positioning the Company to benefit long-term.

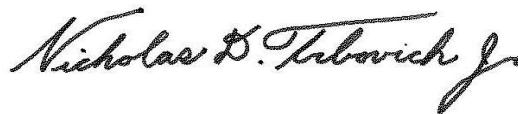
As a result of these efforts, and in light of recent customer demand, we remain cautiously optimistic for the future within the constraints of today's global economic reality and underlying market volatility. During the past 50-plus years there have been six recessions, not including the current one. Our Company has successfully operated through each recession and emerged stronger than before. We believe this is reflective of the current scenario.

Our efforts and dedication are focused on the success of our products and the satisfaction of our customers. We are proud of the many accomplishments and successes that are the direct result of our high caliber employees and their commitment to achieving Company goals. The dedicated efforts of our Directors and the support of our Shareholders are acknowledged and greatly appreciated. We look forward to aggressively confronting future challenges and converting them into meaningful achievements.



DR. NICHOLAS D. TRBOVICH

Founder, Chairman of the Board and Chief Executive Officer



NICHOLAS D. TRBOVICH, JR.

Director, President and Chief Operating Officer

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UNITED STATES SECURITIES AND EXCHANGE COMMISSION

Washington, D. C. 20549

Form 10-K

(Mark One)

☒ ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934

For the fiscal year ended December 31, 2011

or

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

Commission File No. 1-07109

SERVOTRONICS, INC.

(Exact name of registrant as specified in its charter)

Delaware

(State or other jurisdiction of incorporation or organization)

16-0837866

(I. R. S. Employer Identification No.)

1110 Maple Street

Elma, New York 14059

(Address of Principal Executive Office) (Zip Code)

Registrant's telephone number, including area code (716) 655-5990

Securities registered pursuant to Section 12(b) of the Act:

Title of each class

Name of each exchange on which registered

Common Stock, \$.20 par value

NYSE Amex

Securities registered pursuant to Section 12(g) of the Act:

None

(Title of Class)

Indicate by check mark if the registrant is a well-known seasoned issuer, as defined in Rule 405 of the Securities Act.

Yes ☐

No ☒

Indicate by check mark if the registrant is not required to file reports pursuant to Section 13 or Section 15(d) of the Act.

Yes ☐

No ☒

Indicate by checkmark 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 ☒

No ☐

Indicate by checkmark 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 (§232.405) during the preceding 12 months (or for such shorter period that the registrant was required to submit and post such files).

Yes ☒

No ☐

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K (§229.405) is not contained herein, and will not be contained, to the best of registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K. ☒

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 ☐

Accelerated filer ☐

Non-accelerated filer ☐

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 ☐

No ☒

Based on the closing price of the Common Stock on June 30, 2011 (\$8.94) (the last day of the registrant's most recently completed second fiscal quarter), the aggregate market value of the voting stock held by non-affiliates of the registrant was \$13,773,173.

As of February 29, 2012 the number of \$.20 par value common shares outstanding was 2,309,371.

DOCUMENTS INCORPORATED BY REFERENCE

Portions of the Registrant's Proxy Statement for the 2012 Annual Meeting of Shareholders are incorporated by reference in Part III.

NOTE: The Company's Form 10-K as filed with the Securities and Exchange Commission has been appropriately condensed to provide this Annual Report to Shareholders. The complete 10-K is available from the Company to any shareholder as stated on the inside back cover of this Annual Report.

PART I

Item 1. Business

General

Servotronics, Inc. and its subsidiaries (collectively the “Registrant” or the “Company”) design, manufacture and market advanced technology products consisting primarily of control components and consumer products consisting of knives and various types of cutlery and other edged products.

The Company was incorporated in New York in 1959. In 1972, the Company was merged into a wholly-owned subsidiary organized under the laws of the State of Delaware, thereby changing the Company’s state of incorporation from New York to Delaware.

The Company’s shares currently trade on the NYSE Amex under the symbol SVT.

Products

Advanced Technology Products

The Company designs, manufactures and markets a variety of servo-control components which convert an electrical current into a mechanical force or movement and other related products. The principal servo-control components produced include torque motors, electromagnetic actuators, hydraulic valves, pneumatic valves and similar devices, all of which perform the same general function. These are sold principally to the commercial aerospace, missile, aircraft and government related industries, as well as medical and industrial markets.

To fill most of its orders for components, the Company must either modify a standard model or design a new item in order to satisfy the customer’s particular requirements. The Company also produces unique products based on specifications provided by its customers. The Company produces under long-term contracts and other types of orders.

The Company may from time to time produce metallic seals of various cross-sectional configurations. These seals fit between two surfaces, usually metal, to produce a more secure and leak-proof joint. The Company manufactures these seals to close tolerances from standard and special alloy steels. Ductile coatings are often applied to the seals in order to increase their effectiveness.

From time to time, the Company has also produced other products of its own and/or of a given design to meet customers’ requirements.

Consumer Products

The Company designs, manufactures and sells a variety of cutlery products. These products include a wide range of cutlery items such as steak, carving, bread, butcher and paring knives for household use and for use in restaurants, institutions and private industry, and pocket and other types of knives for hunting, fishing and camping. The Company also sells cutlery products to the U.S. Government and related agencies. These products include machetes, bayonets and other types of knives that are primarily for military use. The Company also produces and markets other cutlery items such as various specialty tools, putty knives, linoleum sheet cutters, field knives and other edged products. The Company manufactures its cutlery products from stainless or high carbon steel in numerous styles, designs, models and sizes. Substantially all of the Company’s commercial cutlery related products are intended for the medium to premium priced markets.

The Company sells many of its cutlery products under its own brand names including “Old Hickory” and “Queen”. In the fourth quarter of 2009 the Company acquired the capability to manufacture hot forged edged products which expanded the commercial and government markets for the Consumer Products Group.

Sales, Marketing and Distribution

Advanced Technology Products

The Company’s Advanced Technology Group products (“ATG”) are marketed throughout the United States and in select foreign markets. Products are primarily non-seasonal in nature. These products are sold to the United States Government, government prime contractors, government subcontractors, commercial manufacturers and end users. Sales are made primarily by the Company’s professional staff.

During the Company's 2011 fiscal year, sales of advanced technology products pursuant to contracts with prime or subcontractors for various branches of the United States Government accounted for approximately 18% of the Company's sales as compared to 21% in 2010. The Company's sales of advanced technology products to one customer, including various divisions and subsidiaries of a common parent company, amounted to approximately 25% in 2011 and 22% in 2010 of the Company's consolidated sales. The Company also had sales to another ATG customer that amounted to approximately 10% of total revenues in 2011 and 9% in 2010. No other single customer represented more than 10% of the Company's consolidated revenues in either of these years.

The Company's prime contracts and subcontracts with the United States Government are subject to termination at the convenience of the Government. In the event of such termination, the Company is ordinarily entitled to receive payment for its costs and profits on work done prior to termination. Since the inception of the Company's business, less than 1% of its Government contracts have been terminated for convenience.

Consumer Products

The Company's consumer products are marketed throughout the United States and in select foreign markets. Consumer sales are moderately seasonal. Sales are to hardware, supermarket, variety, department, discount, gift and drug stores. The Company's Consumer Products Group ("CPG") also sells its cutlery products (principally machetes, bayonets, survival knives, kitchen knives and scissors) to various branches of the United States Government which accounted for approximately 20% of the Company's consolidated revenues in 2011 as compared to 21% in 2010. No other single customer of the CPG represented more than 10% of the Company's consolidated sales in 2011. The Company sells its products through its own sales personnel and through independent manufacturers' representatives.

Business Segments

Business segment information is presented in Note 12, Business Segments, of the accompanying consolidated financial statements.

Intellectual Properties

The Company has rights under certain copyrights, trademarks, patents, and registered domain names. In the view of management, the Company's competitive position is not dependent on patent protection.

Research Activities

The amount spent by the Company in research and development activities during its 2011 and 2010 fiscal years was not significant.

Environmental Compliance

The cost of compliance with current environmental laws has not been material and the Company does not anticipate that it will be in the future.

Manufacturing

The Company manufactures its consumer products in Franklinville, New York, Titusville, Pennsylvania and Nashville, Arkansas and its advanced technology products in Elma, New York.

Raw Materials and Other Supplies

The Company purchases raw materials and certain components for its products from outside vendors. The Company is generally not dependent upon a single source of supply for any raw material or component used in its operations.

Competition

Although no reliable industry statistics are available to enable the Company to determine accurately its relative competitive position with respect to any of its products, the Company believes that it is a significant factor with respect to certain of its servo-control components. The Company's share of the overall cutlery market is not significant.

The Company has many different competitors with respect to servo-control components because of the nature of that business and the fact that these products also face competition from other types of control components which, at times, can accomplish the desired result.

The Company encounters active competition with respect to its consumer products from numerous companies, many of which are larger in terms of manufacturing capacity, financial resources and marketing organization. Its principal competitors vary depending upon the customer and/or the products involved. The Company believes that it competes primarily with more than 20 companies with respect to its consumer products, in addition to foreign imports. To the Company's knowledge, its principal competitors with regard to cutlery include World Kitchen, Inc., Benchmade Knife Company, Inc., Tramontina, Inc., Dexter-Russell Inc., W. R. Case & Sons Cutlery Company, Lifetime Hoan Corp., and Gerber.

The Company markets most of its products throughout the United States and to a lesser extent in select foreign markets. The Company believes that it competes in marketing its servo-control products primarily on the basis of operating performance, adherence to rigid specifications, quality, price and delivery and its consumer products primarily on the basis of price, quality and delivery.

Employees

The Company, at December 31, 2011, had approximately 285 employees of which approximately 271 are full time; 231 in Western New York, 20 in Pennsylvania and 20 in Arkansas. Approximately 82% of its employees are engaged in production, inspection, packaging or shipping activities. The balance is engaged in executive, engineering, administrative, clerical or sales capacities.

Item 1A. Risk Factors

The Company is a smaller reporting company by Rule 12b-2 of the Exchange Act and is not required to provide the information required under this item.

Item 1B. Unresolved Staff Comments

The Company is a smaller reporting company by Rule 12b-2 of the Exchange Act and is not required to provide the information required under this item.

Item 2. Properties

The Company's executive offices are located on premises under a capital lease by the Company at 1110 Maple Street, Elma, a suburb of Buffalo, New York. The Company owns, leases and/or has options on real property as set forth in the following table:

<u>Location</u>	<u>Approx. acreage</u>	<u>Principal product manufactured</u>	<u>Number of buildings and type of construction</u>	<u>Approx. floor area (sq. feet)</u>
Elma, New York	38.40	Advanced technology products	1-concrete block/ steel	82,000
Franklinville, New York	12.70	Cutlery products	1-tile/wood 1-concrete/metal 1-concrete block	154,000
Titusville, Pennsylvania	0.40	Cutlery products	2-brick	25,000
Nashville, Arkansas	4.65	Cutlery products	1-concrete/metal	39,000

Pursuant to agreements with a local industrial development agency ("IDA") the Company leases and/or has options to purchase a facility and approximately 38.4 acres of land in Elma, New York. The Company occupies the facility, which serves as the Company's headquarters and major manufacturing and research site for the Company's Advanced Technology Group. The transaction is accounted for by the Company as a capital lease. The facility secures the payment of an outstanding Industrial Development Bond (the "Bond") which financed construction of the facility.

The Bond was originally issued in the principal amount of \$5,000,000 and, after a series of timely payments of principal and interest by the Company in accordance with the governing agreements, the outstanding Bond principal indebtedness has been reduced to approximately \$3.0 million as of December 31, 2011. When the Bond indebtedness has been fully paid, the Company has the right to purchase the Facility for a nominal sum.

The properties in Franklinville, New York and Titusville, Pennsylvania are owned by the Company with no related encumbrances.

As previously reported by the Company, in November 2009 the Company became the operating lessee of real property located in Nashville, Arkansas. The lessor is a related party. The lease was for a period of one year and conferred on the Company an option to purchase the property at the appraised value of \$506,000. The lease expired in November 2010, was extended until November 2011, and extended again until November 2012. The Company has not exercised its purchase option. In the event the Company is successful in obtaining certain tax and/or other incentives from the state the entity operates in, the Company will be required to purchase the building. See Note 10, Related Party Transactions, of the accompanying consolidated financial statements for additional information.

The Company is currently reviewing its manufacturing efficiencies at the Company's various locations and facilities for the manufacture of CPG products. Certain of the operations and facilities are expected to benefit from the evaluations and/or possible consolidation from the perspective of the manufacturing cycle, available manufacturing techniques and current technologies. It appears that the results of this evaluation may result in recommendations for the expansion of manufacturing at the more efficient locations that have the capacity for expansion and the appropriate corresponding consolidation of other CPG manufacturing capabilities. This analysis in combination with current insurance and/or property tax rates may result in initial non-recurring charges that may be expensed immediately upon their determination and have inherent benefit paybacks from manufacturing efficiencies and/or reductions in ongoing insurance and/or property tax rates as such savings are realized.

See the accompanying consolidated financial statements, including Note 9, Commitments, thereto, for further information with respect to the Company's lease commitments.

Item 3. Legal Proceedings

There are no legal proceedings which are material to the Company currently pending by or against the Company other than ordinary routine litigation incidental to the business which is not expected to have a material adverse affect on the business or earnings of the Company.

Item 4. Mine Safety Disclosures

Not applicable.

PART II

Item 5. Market for Registrant's Common Equity, Related Stockholder Matters and Issuer Purchases of Equity Securities

(a) Price Range of Common Stock

The following table shows the range of high and low prices for the Company's common stock as reported by the NYSE Amex (symbol SVT) for 2011 and 2010.

	<u>High</u>	<u>Low</u>
2011		
Fourth Quarter	\$ 9.37	\$ 8.26
Third Quarter	9.24	8.18
Second Quarter	9.51	8.59
First Quarter	9.79	8.29
2010		
Fourth Quarter	\$ 10.25	\$ 8.05
Third Quarter	10.00	8.15
Second Quarter	10.04	8.03
First Quarter	11.00	8.21

(b) Approximate Number of Holders of Common Stock

Title of class	Approximate number of record holders (as of <u>February 29, 2012</u>)
Common Stock, \$.20 par value per share	386

(c) Dividends on Common Stock

On February 22, 2010, the Company announced that its Board of Directors declared a \$0.15 per share cash dividend. The dividend was paid on March 31, 2010 to shareholders of record on March 10, 2010 and was approximately \$336,000 in the aggregate.

On April 4, 2011, the Company announced that its Board of Directors declared a \$0.15 per share cash dividend. The dividend was paid on May 20, 2011 to shareholders of record on April 29, 2011 and was approximately \$336,000 in the aggregate.

On November 8, 2011, the Company announced that its Board of Directors declared a \$0.15 per share cash dividend. The dividend was paid on December 16, 2011 to shareholders of record on November 28, 2011 and was approximately \$346,000 in the aggregate. This dividend does not represent that the Company will pay dividends on a regular or scheduled basis.

(d) Company Purchases of Company's Equity Securities

<u>Period</u>	<u>Total Number of Shares Purchased</u>	<u>Weighted Average Price \$ Paid Per Share</u>	<u>Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs</u>	<u>Maximum Number of Shares that may yet be Purchased under the Plans or Programs</u>
January 1 – December 31, 2011	-	-	-	211,912
Total	-	-	-	211,912

In January 2006, the Board of Directors authorized the purchase of up to 250,000 shares of the Company's outstanding common stock. The shares may be purchased in the open market or in privately negotiated transactions; and at times and in amounts that the Company deems appropriate. On October 31, 2008, the Company announced that its Board of Directors authorized the purchase of an additional 200,000 shares of the Company's common stock under the Company's current purchase program. As of February 29, 2012 the Company has purchased 238,088 shares and there remain 211,912 shares available to purchase under this program. There were no shares repurchased under the program during 2011 and 2010. See also Item 12.

Item 6. Selected Financial Data

The Company is a smaller reporting company by Rule 12b-2 of the Exchange Act and is not required to provide the information required under this item.

Item 7. Management's Discussion and Analysis of Financial Condition and Results of Operations

Business Overview

The aviation and aerospace industries as well as markets for the Company's consumer products are facing new and evolving challenges on a global basis. The operations of the Company can be affected by the trends of the economy, including interest rates, income tax laws, government regulation, legislation, and other factors. In addition, uncertainties in today's global economy, competition from expanding manufacturing capabilities and technical sophistication of low-cost developing countries, particularly in South and East Asia, currency policies in relation to the U.S. dollar of some major foreign exporting countries so as to maintain or increase a pricing advantage of their exports vis-à-vis U.S. manufactured goods, the effect of terrorism, difficulty in predicting defense and other government appropriations, the vitality of the commercial aviation industry and its ability to purchase new aircraft, the willingness and ability of the Company's customers to fund long-term purchase programs, volatile market demand and the continued market acceptance of the Company's advanced technology and cutlery products make it difficult to predict the impact on future financial results.

Both the ATG and CPG markets are sensitive to domestic and foreign economic conditions and policies, which may create volatility in operating results, from period to period. For example, the airline industry is sensitive to fuel price increases and economic conditions. These factors directly impact the demand for aircraft production as well as the amount of repair and overhaul required on in-service aircraft.

Government procurements are subject to Congressional appropriations and priorities that may change from year to year. Such changes could result in, but are not limited thereto, the expansion and/or contraction of Government procurement requirements, a reduction in funding, the continuation or termination of existing programs, the introduction of new programs requiring the funds that were originally directed to current programs, a stretch-out in Government delivery requirements or

such other U.S. Government determinations that could result in increases or reductions of Government purchase orders for the ATG and/or the CPG products.

The Company's suppliers are also subject to all the pressures and volatility being generated by the current global economic conditions. Any interruption of the Company's continuous flow of material and product parts that are required for the manufacture of the Company's products could adversely impact the Company's ability to meet the Company's customers' delivery requirements. Consistent with the evolving requirements of the Aerospace Industry, companies are increasingly being requested to operate under Long-Term Agreements with their Customers on the basis of fixed prices, on the basis of targeted year to year price reductions and/or on the basis of year to year price adjustments predicated on mutually agreed indices and/or a combination of some or all of the above described pricing arrangements and/or otherwise. Therefore, productivity improvements and cost containment strategies are continuously sought within the Company's concept of continuous improvement. The Company's products are labor intensive and as such productivity improvements are expected to have positive effects on the Company's operating results. However, increased costs for raw material, purchased parts and/or labor will have the reverse effect. Therefore, there are strong incentives to continuously improve productivity and to contain/reduce costs.

If any adverse economic events reduce the number of Airliners and/or Aircraft being produced by the Company's relevant prime contractors, the negative effects of that reduction will in turn flow down through the supply chain. Also, certain major manufacturers have successfully imposed extended payment terms to their suppliers. At times, these extended terms of payment are not available to the Company when purchasing raw material such as aluminum, magnetic material, steel, etc. and/or other product support items and services. If the Company's customers delay their payments until after the extended due date or fail to pay, it could adversely impact the Company's operating results.

The Company's ability to manufacture products on a timely basis also depends on the Company's Suppliers' on-time delivery of raw material, sub components, machined parts and other necessary product support supplies. Interruptions of this flow of purchased materials could adversely affect the Company's operations.

Maximizing the Company's operations requires continued dedicated performances from the Company's key and other personnel. In the Company's markets and business arenas there is substantial competition for the services of the highest performing individuals. Competitors, customers and other companies who may have interest in the Company's most experienced and educated/highly trained personnel (i.e., Managerial, Engineering and Accounting/Administrative) are a continuing consequence of the Company's history of successful operational performance. Any unplanned replacement of such personnel may require the hiring of new personnel on an expedited basis (provided they are available) and may temporarily interrupt the Company's operations and efforts for continuous improvement.

The final resolution of the U.S. and foreign economic uncertainties, notwithstanding the Stimulus Plans, may have significant adverse effects on access to capital markets and borrowings for all companies. However, the Company currently enjoys an attractive long-term debt/equity ratio and has a strong balance sheet.

Management Discussion

During the years ended December 31, 2011 and 2010, approximately 39% and 43%, respectively, of the Company's revenues were derived from contracts with agencies of the U.S. Government or their prime contractors and their subcontractors. Sales of products sold for government applications decreased when comparing the results of 2011 to 2010, due to decreased government shipments at the ATG partially offset by an increase in government shipments at the CPG. The Company believes that government involvement in military operations overseas will continue to have an impact on the financial results in both the Advanced Technology and Consumer Products markets. While the Company is optimistic in relation to these potential opportunities, it recognizes that sales to the government are affected by defense budgets, the foreign policies of the U.S. and other nations, the level of military operations and other factors and, as such, it is difficult to predict the impact on future financial results.

The Company's commercial business is affected by such factors as uncertainties in today's global economy, global competition, the vitality and ability of the commercial aviation industry to purchase new aircraft, the effects of terrorism and the threat of terrorism, market demand and acceptance both for the Company's products and its customers' products which incorporate Company made components.

The ATG continues its aggressive business development efforts in its primary markets and is broadening its activities to include new domestic and foreign markets that are consistent with its core competencies. There are substantial uncertainties in the current global economy that are compounded with certain airliner delivery ramp-ups and other delivery stretch-outs being considered and to a lesser degree, being implemented which in turn may adversely affect the Company's sales revenues

in 2012 and beyond. Although the ATG backlog continues to be strong, actual scheduled shipments may be delayed/changed as a function of the Company's customers final delivery determinations that may be based on changes in the global economy and other factors.

The Company's CPG develops new commercial products and products for government and military applications. Included in the significant uncertainties in the near and long term are the effects of the U. S. and world stimulus plans and the difficulty to accurately project the net effect of the vagaries inherent in the government procurement process and programs. The ATG and CPG continue to respond to U.S. government procurement requests for quotes. New product development activities are ongoing along with the acquisition and development of new product lines.

See also Note 12, Business Segments, of the accompanying consolidated financial statements for information concerning business segment operating results.

Results of Operations - Year 2011 as Compared to 2010

The following table compares the Company's statements of income data for the twelve months ended December 31, 2011 and 2010 (\$000's omitted).

	<u>Twelve Months Ended December 31,</u>				<u>2011 vs. 2010</u>	
	<u>2011</u>		<u>2010</u>		<u>Dollar</u>	<u>% Increase</u>
	<u>Dollars</u>	<u>% of Sales</u>	<u>Dollars</u>	<u>% of Sales</u>	<u>Change</u>	<u>(Decrease)</u>
Revenue:						
Advanced Technology	\$21,816	63.8%	\$19,301	61.0%	\$2,515	<u>13.0%</u>
Consumer Products	<u>12,365</u>	<u>36.2%</u>	<u>12,358</u>	<u>39.0%</u>	7	<u>0.1%</u>
	34,181	100.0%	31,659	100.0%	2,522	<u>8.0%</u>
Cost of goods sold, exclusive of depreciation and amortization	25,278	74.0%	22,900	72.3%	2,378	<u>10.4%</u>
Selling, general and administrative	5,019	14.7%	5,001	15.8%	18	<u>0.4%</u>
Depreciation and amortization	<u>686</u>	<u>2.0%</u>	<u>664</u>	<u>2.1%</u>	<u>22</u>	<u>3.3%</u>
Total costs and expenses	<u>30,983</u>	<u>90.7%</u>	<u>28,565</u>	<u>90.2%</u>	<u>2,418</u>	<u>8.5%</u>
Operating income	3,198	9.3%	3,094	9.8%	104	<u>3.4%</u>
Interest expense	65	0.2%	74	0.2%	(9)	<u>(12.2%)</u>
Other income, net	(162)	(0.5%)	(28)	(0.1%)	(134)	<u>478.6%</u>
Income tax provision	<u>669</u>	<u>2.0%</u>	<u>920</u>	<u>2.9%</u>	<u>(251)</u>	<u>(27.3%)</u>
Net income	<u>\$2,626</u>	<u>7.6%</u>	<u>\$2,128</u>	<u>6.8%</u>	<u>\$498</u>	<u>23.4%</u>

Revenue

The Company's consolidated revenues increased approximately \$2,522,000 or 8.0% for the twelve month period ended December 31, 2011 when compared to the same period in 2010. The increase in sales is the result of increased commercial shipments at the ATG. The increase in shipments is the result of increased demand from new and existing customers across various product lines.

Cost of Goods Sold

Cost of goods sold as a percentage of revenues increased from 72.3% to 74.0% for the twelve month period ended December 31, 2011 when compared to the same period in 2010 mainly due to the write off of start up costs associated with new product lines in the amount of approximately \$700,000 compared to \$500,000 for the twelve month periods ended December 31, 2011 and 2010. Variations in cost of goods sold as a percentage of sales is also largely dependent upon the mix of product sold within the operating groups as well as the relative percentage of each operating group's sales to total consolidated sales.

The Company continues to aggressively pursue cost saving opportunities in material procurements and other operating efficiencies through capital investments and technical developments in new machinery as well as investment and development of its labor force.

Selling, General and Administrative Expenses

Selling, general and administrative ("SG&A") expenses increased approximately \$18,000 or 0.4% for the twelve month period ended December 31, 2011 compared to the same period in 2010. Approximately 29% of selling, general and administrative expenses is attributable to the sale and marketing of products. This includes costs of internal and external sales force and active promotion and development of new and existing products. Selling costs increased approximately \$78,000 or

5% when comparing the twelve month period ended December 31, 2011 to the same period in 2010 mainly due to additional costs associated with shipments to customers.

Labor and labor related expenses for general and administrative support account for approximately 45% of total SG&A. These costs increased approximately \$61,000 mainly due to increased salaries and wages at the ATG when comparing the twelve month period ended December 31, 2011 to the same period in 2010. These increases were offset by decreases of approximately \$136,000 in other SG&A expenses for consulting, legal and professional services.

Interest Expense

Interest expense decreased for the twelve month period ended December 31, 2011 compared to the same period in 2010 primarily due to the decrease in the average outstanding debt. See also Note 4, Long-Term Debt, of the accompanying consolidated financial statements for information on long-term debt.

Depreciation and Amortization Expense

Depreciation and amortization expense increased for the twelve month period ended December 31, 2011 compared to the same period in 2010. Depreciation expense fluctuates due to estimated useful lives of depreciable property (as identified in Note 1, Business Description and Summary of Significant Accounting Policies, of the accompanying consolidated financial statements) as well as the amount and nature of capital expenditures in current and previous periods. It is anticipated that the Company's future capital expenditures will, at a minimum, follow the Company's requirements to support its delivery commitments and to meet the information technology related capital expenditure requirements.

Other Income

Components of other income include interest income on cash and cash equivalents, and other amounts not directly related to the sale of the Company's products. Other income is immaterial in relationship to the consolidated financial statements.

Income Taxes

The Company's effective tax rate was 20.3% in 2011 and 30.1% in 2010. The effective tax rate in both years reflects state income taxes, permanent non-deductible expenditures and the tax benefit for manufacturing deductions allowable under the American Jobs Creation Act of 2004. The effective tax rate decreased during 2011 as compared to 2010 primarily due to 2011 including additional benefits relating to ESOP dividend payments and other federal tax incentives. See also Note 7, Income Tax Provision, of the accompanying consolidated financial statements for information concerning income taxes.

Net Income

Net income increased \$498,000 or 23.4% when comparing the twelve month period ended December 31, 2011 to the same period in 2010. The increase in net income is primarily the result of increases in revenues at the Company's Advanced Technology Group combined with cost containment activities and negotiated pricing to maintain product margins as well as a decrease in tax expense due to the lower effective tax rate.

Results of Operations - Year 2010 as Compared to 2009

The following table compares the Company's statements of income data for the twelve months ended December 31, 2010 and 2009 (\$000's omitted).

	<u>Twelve Months Ended December 31,</u>				<u>2010 vs. 2009</u>	
	<u>2010</u>		<u>2009</u>		<u>Dollar</u>	<u>% Increase</u>
	<u>Dollars</u>	<u>% of Sales</u>	<u>Dollars</u>	<u>% of Sales</u>	<u>Change</u>	<u>(Decrease)</u>
Revenue:						
Advanced Technology	\$19,301	61.0%	\$18,000	54.5%	\$1,301	<u>7.2%</u>
Consumer Products	<u>12,358</u>	<u>39.0%</u>	<u>15,008</u>	<u>45.5%</u>	<u>(2,650)</u>	<u>(17.7%)</u>
	31,659	100.0%	33,008	100.0%	(1,349)	<u>(4.1%)</u>
Cost of goods sold, exclusive of depreciation and amortization	22,900	72.3%	24,968	75.6%	(2,068)	<u>(8.3%)</u>
Selling, general and administrative	5,001	15.8%	4,948	15.0%	53	<u>1.1%</u>
Depreciation and amortization	<u>664</u>	<u>2.1%</u>	<u>564</u>	<u>1.7%</u>	<u>100</u>	<u>17.7%</u>
Total costs and expenses	<u>28,565</u>	<u>90.2%</u>	<u>30,480</u>	<u>92.3%</u>	<u>(1,915)</u>	<u>(6.3%)</u>
Operating income	3,094	9.8%	2,528	7.7%	566	<u>22.4%</u>
Interest expense	74	0.2%	84	0.3%	(10)	<u>(11.9%)</u>
Other income	(28)	(0.1%)	(62)	(0.2%)	34	<u>(54.8%)</u>
Income tax provision	<u>920</u>	<u>2.9%</u>	<u>603</u>	<u>1.8%</u>	<u>317</u>	<u>52.6%</u>
Net income	<u>\$2,128</u>	<u>6.8%</u>	<u>\$1,903</u>	<u>5.8%</u>	<u>\$225</u>	<u>11.8%</u>

Revenue

The Company's consolidated revenues decreased approximately \$1,349,000 or 4.1% for the twelve month period ended December 31, 2010 when compared to the same period in 2009. The decrease in revenue is the result of decreased shipments for government related applications at both operating groups. Shipments for government applications were down approximately \$3,400,000 as a result of contract completion at CPG. Procurement and time of shipment under Government contracts can significantly impact operating results from period to period.

Cost of Goods Sold

Cost of goods sold as a percentage of sales decreased for the twelve month period ended December 31, 2010 when compared to the same period in 2009. The decrease is primarily the result of the mix of product sold within the ATG and CPG as well as a larger percentage (61% in 2010 as compared to 55% in 2009) of the total consolidated sales coming from the ATG which generally recognizes higher profit margins. Also during the twelve month period ended December 31, 2010, there were no reserves for cost overruns at year-end while there were approximately \$250,000 during the twelve month period ended December 31, 2009 that negatively impacted gross margins.

The Company continues to aggressively pursue cost saving opportunities in material procurements and other operating efficiencies through capital investments and technical developments in new machinery as well as investment and development of its labor force.

Selling, General and Administrative Expenses

Selling, general and administrative ("SG&A") expenses increased approximately \$53,000 or 1.1% for the twelve month period ended December 31, 2010 compared to the same period in 2009. Approximately 28% of selling, general and administrative expenses is attributable to the sale and marketing of products. This includes costs of internal and external sales force and active promotion and development of new and existing products, such costs increased approximately \$84,000 or 6% when comparing the twelve month period ended December 31, 2010 to the same period in 2009.

Labor and related expenses for general and administrative support account for approximately 44% of total SG&A. These costs increased approximately \$435,000 mainly due to hiring of new employees when comparing the twelve month period ended December 31, 2010 to the same period in 2009. These increases were more than offset by decreases of approximately \$537,000 in information technology costs as well as reductions in legal and professional expenses associated with previously reported merger and acquisition activities.

Interest Expense

Interest expense decreased for the twelve month period ended December 31, 2010 compared to the same period in 2009 due to the decrease in the average outstanding debt and interest rates for the majority of 2010. See also Note 4, Long-Term Debt, of the accompanying consolidated financial statements for information on long-term debt.

Depreciation and Amortization Expense

Depreciation and amortization expense increased for the twelve month period ended December 31, 2010 compared to the same period in 2009. Depreciation expense fluctuates due to estimated useful lives of depreciable property (as identified in Note 1, Business Description and Summary of Significant Accounting Policies, of the accompanying consolidated financial statements) as well as the amount and nature of capital expenditures in current and previous periods. Depreciation and amortization expense also increased \$70,000 due to 2010 being the first full year of depreciation of the machinery and equipment under the \$588,000 capital lease with related party. It is anticipated that the Company's future capital expenditures will, at a minimum, follow the Company's requirements to support its delivery commitments and to meet the information technology related capital expenditure requirements.

Other Income

Components of other income include interest income on cash and cash equivalents, and other amounts not directly related to the sale of the Company's products. The decrease in other income for the twelve month period ended December 31, 2010 when compared to the same twelve month period in 2009 is primarily due to the market driven decline in interest rates on cash and cash equivalents.

Income Taxes

The Company's effective tax rate was 30.1% in 2010 and 24.0% in 2009. The effective tax rate in both years reflects state income taxes, permanent non-deductible expenditures and the tax benefit for manufacturing deductions allowable under the American Jobs Creation Act of 2004. The effective tax rate increased during 2010 as compared to 2009 primarily due to 2009 including additional benefits relating to prior period ESOP dividend payments and R&D tax credits. See also Note 7, Income Tax Provision, of the accompanying consolidated financial statements for information concerning income taxes.

Net Income

Net income increased \$225,000 or 11.8% when comparing the twelve month period ended December 31, 2010 to the same period in 2009. The increase in net income is primarily the result of increases in revenues at the Company's Advanced Technology Group. The Company improved the margin on sales at both the ATG and CPG because of the mix of products sold as well as successful cost containment activities.

Liquidity and Capital Resources

The Company's primary liquidity and capital requirements relate to working capital needs; primarily inventory, accounts receivable, capital expenditures for property, plant and equipment and principal and interest payments on debt. At December 31, 2011, the Company had working capital of approximately \$20,483,000 (\$18,838,000 – 2010) of which approximately \$4,948,000 (\$4,447,000 – 2010) was comprised of cash and cash equivalents.

The Company generated approximately \$2,602,000 in cash from operations during the twelve months ended December 31, 2011 as compared to \$1,932,000 during the twelve months ended December 31, 2010. Cash was generated from operations through net income as well as timing differences of prepaid income taxes. The primary uses of cash for the Company's operating activities for the twelve months ended December 31, 2011 include payments of approximately \$511,000 in income taxes, increases in accounts receivable of \$604,000 and increases of \$697,000 in inventory. ATG and CPG customers are increasingly requesting and/or requiring stock inventory in order to facilitate assurance of meeting their often volatile delivery schedule needs. As these requirements increase, they directly impact comparative cash flows when implemented and increased inventory levels when it is a continuing requirement. Additionally, at times, the Company takes advantage of price discounts on volume purchases for common parts. Cash generated and used in operations is consistent with sales volume, customer expectations and competitive pressures. The Company's primary use of cash in its financing and investing activities in the twelve months ended December 31, 2011 included approximately \$323,000 of current principal payments on long-term debt, as well as approximately \$682,000 for cash dividends paid on May 20, 2011 and December 16, 2011 and \$517,000 to purchase unexercised outstanding stock options. The Company also expended approximately \$608,000 for capital expenditures.

At December 31, 2011, there are no material commitments for capital expenditures.

The Company also has an unsecured \$1,000,000 line of credit on which there was no balance outstanding at December 31, 2011 or 2010. If needed, this can be used to fund cash flow required for operations. The Company believes that it has adequate internal and external resources available to fund expected working capital and capital expenditure requirements through fiscal 2012 as supported by the level of cash/cash equivalents on hand, cash flow from operations and bank lines of credit.

Off Balance Sheet Arrangements

None.

Critical Accounting Policies

The Company prepares its consolidated financial statements in accordance with GAAP. As such, the Company is required to make certain estimates, judgments and assumptions that the Company believes are reasonable based upon the information available. These estimates and assumptions affect the reported amounts of assets and liabilities as of the date of the consolidated financial statements and the reported amounts of revenues and expenses during the periods presented. Actual results could differ significantly from those estimates under different assumptions and conditions. The Company believes that the following discussion addresses the Company's most critical accounting policies, which are those that are most important to the portrayal of the Company's financial condition and results of operations and which require the Company's most difficult and subjective judgments, often as a result of the need to make estimates about the effect of matters that are inherently uncertain. Note 1, Business Description and Summary of Significant Accounting Policies, of the accompanying consolidated financial statements includes a summary of the significant accounting policies used in the preparation of the consolidated financial statements.

Revenue Recognition

Revenues are recognized as services are rendered or as units are shipped at the designated FOB point consistent with the transfer of title, risks and rewards of ownership. Such purchase orders generally include specific terms relative to quantity, item description, specifications, price, customer responsibility for in-process costs, delivery schedule, shipping point, payment and other standard terms and conditions of purchase.

Inventories

Inventories are stated at the lower of standard cost or net realizable value. Cost includes all costs incurred to bring each product to its present location and condition, which approximates actual cost (first-in, first-out). Market provisions in respect to net realizable value and obsolescence are applied to the gross value of the inventory. Pre-production and start-up costs are expensed as incurred.

Employee Benefit Plans

The Company provides a range of benefits to its employees and retired employees. The Company records annual amounts relating to these plans based on calculations specified by GAAP, which includes various actuarial assumptions, such as discount rates, assumed rates of return on plan assets and health care cost trend rates. The Company believes that the assumptions utilized in recording its obligations under its plans are reasonable based on advice from its actuaries.

Use of Estimates

The preparation of the consolidated financial statements in conformity with GAAP 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. Such estimates include, but are not limited to, reserves and allowances for inventories and trade receivables. Actual results could differ from those estimates.

Income Taxes

The Company recognizes deferred tax liabilities and assets for the expected future tax consequences of operating loss and credit carryforwards and temporary differences between the carrying amounts and the tax basis of assets and liabilities.

Recent Accounting Pronouncements

In June 2011, the FASB issued new accounting guidance related to the presentation of comprehensive income that eliminates the option to present components of other comprehensive income as part of the statement of changes in shareholders' equity. The amendments require that all nonowner changes in stockholders' equity be presented either in a single continuous statement of comprehensive income or in two separate but consecutive statements. The amendments do not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. This guidance is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011, with early adoption permitted. The Company will adopt this new pronouncement in the first quarter of 2012. The Company is currently evaluating which presentation option it will utilize for reporting comprehensive income in its consolidated financial statements.

Item 7A. Quantitative and Qualitative Disclosures About Market Risk

The Company is a smaller reporting company by Rule 12b-2 of the Exchange Act and is not required to provide the information required under this item.

Item 8. Financial Statements and Supplementary Data

The consolidated financial statements of the Company which are included in this Form 10-K Annual Report are described in the accompanying Index to Consolidated Financial Statements on Page F1.

Item 9. Changes in and Disagreements with Accountants on Accounting and Financial Disclosure

None.

Item 9A. Controls and Procedures

(i) Disclosure Controls and Procedures

The Company carried out an evaluation under the supervision and with the participation of its management, including the Company's Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"), of the effectiveness of the Company's disclosure controls and procedures (as defined in Exchange Act Rule 13a-15(e)) as of December 31, 2011. Based upon that evaluation, the CEO and CFO concluded that the Company's disclosure controls and procedures are effective to ensure that the information required to be disclosed by the Company in SEC reports under the Exchange Act (i) is recorded, processed, summarized and reported within the time periods specified in SEC rules and forms, and (ii) is accumulated and communicated to the Company's management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure.

(ii) Management's Report on Internal Control over Financial Reporting

The Company's management is responsible for establishing and maintaining adequate internal controls over financial reporting (as defined in Exchange Act Rule 13a-15(f)). Under the supervision and with the participation of management, including the CEO and CFO, the Company conducted an evaluation of the effectiveness of internal control over financial reporting based on the framework in Internal Control – Integrated Framework issued by the Committee of Sponsoring Organizations of the Treasury Commission. Based on the Company's evaluation under the framework, management concluded that the Company's internal control over financial reporting was effective as of December 31, 2011.

(iii) Changes in Internal Control Over Financial Reporting

There were no changes in the Company's internal controls over financial reporting during the fourth quarter of 2011 that have materially affected, or are reasonably likely to affect, the Company's internal controls over financial reporting.

Item 9B. Other Information

None.

PART III

Item 10. Directors, Executive Officers and Corporate Governance

Information regarding directors and executive officers of the Company, compliance with Section 16(a) of the Securities Exchange Act and the Company's Audit Committee, its members and the Audit Committee financial expert is incorporated herein by reference to the information included in the Company's definitive proxy statement if it is filed with the Commission within 120 days after the end of the Company's 2011 fiscal year or such information will be included by amendment to this Form 10-K.

Code of Ethics

The Company has adopted a Code of Ethics and Business Conduct that applies to all directors, officers and employees of the Company as required by the listing standards of the NYSE Amex. The Code is available on the Company's website at www.servotronics.com and the Company intends to disclose on this website any amendment to the Code. Waivers under the Code, if any, will be disclosed under the rules of the SEC and the NYSE Amex.

Item 11. Executive Compensation

Information regarding executive compensation is incorporated herein by reference to the information included in the Company's definitive proxy statement if it is filed with the Commission within 120 days after the end of the Company's 2011 fiscal year or such information will be included by amendment to this Form 10-K.

Item 12. Security Ownership of Certain Beneficial Owners and Management and Related Stockholder Matters

Securities Authorized for Issuance Under Equity Compensation Plans

The following table sets forth the securities authorized for issuance under the Company's equity compensation plans as of December 31, 2011.

<u>Plan category</u>	<u>Number of securities to be issued upon exercise of outstanding options, warrants and rights (a)</u>	<u>Weighted-average exercise price of outstanding options, warrants and rights (b)</u>	<u>Number of securities remaining available for future issuance under equity compensation plans (excluding securities reflected in column (a)) (c)</u>
Equity compensation plans approved by security holders	108,500	\$3.60	0
Equity compensation plans not approved by security holders	<u>0</u>	<u>0</u>	<u>0</u>
Total	<u>108,500</u>	<u>\$3.60</u>	<u>0</u>

Information regarding security ownership of certain beneficial owners and management is incorporated herein by reference to the information included in the Company's definitive proxy statement if it is filed with the Commission within 120 days after the end of the Company's 2011 fiscal year or such information will be included by amendment to this Form 10-K.

Also incorporated by reference is the information in the table under the heading "Securities Authorized for Issuance Under Equity Compensation Plans" included in Item 5 of this Form 10-K.

Item 13. Certain Relationships and Related Transactions and Director Independence

Information regarding certain relationships and related transactions and director independence is incorporated herein by reference to the information included in the Company's definitive proxy statement if it is filed with the Commission within 120 days after the end of the Company's 2011 fiscal year or such information will be included by amendment to this Form 10-K.

Item 14. Principal Accountant Fees and Services

Information regarding principal accountant fees and services is incorporated herein by reference to the information included in the Company's definitive proxy statement if it is filed with the Commission within 120 days after the end of the Company's 2011 fiscal year or such information will be included by amendment to this Form 10-K.

PART IV

Item 15. The information in Part IV (except the list of Exhibits and Signatures) is contained in the Company's Proxy Statement.

FORWARD-LOOKING STATEMENTS

In addition to historical information, certain sections of this Form 10-K contain forward-looking statements within the meaning of Section 27A of the Securities Act of 1933 and Section 21E of the Securities Exchange Act of 1934, such as those pertaining to the Company's capital resources and profitability. Forward-looking statements involve numerous risks and uncertainties. The Company derives a material portion of its revenues from contracts with agencies of the U.S. Government or their prime contractors. The Company's business is performed under fixed price contracts and the following factors, among others discussed herein, could cause actual results and future events to differ materially from those set forth or contemplated in the forward-looking statements: uncertainties in today's global economy, global competition, difficulty in predicting defense appropriations, the vitality of the commercial aviation industry and its ability to purchase new aircraft, the willingness and ability of the Company's customers to fund long-term purchase programs and market demand and acceptance both for the Company's products and its customers' products which incorporate Company-made components. The operations of the Company can be affected by the trends of the economy, including interest rates, income tax laws, governmental regulation, legislation, population changes and those factors discussed elsewhere in this Form 10-K. Readers are cautioned not to place undue reliance on forward-looking statements, which reflect management's analysis only as the date hereof. The Company assumes no obligation to update forward-looking statements.

SERVOTRONICS, INC. AND SUBSIDIARIES
INDEX TO CONSOLIDATED FINANCIAL STATEMENTS

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 Consolidating financial statement schedules are omitted because they are not applicable to smaller reporting companies.	

Report of Independent Registered Public Accounting Firm

To the Board of Directors and Shareholders
Servotronics, Inc. and Subsidiaries

We have audited the accompanying consolidated balance sheets of Servotronics, Inc. and Subsidiaries (the “Company”) as of December 31, 2011 and 2010, and the related consolidated statements of income and cash flows for the years then ended. These financial statements are the responsibility of the Company’s management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. The Company is not required to have, nor were we engaged to perform an audit of its internal control over financial reporting. Our audits included consideration of internal control over financial reporting as a basis for designing audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Company’s internal control over financial reporting. Accordingly, we express no such opinion. An audit also includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of Servotronics, Inc. and Subsidiaries as of December 31, 2011 and 2010, and the results of its operations and its cash flows for the years then ended in conformity with U.S. generally accepted accounting principles.

/s/ Freed Maxick CPAs, P.C. (Formerly known as Freed Maxick & Battaglia, CPAs, PC)
Buffalo, New York

March 29, 2012

SERVOTRONICS, INC. AND SUBSIDIARIES
CONSOLIDATED BALANCE SHEETS
(\$000's omitted except share and per share data)

	December 31,	
Assets	<u>2011</u>	<u>2010</u>
Current assets:		
Cash and cash equivalents	\$ 4,948	\$ 4,447
Accounts receivable, net	6,031	5,427
Inventories, net	11,607	11,032
Prepaid income taxes	133	226
Deferred income taxes	754	567
Other assets	<u>505</u>	<u>352</u>
Total current assets	23,978	22,051
Property, plant and equipment, net	6,103	6,159
Other non-current assets	<u>342</u>	<u>296</u>
Total Assets	<u>\$ 30,423</u>	<u>\$ 28,506</u>
Liabilities and Shareholders' Equity		
Current liabilities:		
Current portion of long-term debt	\$ 202	\$ 323
Current portion of capital lease related party	81	81
Accounts payable	1,451	1,247
Accrued employee compensation and benefit costs	1,434	1,332
Other accrued liabilities	<u>327</u>	<u>230</u>
Total current liabilities	3,495	3,213
Long-term debt	2,855	3,058
Long-term portion of capital lease related party	333	414
Deferred income taxes	496	509
Shareholders' equity:		
Common stock, par value \$.20; authorized 4,000,000 shares; issued 2,614,506 shares; outstanding 2,074,257 (1,981,877 – 2010) shares	523	523
Capital in excess of par value	13,774	13,491
Retained earnings	12,490	11,467
Accumulated other comprehensive loss	(67)	(78)
Employee stock ownership trust commitment	(1,266)	(1,367)
Treasury stock, at cost 305,135 (377,135 – 2010) shares	<u>(2,210)</u>	<u>(2,724)</u>
Total shareholders' equity	<u>23,244</u>	<u>21,312</u>
Total Liabilities and Shareholders' Equity	<u>\$ 30,423</u>	<u>\$ 28,506</u>

See notes to consolidated financial statements

SERVOTRONICS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF INCOME
(\$000's omitted except per share data)

	Years Ended December 31,	
	<u>2011</u>	<u>2010</u>
Revenue	\$ 34,181	\$ 31,659
Costs, expenses and other income:		
Cost of goods sold, exclusive of depreciation and amortization	25,278	22,900
Selling, general and administrative	5,019	5,001
Interest expense	65	74
Depreciation and amortization	686	664
Other income, net	<u>(162)</u>	<u>(28)</u>
	<u>30,886</u>	<u>28,611</u>
Income before income tax provision	3,295	3,048
Income tax provision	<u>669</u>	<u>920</u>
Net income	<u><u>\$ 2,626</u></u>	<u><u>\$ 2,128</u></u>
Income per share:		
Basic		
Net income per share	<u><u>\$ 1.31</u></u>	<u><u>\$ 1.08</u></u>
Diluted		
Net income per share	<u><u>\$ 1.24</u></u>	<u><u>\$ 1.01</u></u>

See notes to consolidated financial statements

SERVOTRONICS, INC. AND SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CASH FLOWS
(\$000's omitted)

	Years Ended December 31,	
	<u>2011</u>	<u>2010</u>
Cash flows related to operating activities:		
Net income	\$ 2,626	\$ 2,128
Adjustments to reconcile net income to net cash generated in operating activities -		
Depreciation and amortization	686	664
Deferred income taxes (benefit)	(206)	(23)
Increase in inventory reserve	122	103
Change in assets and liabilities:		
Accounts receivable	(604)	(1,340)
Inventories	(697)	391
Prepaid income taxes	376	161
Other assets	(168)	98
Other non-current assets	(54)	(104)
Accounts payable	204	132
Accrued employee compensation and benefit costs	119	246
Other accrued liabilities	97	(625)
Employee stock ownership trust payment	<u>101</u>	<u>101</u>
Net cash generated in operating activities	<u>2,602</u>	<u>1,932</u>
Cash flows related to investing activities:		
Capital expenditures - property, plant and equipment	(608)	(492)
Proceeds from certificates of deposit	<u>-</u>	<u>495</u>
Net cash (used) generated in investing activities	<u>(608)</u>	<u>3</u>
Cash flows related to financing activities:		
Principal payments on long-term debt	(323)	(323)
Principal payments on capital lease related party	(81)	(81)
Cash dividend	(682)	(336)
Purchase of stock options	(517)	(573)
Proceeds from exercise of stock options	<u>110</u>	<u>-</u>
Net cash used in financing activities	<u>(1,493)</u>	<u>(1,313)</u>
Net increase in cash and cash equivalents	<u>501</u>	<u>622</u>
Cash and cash equivalents at beginning of year	<u>4,447</u>	<u>3,825</u>
Cash and cash equivalents at end of year	<u>\$ 4,948</u>	<u>\$ 4,447</u>
Supplemental disclosures:		
Income taxes paid	<u>\$ 511</u>	<u>\$ 754</u>
Interest paid	<u>\$ 65</u>	<u>\$ 74</u>

See notes to consolidated financial statements

SERVOTRONICS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. Business Description and Summary of Significant Accounting Policies

Business Description

Servotronics, Inc. and its subsidiaries design, manufacture and market advanced technology products consisting primarily of control components and consumer products consisting of knives and various types of cutlery and other edged products.

Principles of Consolidation

The consolidated financial statements include the accounts of Servotronics, Inc. and its wholly-owned subsidiaries (the "Company"). All intercompany balances and transactions have been eliminated upon consolidation.

Cash and Cash Equivalents

The Company considers cash and cash equivalents to include all cash accounts and short-term investments purchased with an original maturity of three months or less.

Accounts Receivable

The Company grants credit to substantially all of its customers and carries its accounts receivable at original invoice amount less an allowance for doubtful accounts. On a periodic basis, the Company evaluates its accounts receivable and establishes an allowance for doubtful accounts based on history of past write-offs, collections, and current credit conditions. The allowance for doubtful accounts amounted to approximately \$101,000 at December 31, 2011 and \$117,000 at December 31, 2010.

Revenue Recognition

Revenues are recognized as services are rendered or as units are shipped and at the designated FOB point consistent with the transfer of title, risks and rewards of ownership. Such purchase orders generally include specific terms relative to quantity, item description, specifications, price, customer responsibility for in-process costs, delivery schedule, shipping point, payment and other standard terms and conditions of purchase.

Inventories

Inventories are stated at the lower of cost or net realizable value. Cost includes all cost incurred to bring each product to its present location and condition. Market provisions in respect of lower of cost or market adjustments and inventory expected to be used in greater than one year are applied to the gross value of the inventory through a reserve of approximately \$773,000 and \$651,000 at December 31, 2011 and 2010, respectively. Pre-production and start-up costs are expensed as incurred.

The purchase of suppliers' minimum economic quantities of material such as steel, etc. may result in a purchase of quantities exceeding one year of customer requirements. Also, in order to maintain a reasonable and/or agreed to lead time, certain larger quantities of other product support items may have to be purchased and may result in over one year's supply.

Shipping and Handling Costs

Shipping and handling costs are classified as a component of cost of goods sold.

Property, Plant and Equipment

Property, plant and equipment is carried at cost; expenditures for new facilities and equipment and expenditures which substantially increase the useful lives of existing plant and equipment are capitalized; expenditures for maintenance and repairs are expensed as incurred. Upon disposal of properties, the related cost and accumulated depreciation are removed from the respective accounts and any profit or loss on disposition is included in income.

Depreciation is provided on the basis of estimated useful lives of depreciable properties, primarily by the straight-line method for financial statement purposes and by accelerated methods for tax purposes. Depreciation expense includes the amortization of capital lease assets. The estimated useful lives of depreciable properties are generally as follows:

Buildings and improvements	5-39 years
Machinery and equipment	5-15 years
Tooling	3-5 years

SERVOTRONICS, INC. AND SUBSIDIARIES

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Income Taxes

The Company recognizes deferred tax liabilities and assets for the expected future tax consequences of operating loss and credit carryforwards and temporary differences between the carrying amounts and the tax basis of assets and liabilities. The Company and its subsidiaries file a consolidated federal income tax return, a consolidated New York State income tax return and a separate Pennsylvania, Arkansas and Texas state income tax returns.

The Company's practice is to recognize interest and/or penalties related to income tax matters in income tax expense. The Company did not have any accrued interest or penalties included in its consolidated balance sheets at December 31, 2011 or 2010, and did not recognize any interest and/or penalties in its consolidated statements of income during the years ended December 31, 2011 and 2010.

During the third quarter of 2009, the New York State Department of Taxation and Finance ("NYS") commenced an examination of the Company's New York State franchise tax returns for the years 2005 through 2007. In the third quarter of 2010, the examination was completed and resulted in no change to the Company's originally filed returns. Also, during the third quarter of 2010, the Internal Revenue Service commenced an examination of the Company's Federal income tax returns for the years 2008 and 2009. In the first quarter of 2011, the examination was completed and resulted in no material adjustments to the Company's originally filed returns. The 2008 through 2010 federal and state tax returns remain open under statute.

Employee Stock Ownership Plan

Contributions to the employee stock ownership plan are determined annually by the Company according to plan formula.

Impairment of Long-Lived Assets

The Company reviews long-lived assets for impairment whenever events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable based on undiscounted future operating cash flow analyses. If an impairment is determined to exist, any related impairment loss is calculated based on fair value. Impairment losses on assets to be disposed of, if any, are based on the estimated proceeds to be received, less costs of disposal. The Company has determined that no impairment of long lived assets existed at December 31, 2011 and 2010.

Use of Estimates

The preparation of the consolidated financial statements in conformity with U.S. generally accepted accounting principles ("GAAP") 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.

Research and Development Costs

Research and development costs are expensed as incurred.

Concentration of Credit Risks

Financial instruments that potentially subject the Company to concentration of credit risks principally consist of cash accounts in financial institutions. Although the accounts exceed the federally insured deposit amount, management does not anticipate nonperformance by the financial institutions. Refer to Note 12, Business Segments, for disclosures related to customer concentrations.

Fair Value of Financial Instruments

The carrying amount of cash and cash equivalents, accounts receivable, inventories, accounts payable and accrued expenses are reasonable estimates of their fair value due to their short maturity. Based on variable interest rates and the borrowing rates currently available to the Company for loans similar to its long-term debt, the fair value approximates its carrying amount.

Recent Accounting Pronouncements

In June 2011, the FASB issued new accounting guidance related to the presentation of comprehensive income that eliminates the option to present components of other comprehensive income as part of the statement of changes in shareholders' equity. The amendments require that all nonowner changes in stockholders' equity be presented either in a single continuous

SERVOTRONICS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

statement of comprehensive income or in two separate but consecutive statements. The amendments do not change the items that must be reported in other comprehensive income or when an item of other comprehensive income must be reclassified to net income. This guidance is effective for fiscal years, and interim periods within those years, beginning after December 15, 2011, with early adoption permitted. The Company will adopt this new pronouncement in the first quarter of 2012. The Company is currently evaluating which presentation option it will utilize for reporting comprehensive income in its consolidated financial statements.

Reclassifications

Certain balances as of December 31, 2010 were reclassified to conform with classifications adopted in the current year.

2. Inventories

	December 31,	
	<u>2011</u>	<u>2010</u>
	(\$000's omitted)	
Raw materials and common parts	\$ 5,727	\$ 5,491
Work-in-process	3,511	3,358
Finished goods	<u>2,369</u>	<u>2,183</u>
Total inventories, net of reserve	<u>\$11,607</u>	<u>\$11,032</u>

3. Property, Plant and Equipment

	December 31,	
	<u>2011</u>	<u>2010</u>
	(\$000's omitted)	
Land	\$ 25	\$ 25
Buildings	7,181	7,060
Machinery, equipment and tooling (including capital lease)	<u>12,930</u>	<u>12,444</u>
	20,136	19,529
Less accumulated depreciation and amortization	<u>(14,033)</u>	<u>(13,370)</u>
Total property, plant and equipment	<u>\$ 6,103</u>	<u>\$ 6,159</u>

Property, plant and equipment includes land and building in Elma, New York, under a \$5,000,000 capital lease which can be purchased for a nominal amount at the end of the lease term. As of December 31, 2011 and 2010, accumulated amortization on the building amounted to approximately \$2,423,000 and \$2,293,000, respectively. Amortization expense amounted to \$130,000 for the twelve month periods ended December 31, 2011 and 2010, respectively. The associated current and long-term liabilities are discussed in Note 4, Long-Term Debt, of the accompanying consolidated financial statements. Property, plant and equipment also includes machinery and equipment under a \$588,000 capital lease with a related party. As of December 31, 2011 and 2010, accumulated amortization on the machinery and equipment amounted to approximately \$182,000 and \$98,000, respectively. Amortization expense amounted to \$84,000 for each of the twelve month periods ended December 31, 2011 and 2010, respectively. The associated current and long-term liabilities are discussed in Note 5, Capital Lease – Related Party, of the accompanying consolidated financial statements.

Depreciation expense amounted to \$449,000 and \$427,000 for the twelve month periods ended December 31, 2011 and 2010, respectively. The combined depreciation and amortization expense were \$686,000 and \$664,000 for the twelve month periods ended December 31, 2011 and 2010, respectively. The Company believes that it maintains property and casualty insurance in amounts adequate for the risk and nature of its assets and operations and which are generally customary in its industry.

SERVOTRONICS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

4. Long-Term Debt

	December 31,	
	<u>2011</u>	<u>2010</u>
	(\$000's omitted)	
Industrial Development Revenue Bonds; secured by an equivalent letter of credit from a bank with interest payable monthly at a floating rate (0.38% at December 31, 2011)(A)	\$ 2,960	\$ 3,130
Term loan payable to a financial institution; interest at LIBOR plus 2%; quarterly principal payments of \$26,786 through the fourth quarter of 2011	-	107
Secured term loan payable to a government agency; monthly payments of \$1,950 including interest fixed at 3% payable through fourth quarter of 2015	86	107
Secured term loan payable to a government agency; monthly principal payments of approximately \$2,200 with interest waived payable through second quarter of 2012	<u>11</u>	<u>37</u>
	3,057	3,381
Less current portion	<u>(202)</u>	<u>(323)</u>
	<u><u>\$ 2,855</u></u>	<u><u>\$ 3,058</u></u>

(A) The Industrial Development Revenue Bonds were issued by a government agency to finance the construction of the Company's headquarters/advanced technology facility. Annual sinking fund payments of \$170,000 commenced December 1, 2000 and continue through 2013, with a final payment of \$2,620,000 due December 1, 2014. The Company has agreed to reimburse the issuer of the letter of credit if there are draws on that letter of credit. The Company pays the letter of credit bank an annual fee of 1% of the amount secured thereby and pays the remarketing agent for the bonds an annual fee of .25% of the principal amount outstanding. The Company's interest under the facility capital lease has been pledged to secure its obligations to the government agency, the bank and the bondholders.

Principal maturities of long-term debt are as follows: 2012 - \$202,000, 2013 - \$192,000, 2014 - \$2,642,000 and 2015 - \$21,000.

The Company also has an unsecured \$1,000,000 line of credit on which there was no balance outstanding at December 31, 2011 or 2010.

Certain lenders require the Company to comply with debt covenants as described in the specific loan documents, including a debt service ratio. At December 31, 2011 and 2010, the Company was in compliance with its debt covenants.

5. Capital Lease – Related Party

On November 3, 2009, the Company entered into a capital lease with a related party of the Company for certain equipment to be used in the expansion of the Company's capabilities and product lines which was appropriately disclosed in the Company's Form 8-K filing on November 3, 2009. See Note 10, Related Party Transactions, of the accompanying consolidated financial statements for information on the related party transaction. Monthly payments of \$7,500 which include an imputed fixed interest rate of 2.00% commenced November 3, 2009 and will continue through the fourth quarter of 2016. At December 31, 2011 the present value of the minimal lease payment is approximately \$414,000 (after subtracting approximately \$21,000 of imputed interest).

Aggregate payments required under the capital lease subsequent to December 31, 2011 are as follows: 2012 - \$90,000, 2013 - \$90,000, 2014 - \$90,000, 2015 - \$90,000 and 2016 - \$75,000.

SERVOTRONICS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

6. Employee Benefit Plans

Employee Stock Ownership Plan (ESOP)

In 1985, the Company established an employee stock ownership plan ("ESOP") for the benefit of employees who meet certain minimum age and service requirements. Upon inception of the ESOP, the Company borrowed \$2,000,000 from a bank and lent the proceeds to the trust established under the ESOP to purchase shares of the Company's common stock. The Company's loan to the trust is at an interest rate approximating the prime rate and is repayable to the Company over a 40-year term ending in December 2024. During 1987 and 1988, the Company loaned an additional \$1,942,000 to the trust under terms similar to those under the Company's original loan.

ESOP shares are held by the plan trustees in a suspense account until allocated to participant accounts. Each year the Company makes contributions to the trust sufficient to enable the trust to repay the principal and interest due to the Company under the trust loans. As the loans are repaid, shares are released from the suspense account *pro rata* based on the portion of the aggregate loan payments that are paid during the year. During 2010, the ESOP plan was amended to allow dividends on unallocated shares be distributed to participants in cash, unless otherwise directed. ESOP shares released from the suspense account are allocated to participants on the basis of their relative compensation in the year of allocation and/or on the participant's account balance. For this purpose, "compensation" means taxable pay.

If Servotronics shares are not readily tradable on an established securities market at the times of an ESOP participant's termination of employment or retirement and if such ESOP participant requests that his/her ESOP distributed shares be repurchased by the Company, the Company is obligated to do so. The Company's shares currently trade on NYSE Amex, formerly known as the American Stock Exchange. There were no outstanding shares subject to the repurchase obligation at December 31, 2011.

Since inception of the ESOP, approximately 437,082 shares have been allocated, exclusive of shares distributed to ESOP participants. At December 31, 2011 and 2010 approximately 235,114 and 255,494 shares, respectively, purchased by the ESOP remain unallocated.

Related compensation expense associated with the Company's ESOP, which is equal to the principal reduction on the loans receivable from the trust, amounted to \$101,000 in 2011 and 2010. Included as a reduction to shareholders' equity is the ESOP trust commitment which represents the remaining indebtedness of the trust to the Company. Employees are entitled to vote allocated shares and the ESOP trustees are entitled to vote unallocated shares and those allocated shares not voted by the employees.

Other Postretirement Benefit Plans

The Company provides certain post retirement health and life insurance benefits for certain executives of the Company. Upon retirement and after attaining at least the age of 65, the Company will pay the annual cost of health insurance for the retired executives and dependents and will continue the Company provided life insurance offered at the time of retirement. The retiree's health insurance benefits ceases upon the death of the retired executive. The actuarially calculated future obligation of the benefits at December 31, 2011 and 2010 is \$316,395 and \$295,477, respectively, and is being amortized into expense at a rate of approximately \$38,000 per year. Estimated future annual expenses associated with the plan are immaterial. Included in accumulated other comprehensive loss for 2011 and 2010 is approximately \$67,000 and \$78,000, respectively, net of deferred taxes, associated with the unrecognized service cost of the plan.

SERVOTRONICS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

7. Income Tax Provision

There are no uncertain tax positions or unrecognized tax benefits for 2011 and 2010.

The income tax provision (benefit) for income taxes included in the consolidated statements of income consists of the following:

	<u>2011</u>	<u>2010</u>
	(\$000's omitted)	
Current:		
Federal	\$ 878	\$ 929
State	<u>(2)</u>	<u>14</u>
	<u>876</u>	<u>943</u>
Deferred:		
Federal	(167)	(4)
State	<u>(40)</u>	<u>(19)</u>
	<u>(207)</u>	<u>(23)</u>
	<u><u>\$ 669</u></u>	<u><u>\$ 920</u></u>

The reconciliation of the difference between the Company's effective tax rate based upon the total income tax provision (benefit) and the federal statutory income tax rate is as follows:

	<u>2011</u>	<u>2010</u>
Federal statutory rate	34.0%	34.0%
Deferred tax adjustment	(4.9%)	-
Business credits	(4.1%)	(1.8%)
ESOP dividend	(2.1%)	(1.2%)
Domestic production activities deduction	(2.1%)	(1.2%)
Other	0.3%	0.5%
State income taxes (less federal effect)	<u>(0.8%)</u>	<u>(0.2%)</u>
Effective tax rate	<u><u>20.3%</u></u>	<u><u>30.1%</u></u>

At December 31, 2011 and 2010, the deferred tax assets (liabilities) were comprised of the following:

	<u>2011</u>	<u>2010</u>
	(\$000's omitted)	
Inventories	\$ 380	\$ 300
Accrued employee compensation and benefit costs	373	347
Operating loss and credit carryforwards	300	59
Other	38	46
Minimum pension liability	<u>39</u>	<u>-</u>
Total deferred tax assets	1,130	752
Valuation allowance	<u>(270)</u>	<u>(57)</u>
Net deferred tax asset	860	695
Minimum pension liability	-	(57)
Property, plant and equipment	<u>(602)</u>	<u>(580)</u>
Total deferred tax liabilities	<u>(602)</u>	<u>(637)</u>
Net deferred tax asset	<u><u>\$ 258</u></u>	<u><u>\$ 58</u></u>

At December 31, 2011, the Company has New York State net operating loss carryforwards of approximately \$453,000 (approximately a \$2,000 net tax benefit) that begin to expire in 2019, which is fully reserved for at December 31, 2011. The Company has a State of Pennsylvania net operating loss carryforward of approximately \$1,797,000 (approximately a \$179,000 net tax benefit) that begins to expire in 2019, which is fully reserved for at December 31, 2011. The Company also has a State of Arkansas net operating loss carryforward of approximately \$1,489,000 (approximately a \$89,000 net tax benefit) that begins to expire in 2015, which is fully reserved for at December 31, 2011.

During the third quarter of 2009, the New York State Department of Taxation and Finance ("NYS") commenced an examination of the Company's New York State franchise tax returns for the years 2005 through 2007. In the third quarter of 2010, the examination was completed and resulted in no change to the Company's originally filed returns. Also, during the third

SERVOTRONICS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

quarter of 2010, the Internal Revenue Service commenced an examination of the Company's Federal income tax returns for the years 2008 and 2009. In the first quarter of 2011, the examination was completed and resulted in no material adjustments to the Company's originally filed returns. The 2008 through 2010 federal and state tax returns remain open under statute.

8. Common Shareholders' Equity

	Common stock						Accumulated	
	Number of shares issued	Amount	Capital in excess of par value	Retained earnings	ESOP	Treasury stock	Other Comprehensive Loss	Total Shareholders' Equity
				(\$000's omitted except share amounts)				
Balance December 31, 2009	<u>2,614,506</u>	<u>\$ 523</u>	<u>\$ 13,296</u>	<u>\$ 10,248</u>	<u>(\$1,468)</u>	<u>(\$ 2,724)</u>	<u>(\$ 61)</u>	<u>\$ 19,814</u>
Comprehensive income:								
Net income	-	-	-	\$ 2,128	-	-	-	\$ 2,128
Other comprehensive income, net of tax								
Retirement benefits adjustment	-	-	-	-	-	-	(17)	(17)
Total comprehensive income	-	-	-	-	-	-	-	2,111
Compensation expense	-	-	-	-	101	-	-	101
Cash dividend	-	-	-	(336)	-	-	-	(336)
Surrender of unexercised options, net of tax benefit	-	-	195	(573)	-	-	-	(378)
Balance December 31, 2010	<u>2,614,506</u>	<u>\$ 523</u>	<u>\$ 13,491</u>	<u>\$ 11,467</u>	<u>(\$1,367)</u>	<u>(\$ 2,724)</u>	<u>(\$ 78)</u>	<u>\$ 21,312</u>
Comprehensive income								
Net income	-	-	-	\$ 2,626	-	-	-	\$ 2,626
Other comprehensive loss, net of tax								
Retirement benefits adjustment	-	-	-	-	-	-	11	11
Total comprehensive income	-	-	-	-	-	-	-	2,637
Compensation expense	-	-	-	-	101	-	-	101
Cash dividend	-	-	-	(682)	-	-	-	(682)
Surrender of unexercised options, net of tax benefit	-	-	176	(517)	-	-	-	(341)
Exercise of stock options, net of tax benefit	-	-	107	(404)	-	514	-	217
Balance December 31, 2011	<u>2,614,506</u>	<u>\$ 523</u>	<u>\$ 13,774</u>	<u>\$ 12,490</u>	<u>(\$1,266)</u>	<u>(\$ 2,210)</u>	<u>(\$ 67)</u>	<u>\$ 23,244</u>

In January of 2006, the Company's Board of Directors authorized the purchase by the Company of up to 250,000 shares of its common stock in the open market or in privately negotiated transactions. On October 31, 2008, the Company announced that its Board of Directors authorized the purchase of an additional 200,000 shares of the Company's common stock under the Company's current purchase program. As of February 29, 2012, the Company has purchased 238,088 shares and there remain 211,912 shares available to purchase under this program.

Consistent with the Company's current policy to reduce the number of outstanding Company shares thereby increasing the reported earnings per share, certain option holders elected on July 12, 2011 to surrender 112,000 unexercised options to the Company in exchange for a cash payment equal to the difference between the exercise price and the average of the high and the low market price of the Company's common stock on the day of surrender less an administrative charge. Such transactions aggregated \$517,000. A tax benefit, to the Company of approximately \$176,000 associated with these transactions reduced taxes payable and was credited directly to capital in excess of par value. In the fourth quarter of 2011 certain option holders elected to exercise 78,000 options, of which 6,000 were bought back by the Company resulting in 72,000 net shares issued out of treasury stock. A tax benefit, to the Company, of approximately \$107,000 associated with these transactions reduced taxes payable and was credited directly to capital in excess of par value.

SERVOTRONICS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

On April 4, 2011, the Company announced that its Board of Directors declared a \$0.15 per share cash dividend. The dividend was paid on May 20, 2011 to shareholders of record on April 29, 2011 and was approximately \$336,000 in the aggregate. On November 8, 2011, the Company announced that its Board of Directors declared a \$0.15 per share cash dividend. The dividend was paid on December 16, 2011 to shareholders of record on November 28, 2011 and was approximately \$346,000 in the aggregate. These dividends do not represent that the Company will pay dividends on a regular or scheduled basis.

Other Comprehensive Loss

The only component of accumulated other comprehensive loss included in equity at December 31, 2011 is \$67,000 (\$78,000 – 2010) of unrecognized actuarial losses and net transition obligations for post retirement, health and life insurance benefits (see Note 6 Employee Benefit Plans). These amounts are shown net of income tax benefit of \$39,000 (\$46,000 – 2010).

Earnings Per Share

Basic earnings per share is computed by dividing net earnings by the weighted average number of shares outstanding during the period. Diluted earnings per share is computed by dividing net earnings by the weighted average number of shares outstanding during the period plus the number of shares of common stock that would be issued assuming all contingently issuable shares having a dilutive effect on earnings per share were outstanding for the period. Unallocated ESOP shares are not included in the calculation of weighted average common shares outstanding. Incremental shares from assumed conversions are calculated as the number of shares that would be issued, net of the number of shares that could be purchased in the marketplace with the cash received upon stock option exercise.

	Year Ended December 31,	
	<u>2011</u>	<u>2010</u>
	(\$000's omitted except per share data)	
Net income	<u>\$ 2,626</u>	<u>\$ 2,128</u>
Weighted average common shares outstanding (basic)	1,997	1,964
Incremental shares from assumed conversions of stock options	<u>112</u>	<u>145</u>
Weighted average common shares outstanding (diluted)	<u>2,109</u>	<u>2,109</u>
<u>Basic</u>		
Net income per share	<u>\$ 1.31</u>	<u>\$ 1.08</u>
<u>Diluted</u>		
Net income per share	<u>\$ 1.24</u>	<u>\$ 1.01</u>

Share Based Payments

Under the Servotronics, Inc. 2000 Employee Stock Option Plan authorized by the Board of Directors and the 2001 Long-Term Stock Incentive Plan authorized by the Board of Directors and the Shareholders, and other separate agreements authorized by the Board of Directors, the Company has granted options to certain Directors, Officers and employees. No options were granted and there was no corresponding stock based compensation in 2011 or 2010. At December 31, 2011, there were no stock options available for issuance as no awards are available to be granted after July 2, 2011 under the 2001 Long-Term Stock Incentive Plan. Options granted under this plan have durations of ten years and vesting periods ranging from immediate vesting to four years.

SERVOTRONICS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

A summary of the status of options granted under all employee plans is presented below:

	Options Outstanding	Weighted Average Exercise Price (\$)	Weighted Average Remaining Contractual Life	Aggregate Intrinsic Value (\$)
Outstanding as of December 31, 2009	407,700	<u>3.55</u>	<u>5.11</u>	
Granted in 2010	-	-		
Exercised in 2010	-	-		
Surrendered in 2010	<u>101,200</u>	<u>3.73</u>		
Outstanding as of December 31, 2010	306,500	<u>3.49</u>	<u>2.55</u>	
Granted in 2011	-	-		
Expired in 2011	8,000	<u>4.38</u>		
Exercised in 2011	78,000	<u>2.05</u>		
Surrendered in 2011	<u>112,000</u>	<u>4.33</u>		
Outstanding and exercisable as of December 31, 2011	<u>108,500</u>	<u>3.60</u>	<u>2.96</u>	<u>586,025</u>

The aggregate intrinsic value in the preceding table represents the total pretax intrinsic value based on the closing stock price of \$9.00 at December 31, 2011. The total intrinsic value of options exercised during the year ended December 31, 2011 amounted to \$497,340.

Shareholders' Rights Plan

During 2002, the Company's Board of Directors adopted a shareholders' rights plan (the "Rights Plan") and simultaneously declared a dividend distribution of one right for each outstanding share of the Company's common stock outstanding at August 28, 2002. The Rights Plan replaced a previous shareholders rights plan that was adopted in 1992 and expired on August 28, 2002. The Rights do not become exercisable until the earlier of (i) the date of the Company's public announcement that a person or affiliated group other than Dr. Nicholas D. Trbovich or the ESOP trust (an "Acquiring Person") has acquired, or obtained the right to acquire, beneficial ownership of 25% or more of the Company's common stock (excluding shares held by the ESOP trust) or (ii) ten business days following the commencement of a tender offer that would result in a person or affiliated group becoming an Acquiring Person.

The exercise price of a right has been established at \$32.00. Once exercisable, each right would entitle the holder to purchase one one-hundredth of a share of Series A Junior Participating Preferred Stock. In the event that any person becomes an Acquiring Person, each Right would entitle any holder other than the Acquiring Person to purchase common stock or other securities of the Company having a value equal to three times the exercise price. The Board of Directors has the discretion in such event to exchange two shares of common stock or two one-hundredths of a share of preferred stock for each Right held by any holder other than the Acquiring Person.

9. Commitments

The Company leases certain equipment and real property pursuant to operating lease arrangements. Total rental expense in 2011 and 2010 and future minimum payments under such leases are not material to the consolidated financial statements. The Company also leases certain personal property being accounted for under a capital lease. See also Note 3, Property, Plant and Equipment, Note 4, Long-Term Debt and Note 5, Capital Lease-Related Party, of the accompanying consolidated financial statements for information on the capital leases.

10. Related Party Transactions

During 2009 the Company formed a new wholly owned subsidiary that leased certain personal property from a related party through the execution of a capital lease. See Note 5, Capital Lease-Related Party, of the accompanying consolidated financial statements. The Company also entered into a real property lease agreement, with the same related party, which provides for annual rental of \$60,000. The Company has the option to purchase the building at the appraised value of \$506,000. In addition, in the event the Company is successful in obtaining certain tax and/or other incentives from the state the entity operates in, the Company will be required to purchase the building. The Company did not obtain the incentives and did not exercise its purchase option, but the lessor and the Company extended the lease including purchase option for another year.

SERVOTRONICS, INC. AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

Additionally, in the event that the Company purchases the building, there is an arrangement payable to the related party, providing a threshold in annual earnings is reached by the new subsidiary, which will result in a percentage payment which could be as low as zero dollars to a maximum total in the aggregate of \$600,000 which is non-recurring. These transactions are disclosed as related party transactions because the wife of an officer of Servotronics, Inc. is a sole shareholder of the company that is leasing/selling the assets. Purchases for inventory from the related party amounted to \$0 and \$56,000 during 2011 and 2010 respectively.

11. Litigation

There are no legal proceedings which are material to the Company currently pending by or against the Company other than ordinary routine litigation incidental to the business which is not expected to materially adversely affect the business or earnings of the Company.

12. Business Segments

The Company operates in two business segments, Advanced Technology Group (“ATG”) and Consumer Products Group (“CPG”). The Company’s reportable segments are strategic business units that offer different products and services. The segments are composed of separate corporations and are managed separately. Operations in ATG primarily involve the design, manufacture, and marketing of servo-control components (i.e., torque motors, control valves, actuators, etc.) for government, commercial and industrial applications. CPG’s operations involve the design, manufacture and marketing of a variety of cutlery products for use by consumers and government agencies. The Company derives its primary sales revenue from domestic customers, although a portion of finished products are for foreign end use.

As of December 31, 2011, the Company had identifiable assets of approximately \$30,423,000 (\$28,506,000 – December 31, 2010) of which approximately \$18,004,000 (\$15,342,000 – December 31, 2010) was for ATG and approximately \$12,419,000 (\$13,164,000 – December 31, 2010) was for CPG.

Information regarding the Company’s operations in these segments is summarized as follows (\$000’s omitted):

	<u>ATG</u> Years ended December 31,		<u>CPG</u> Years ended December 31,		<u>Consolidated</u> Years ended December 31,	
	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>	<u>2011</u>	<u>2010</u>
Revenues from unaffiliated customers	\$ 21,816	\$ 19,301	\$ 12,365	\$ 12,358	\$ 34,181	\$ 31,659
Cost of goods sold, exclusive of depreciation and amortization	(14,710)	(12,943)	(10,568)	(9,957)	(25,278)	(22,900)
Selling, general and administrative	(3,034)	(3,023)	(1,985)	(1,978)	(5,019)	(5,001)
Interest expense	(56)	(63)	(9)	(11)	(65)	(74)
Depreciation and amortization	(431)	(417)	(255)	(247)	(686)	(664)
Other income, net	<u>150</u>	<u>14</u>	<u>12</u>	<u>14</u>	<u>162</u>	<u>28</u>
Net income (loss) before income tax provision	<u>\$ 3,735</u>	<u>\$ 2,869</u>	<u>\$ (440)</u>	<u>\$ 179</u>	<u>\$ 3,295</u>	<u>\$ 3,048</u>
Capital expenditures	<u>\$ 271</u>	<u>\$ 276</u>	<u>\$ 337</u>	<u>\$ 216</u>	<u>\$ 608</u>	<u>\$ 492</u>

The Company engages in a significant amount of business with the United States Government through sales to its prime contractors and otherwise. Such contracts by the Advanced Technology Group accounted for revenues of approximately \$6,300,000 in 2011 and \$6,700,000 in 2010. Similar contracts by the Consumer Products Group accounted for revenues of approximately \$6,900,000 in 2011 and \$6,800,000 in 2010. Sales of advanced technology products to one customer, including various divisions and subsidiaries of a common parent company, amounted to approximately 25% of total revenues in 2011 and 22% in 2010. The Company also had sales to another ATG customer that amounted to approximately 10% of total revenues in 2011 and 9% in 2010. No other single customer represented more than 10% of the Company’s revenues in any of these years.

Directors



DR. NICHOLAS D. TRBOVICH
Founder, Chairman of the Board of Directors and Chief Executive Officer, Servotronics, Inc.



DONALD W. HEDGES, ESQ.
*Director, Servotronics, Inc.
Attorney*



DR. WILLIAM H. DUERIG
*Director, Servotronics, Inc.
Physicist and Senior Program Manager
Kearfoot Guidance & Navigation
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NICHOLAS D. TRBOVICH, JR.
Director, President and Chief Operating Officer, Servotronics, Inc.

Officers

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*Founder, Chairman of the Board of Directors and
Chief Executive Officer*

NICHOLAS D. TRBOVICH, JR.
Director, President and Chief Operating Officer

CARI L. JAROSLAWSKY, CPA
Chief Financial Officer and Treasurer

SALVATORE SAN FILIPPO
Senior Vice President

JAMES C. TAKACS
Vice President

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FORM 10-K REPORT
Servotronics' Annual Report to the Securities and Exchange Commission on Form 10-K (including related financial statements and schedules) for its fiscal year ended December 31, 2011 is available to all stockholders, without charge, upon written request. Written requests should be addressed to:

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