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AIR INDUSTRIES GROUP, INC.
CONDENSED CONSOLIDATED FINANCIAL STATEMENTS and FOOTNOTES
With INDEPENDENT ACCOUNTANTS' REVIEW REPORT
SEPTEMBER 30, 2012 and 2011

Air Industries Group, Inc.

Index to Condensed Consolidated Financial Statements and Footnotes

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INDEPENDENT ACCOUNTANTS' REVIEW REPORT

To the Board of Directors and Stockholders of
Air Industries Group, Inc.
Bay Shore, NY 11706

We have reviewed the accompanying condensed consolidated balance sheet of Air Industries Group, Inc. and Subsidiaries (the "Company") as of September 30, 2012, and the related condensed consolidated statements of income for the three and nine months ended September 30, 2012 and 2011 and the condensed consolidated statements of stockholders' equity and cash flows for the nine months ended September 30, 2012 and 2011. A review includes primarily applying analytical procedures to management's financial data and making inquiries of Company management. A review is substantially less in scope than an audit, the objective of which is the expression of an opinion regarding the condensed consolidated financial statements as a whole. Accordingly, we do not express such an opinion.

Management is responsible for the preparation and fair presentation of the condensed consolidated financial statements in accordance with accounting principles generally accepted in the United States and for designing, implementing, and maintaining internal control relevant to the preparation and fair presentation of the condensed consolidated financial statements.

Our responsibility is to conduct the review in accordance with the standards of the Public Company Accounting Oversight Board (United States) ("PCAOB"). Those standards require us to perform procedures to obtain limited assurance that there are no material modifications that should be made to the condensed consolidated financial statements. We believe that the results of our procedures provide a reasonable basis for our report.

Based on our review, we are not aware of any material modifications that should be made to the accompanying condensed consolidated financial statements in order for them to be in conformity with accounting principles generally accepted in the United States.

We have previously audited, in accordance with auditing standards of the PCAOB, the consolidated balance sheet of the Company as of December 31, 2011, and the related consolidated statements of operations, stockholders' equity, and cash flows for the year then ended (not presented herein); and in our report dated March 15, 2012, we expressed an unqualified opinion on those financial statements. In our opinion, the information set forth in the accompanying condensed consolidated balance sheet as of December 31, 2011, is fairly stated, in all material respects, in relation to the consolidated balance sheet from which it has been derived.

Rotenberg Meril Solomon Bertiger & Guttilla, P.C.

Rotenberg Meril Solomon Bertiger & Guttilla, P.C.
Saddle Brook, New Jersey
October 26, 2012

AIR INDUSTRIES GROUP, INC.
Condensed Consolidated Balance Sheets

		September 30, 2012 (Unaudited)		December 31, 2011
ASSETS				
Current Assets				
Cash and Cash Equivalents	$	1,120,000	$	577,000
Accounts Receivable, Net of Allowance for Doubtful Accounts of $609,000 and $950,000		8,348,000		6,042,000
Inventory		27,420,000		22,521,000
Prepaid Expenses and Other Current Assets		247,000		330,000
Deposits - Customers		13,000		2,000
Total Current Assets		37,148,000		29,472,000
Property and Equipment, net		4,920,000		3,971,000
Capitalized Engineering Costs - net of Accumulated Amortization of $3,330,000 and $2,990,000		838,000		969,000
Deferred Financing Costs, net, deposit and other assets		652,000		671,000
Intangible Assets, net		6,180,000		1,607,000
Goodwill		453,000		291,000
TOTAL ASSETS	$	50,191,000	$	36,981,000
LIABILITIES AND STOCKHOLDERS' EQUITY				
Current liabilities				
Notes Payable and Capitalized Lease Obligations - Current Portion	$	16,290,000	$	14,055,000
Accounts Payable and Accrued Expenses		7,392,000		7,432,000
Lease Impairment - Current		88,000		85,000
Deferred Gain on Sale - Current Portion		38,000		38,000
Income Taxes Payable		1,014,000		41,000
Total Current Liabilities		24,822,000		21,651,000
Long term liabilities				
Notes Payable and Capitalized Lease Obligation - Net of Current Portion		5,141,000		8,992,000
Lease Impairment - Net of Current Portion		147,000		175,000
Deferred Gain on Sale - Net of Current Portion		494,000		523,000
Deferred Rent		1,046,000		974,000
TOTAL LIABILITIES		31,650,000		32,315,000
Commitments and contingencies				
Stockholders' Equity				
Preferred Stock Par Value $.001-Authorized 8,003,716 shares Designated as Series "A" Convertible Preferred - $.001 par Value, 1,000 Shares Authorized 0 Shares issued and outstanding as of September 30, 2012 and December 31, 2011, respectively.		-		-
Designated as Series "B" Convertible Preferred -$.001 Par Value, 4,000,000 Shares Authorized, 0 shares issued and outstanding as of September 30, 2012 and December 31, 2011, respectively; Liquidation Value, $ 0		-		-
Common Stock - $.001 Par, 20,000,000 Shares Authorized, 5,711,093 and 3,579,114 Shares Issued and Outstanding as of September 30, 2012 and December 31, 2011, respectively		6,000		4,000
Additional Paid-In Capital		38,259,000		26,141,000
Accumulated Deficit		(19,724,000)		(21,479,000)
TOTAL STOCKHOLDERS' EQUITY		18,541,000		4,666,000
TOTAL LIABILITIES AND STOCKHOLDERS' EQUITY	$	50,191,000	$	36,981,000

See independent accountants' review report and notes to condensed consolidated financial statements

AIR INDUSTRIES GROUP, INC.
Condensed Consolidated Statements of Income
(Unaudited)

	Three Months Ended September 30, 2012	Three Months Ended September 30, 2011	Nine Months Ended September 30, 2012	Nine Months Ended September 30, 2011
Net Sales	$ 15,558,000	$ 13,255,000	$ 46,835,000	$ 38,978,000
Cost of Sales	11,724,000	10,420,000	36,295,000	31,112,000
Gross Profit	3,834,000	2,835,000	10,540,000	7,866,000
Operating Expenses	2,379,000	1,584,000	6,190,000	4,683,000
Income from operations	1,455,000	1,251,000	4,350,000	3,183,000
Interest and financing costs	(452,000)	(533,000)	(1,422,000)	(1,576,000)
Other (expense) income, net	(2,000)	15,000	(137,000)	12,000
Income before provision for income taxes	1,001,000	733,000	2,791,000	1,619,000
Provision for income taxes	387,000	31,000	1,036,000	57,000
Net income attributable to common stockholder	$ 614,000	$ 702,000	$ 1,755,000	$ 1,562,000
Income per share - basic	$ 0.11	$ 0.20	$ 0.40	$ 0.44
Income per share - diluted	$ 0.11	$ 0.20	$ 0.40	$ 0.44
Weighted average shares outstanding - basi	5,706,510	3,579,114	4,334,570	3,579,114
Weighted average shares outstanding - diluted	5,790,555	3,579,114	4,407,356	3,579,258

See independent accountants' review report and notes to condensed consolidated financial statements

AIR INDUSTRIES GROUP, INC.
Condensed Consolidated Statements of Stockholders' Equity
(Unaudited)

Nine Months ended September 30, 2012

	Series A Preferred Stock		Series B Preferred Stock		Common Stock		Additional Paid-in	Accumulated	Total Stockholders'
	Shares	Amount	Shares	Amount	Shares	Amount	Capital	Deficit	Equity
Balance, January 1, 2012	**-**	**$ -**	**-**	**$ -**	**3,579,114**	**$ 4,000**	**$ 26,141,000**	**$ (21,479,000)**	**$ 4,666,000**
Issuance of Shares For Acquisition	-	-	-	-	66,667	-	300,000	-	300,000
Issuance of Shares For Private Placement	-	-	-	-	1,185,851	1,000	6,527,000	-	6,528,000
Issuance of Shares For conversion of Junior Subordinated Notes	-	-	-	-	867,461	1,000	5,203,000	-	5,204,000
Issuance of Shares For Costs Associated with Private Placement	-	-	-	-	12,000	-	-	-	-
Stock compensation expense	-	-	-	-	-	-	88,000	-	88,000
Net income	-	-	-	-	-	-	-	1,755,000	1,755,000
Balance, September 30, 2012	**-**	**$ -**	**-**	**$ -**	**5,711,093**	**$ 6,000**	**$ 38,259,000**	**$ (19,724,000)**	**$ 18,541,000**

Nine Months ended September 30, 2011

	Series A Preferred Stock		Series B Preferred Stock		Common Stock		Additional Paid-in	Accumulated	Total Stockholders'
	Shares	Amount	Shares	Amount	Shares	Amount	Capital	Deficit	Equity
Balance, January 1, 2011	**-**	**$ -**	**-**	**$ -**	**3,579,114**	**$ 4,000**	**$ 26,009,000**	**$ (23,726,000)**	**$ 2,287,000**
Stock compensation expense	-	-	-	-	-	-	101,000	-	101,000
Net income	-	-	-	-	-	-	-	1,562,000	1,562,000
Balance, September 30, 2011	**-**	**$ -**	**-**	**$ -**	**3,579,114**	**$ 4,000**	**$ 26,110,000**	**$ (22,164,000)**	**$ 3,950,000**

See independent accountants' review report and notes to condensed consolidated financial statements

AIR INDUSTRIES GROUP, INC.

Condensed Consolidated Statements of Cash Flows For the Nine Months Ended September 30,

	2012	2011
	(Unaudited)	
CASH FLOWS FROM OPERATING ACTIVITIES		
Net Income	$ 1,755,000	$ 1,562,000
Adjustments to Reconcile Net Income to Net Cash provided by Operating Activities		
Depreciation of property and equipment	1,128,000	1,140,000
Amortization of intangible assets	402,000	126,000
Amortization of capitalized engineering costs	340,000	460,000
Bad debt expense	64,000	249,000
Non-cash compenstion expense	88,000	101,000
Amortization of deferred financing costs	42,000	122,000
Gain on sale of real estate	(28,000)	(28,000)
Adjustments to Lease Impairment	53,000	-
Changes in Assets and Liabilities		
(Increase) Decrease in Operating Assets:		
Accounts Receivable	(1,307,000)	(2,512,000)
Inventory	454,000	(1,468,000)
Prepaid Expenses and Other Current Assets	83,000	102,000
Deposits	(11,000)	50,000
Other Assets	(3,000)	(61,000)
Increase (Decrease) in Operating Liabilities		
Accounts payable and accrued expenses	(1,219,000)	1,464,000
Deferred Rent	71,000	143,000
Income Taxes payable	973,000	57,000
NET CASH PROVIDED BY OPERATING ACTIVITIES	2,885,000	1,507,000
CASH FLOWS FROM INVESTING ACTIVITIES		
Cash paid for acquisition	(11,600,000)	-
Capitalized engineering costs	(209,000)	(404,000)
Purchase of property and equipment	(471,000)	(422,000)
Deposit for new property and equipment	(81,000)	-
NET CASH USED IN INVESTING ACTIVITIES	(12,361,000)	(826,000)
CASH FLOWS FROM FINANCING ACTIVITIES		
Proceeds from Private Placement	7,115,000	-
Payment of Issuance costs for Private Placement	(587,000)	-
Notes payable - Sellers	(447,000)	(293,000)
Capital lease obligations	(426,000)	(296,000)
Notes payable-Jr. Subordinated Debt	(115,000)	-
Notes payable - Revolver	2,950,000	635,000
Notes payable - Term Loan PNC	1,627,000	(750,000)
Cash paid for deferred financing costs	(20,000)	(20,000)
Payments related to Lease Impairment	(78,000)	(74,000)
NET CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES	10,019,000	(798,000)
NET INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	543,000	(117,000)
CASH AND CASH EQUIVALENTS AT BEGINNING OF PERIOD	577,000	537,000
CASH AND CASH EQUIVALENTS AT END OF PERIOD	$ 1,120,000	$ 420,000
Supplemental cash flow information		
Cash paid during the period for interest	$ 1,225,000	$ 1,266,000
Supplemental cash flow information		
Cash paid during the period for income taxes	$ 64,000	$ -
Supplemental schedule of non-cash investing and financing activities		
Junior Subordinated Debt Converted to Common Stock	$ 5,204,000	$ -
Property and equipment acquired under capital lease	$ -	$ 827,000
Purchase of substantially all assets of Nassau Tool Works, Inc and assumption of liabilities in the acquisition as follows:		
Fair Value of Tangible Assets acquired	$ 7,941,000	
Intangible assets, subject to amortization	4,975,000	
Goodwill	162,000	
Liabilities assumed	(660,000)	
Due to Seller	(518,000)	
Common Stock	(300,000)	
Cash paid for acquisition	$ 11,600,000	

See independent accountants' review report and notes to condensed consolidated financial statements

Note 1. FORMATION AND BASIS OF PRESENTATION

Organization and Principal Business Activity

Air Industries Group, Inc. (the "Company" or "AIRI"), a Delaware corporation, was incorporated on January 13, 2006.

The accompanying condensed consolidated financial statements presented are those of AIRI, and its wholly-owned subsidiaries; Air Industries Machining Corporation ("AIM"), Welding Metallurgy, Inc. ("Welding") and Nassau Tool Works, Inc. ("NTW") which was acquired on June 20, 2012.

The Company through its AIM subsidiary is primarily engaged in manufacturing aircraft structural parts, and assemblies for prime defense contractors in the aerospace industry in the United States. The Company's customers consist mainly of publicly- traded companies in the aerospace industry. Welding is a specialty welding and products provider whose significant customers include the world's largest aircraft manufacturers, subcontractors, and original equipment manufacturers. NTW is a manufacturer of aerospace components, principally landing gear for F-16 and F-18 fighter aircraft.

Basis of Presentation

These condensed consolidated financial statements have been prepared by the Company in accordance with accounting principles generally accepted in the United States of America for interim financial reporting. Accordingly, they do not include all of the information and notes required by generally accepted accounting principles for complete financial statements. These unaudited interim condensed consolidated financial statements, which, in the opinion of management, reflect all adjustments (including normal recurring adjustments) necessary for a fair presentation, should be read in conjunction with the consolidated financial statements and notes thereto for the year ended December 31, 2011. Operating results for the three and nine months ended September 30, 2012 are not necessarily indicative of the results that may be expected for any future interim period or for the entire fiscal year. The results of NTW are included as of June 20, 2012.

Note 2. ACQUISITION

On March 15, 2012, the Company, through a newly created subsidiary, entered into a contract with NTW and its shareholders (the "NTW Sellers") to purchase substantially all of the assets, and to assume certain liabilities, for $12.0 million ($12,000,000), subject to positive or negative adjustments based on net working capital at closing. The acquisition was completed on June 20, 2012, and the assets, liabilities and the business of NTW is now operated through our new third subsidiary of the Company. The two former shareholders of NTW have joined the management team of the Company pursuant to management contracts.

The acquisition of NTW, Inc. was financed by a combination of debt and equity. The Company increased its borrowings from its existing revolving loan and term facilities which have been expanded (see Note 8), and raised equity from a Private Placement during June 2012 (see Note 9).

NTW founded in 1959 is a manufacturer of aerospace components, principally landing gear for F-16 and F-18 fighter aircraft. In recent years approximately 80% of NTW's net sales are direct to the US Government, specifically the US Navy and Air Force. NTW believes that some of its products are ultimately shipped abroad to support foreign military sales by the US Government. NTW supplies both individual components for repair and complete landing gear for refurbishment. The balance of NTW's net sales involve machining, turning, deep-hole drilling, and trepanning projects for other aerospace manufacturers.

The acquisition of NTW by AIRI results in a larger enterprise, with greater diversification of customers and aircraft platforms. The combined company has enhanced technical capabilities which we believe will lead to increased sales of landing gear product to our existing and prospective customers.

The acquisition of NTW was accounted for under ASC 805, "Business Combinations." The total purchase price was allocated to assets acquired and liabilities assumed based on a study of their relative fair values. The final valuation has been completed. The purchase price allocation is set forth below.

Fair Value of Tangible Assets acquired	$ 7,941,000
Intangible assets, subject to amortization	4,975,000
Goodwill	162,000
Liabilities assumed	(660,000)
Total	$12,418,000

The cost of the acquisition totaled $12,418,000. The purchase price of the acquisition is as follows:

1. At closing, the NTW Sellers were paid $11,400,000.
2. The issuance of 66,667 shares of common stock valued at $300,000.
3. $200,000 paid in July after the release of a lien on certain property and equipment purchased.
4. $518,000 to be paid for a working capital adjustment. See below.

It was determined that an increase in the NTW Sellers' working capital adjustment in the amount of $518,000 was necessary and is reflected in the purchase price allocation above. In addition, in July 2012, the Company paid $107,000 of liabilities of NTW not assumed under the acquisition agreement. Such amount will either be repaid by NTW or offset against amounts owed to the NTW Sellers. For financial statement purposes, such amount has been offset against the working capital adjustment. At September 30, 2012, the amount due and payable to the NTW Sellers totaled $411,000 and is included on the condensed consolidated balance sheet in accounts payable and accrued expenses.

Note 3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Accounts Receivable

Accounts receivable are reported at their outstanding unpaid principal balances net of allowances for uncollectible accounts. The Company provides for allowances for uncollectible receivables based on management's estimate of uncollectible amounts considering age, collection history, and any other factors considered appropriate. The Company writes off accounts receivable against the Allowance for Doubtful Accounts when a balance is determined to be uncollectible.

	September 30, 2012 (Unaudited)	December 31, 2011
Accounts Receivable Gross	$ 8,957,000	$ 6,992,000
Allowance for Doubtful Accounts	(609,000)	(950,000)
Accounts Receivable Net	$ 8,348,000	$ 6,042,000

Inventory Valuation

Inventory at September 30, 2012 and 2011 was computed based on a “gross profit” method.

The Company valued inventory at December 31, 2011 at the lower of cost on a first-in-first-out basis or market.

Long-Lived and Intangible Assets

Identifiable intangible assets are amortized using the straight-line method over the period of expected benefit.

Long-lived assets and intangible assets subject to amortization to be held and used are reviewed for impairment whenever events or changes in circumstances indicate that the related carrying amount may be impaired. The Company records an impairment loss if the undiscounted future cash flows are found to be less than the carrying amount of the asset. If an impairment loss has occurred, a charge is recorded to reduce the carrying amount of the asset to fair value. There has been no impairment as of September 30, 2012 and December 31, 2011.

Credit and Concentration Risks

There were three customers that represented 59.0% and 74.6% of total sales for the three months ended September 30, 2012 and 2011, respectively. This is set forth in the table below.

Customer	Percentage of Sales	
	2012	**2011**
	(Unaudited)	**(Unaudited)**
1	25.0	43.6
2	22.7	17.8
3	11.3	13.2

There were two customers that represented 59.2% and 65.1% of total sales for the nine months ended September 30, 2012 and 2011, respectively. This is set forth in the table below.

Customer	Percentage of Sales	
	2012	**2011**
	(Unaudited)	**(Unaudited)**
1	30.9	46.4
2	28.3	18.7

There were four customers that represented 63.3% of gross accounts receivable at September 30, 2012 and five customers that represented 82.2% of gross accounts receivable at December 31, 2011. This is set forth in the table below.

Customer	Percentage of Receivables	
	September 2012 (Unaudited)	**December 2011**
1	20.5	12.9
2	16.9	26.2
3	14.4	18.3
4	11.5	13.3
5	*	11.5

* Customer was less than 10% of receivables at September 30, 2012

During the year, the Company had occasionally maintained balances in its bank accounts that were in excess of the FDIC limit. The Company has not experienced any losses on these accounts.

Substantially all of the workforce at AIM is subject to a union contract with the United Service Workers Union TUJAT Local 355 (the "Union"). The contract expires on December 31, 2015.

AIM has several key sole-source suppliers of various parts that are important for one or more of our products. These suppliers are our only source for such parts and, therefore, in the event any of them were to go out of business or be unable to provide us parts for any reason, our business could be severely harmed.

Earnings per share

Basic earnings per share is computed by dividing the net income applicable to common stockholders by the weighted-average number of shares of common stock outstanding for the period. Potentially dilutive shares, using the treasury stock method, are included in the diluted per-share calculations for all periods when the effect of their inclusion is dilutive. The following securities have been excluded from the calculation as their effect would be anti-dilutive:

	September 30, 2012	**September 30, 2011**
Stock Options	15,548	291,428
Warrants	250	19,865

Stock-Based Compensation

The Company accounts for stock-based compensation in accordance with FASB ASC 718, "Compensation – Stock Compensation." Under the fair value recognition provision of the ASC, stock-based compensation cost is estimated at the grant date based on the fair value of the award. The Company estimates the fair value of stock options and warrants granted using the Black-Scholes-Merton option pricing model.

The Company recorded expenses of $45,000 and $41,000 for the three months ended September 30, 2012 and 2011, respectively and expenses of $88,000 and $101,000 for the nine months ended September 30, 2012 and 2011, respectively, in its consolidated statement of operations. These expenses are included as a component of general and administrative expense.

Goodwill

Goodwill represents the excess of the acquisition cost of businesses over the fair value of the identifiable net assets acquired. The goodwill amount of $453,000 is comprised of $291,000 that relates to the acquisition of Welding and $162,000 that relates to the acquisition of NTW. Goodwill is not amortized, but is tested at least annually for impairment, or if circumstances change that will more likely than not reduce the fair value of the reporting unit below its carrying amount.

The Company performs impairment testing for goodwill annually, or more frequently when indicators of impairment exist. The Company has determined that there has been no impairment of goodwill at September 30, 2012 and December 31, 2011.

Subsequent Events

Management has evaluated subsequent events through October 26, 2012, the date at which the financial statements were available to be issued.

Note 4. INVENTORY

The components of inventory at December 31, 2011 consisted of the following:

Raw Materials	$ 5,209,000
Work In Progress	12,094,000
Finished Goods	7,021,000
Inventory Reserve	(1,803,000)
Total Inventory	$ 22,521,000

Note 5. PROPERTY AND EQUIPMENT

The components of property and equipment consisted of the following:

	September 30, 2012 (Unaudited)	December 31, 2011	
Machinery and Equipment	$ 5,565,000	$ 3,700,000	5 - 8 years
Capital Lease Machinery and Equipment	3,877,000	3,877,000	5 - 8 years
Tools and Instruments	3,459,000	3,417,000	1.5 - 7 years
Automotive Equipment	55,000	55,000	5 years
Furniture and Fixtures	232,000	219,000	5 - 8 years
Leasehold Improvements	612,000	595,000	Term of Lease
Computers and Software	298,000	158,000	4-6 years
Total Property and Equipment	14,098,000	12,021,000	
Less: Accumulated Depreciation	(9,178,000)	(8,050,000)	
Property and Equipment, net	$ 4,920,000	$ 3,971,000	

Depreciation expense for the three months ended September 30, 2012 and 2011 were approximately $413,000 and $349,000, respectively. Depreciation expense for the nine months ended September 30, 2012 and 2011 were approximately $1,097,000 and $1,140,000, respectively.

Note 6. INTANGIBLE ASSETS

The components of the intangibles assets consisted of the following:

	September 30, 2012 (Unaudited)	December 31, 2011	
Customer Relationships	$ 5,815,000	$ 890,000	5 to 14 years
Trade Names	770,000	770,000	20 years
Technical Know-how	660,000	660,000	10 years
Non-Compete	50,000	-	5 years
Professional Certifications	15,000	15,000	.25 to 2 years
Total Intangible Assets	7,310,000	2,335,000	
Less: Accumulated Amortization	(1,130,000)	(728,000)	
Intangible Assets, net	$ 6,180,000	$ 1,607,000	

The expense for the amortization of intangibles for the three months ended September 30, 2012 and 2011 were approximately $318,000 and $42,000, respectively. The expense for the amortization of intangibles for the nine months ended September 30, 2012 and 2011 were approximately $402,000 and $126,000, respectively.

Note 7. SALE AND LEASEBACK TRANSACTION

On October 24, 2006, the Company consummated a Sale and Leaseback Arrangement, whereby the Company sold the buildings and real property comprising its corporate headquarters in Bay Shore, New York (the "Property") for a purchase price of $6,200,000. The Company accounted for the transaction under the provisions of FASB ASC 840-40, "Leases – Sale-Leaseback Transactions." The Company realized a gain on the sale of $1,051,000 of which $300,000 was recognized during the year ended December 31, 2006. The remaining $751,000 is being recognized ratably over the remaining term of the twenty year lease at approximately $38,000 per year. The gain is included in Other Income in the accompanying Condensed Consolidated Statement of Income. The unrecognized portion of the gain in the amount of $532,000 and $561,000 as of September 30, 2012 and December 31, 2011, respectively, is classified as Deferred Gain on Sale in the accompanying Condensed Consolidated Balance Sheet.

Note 8. NOTES PAYABLE AND CAPITAL LEASE OBLIGATIONS

Notes payable and capital lease obligations consist of the following:

	September 30, 2012 (Unaudited)	December 31, 2011
Revolving credit notes payable to PNC Bank N.A. ("PNC") and secured by substantially all assets	$ 12,507,000	$ 10,880,000
Term loan, PNC	4,950,000	2,000,000
Capital lease obligations	1,444,000	1,871,000
Notes payable to sellers of acquired business	1,530,000	1,976,000
Junior subordinated notes	1,000,000	6,320,000
Subtotal	21,431,000	23,047,000
Less: Current portion of notes and capital obligations	(16,290,000)	(14,055,000)
Notes payable and capital lease obligations, net of current portion	$ 5,141,000	$ 8,992,000

PNC Bank N.A. ("PNC")

The Company has a credit facility with PNC (the "Loan Facility"), secured by substantially all of its assets. Simultaneously with the acquisition of NTW, the Company entered in to an amendment to the Loan Facility and paid an amendment fee of $50,000. The Loan Facility now provides for maximum borrowings of $23,400,000 (increased from $19,000,000) consisting of the following:

(i) a $18,000,000 revolving loan (includes inventory sub-limit of $12,250,000)
(ii) a $5,400,000 term loan and
(iii) adds NTW as one of the borrowers

The Company borrowed an additional $2,840,000 under the revolving loan as part of the acquisition of NTW. The revolving loan bears interest at (a) the sum of PNC's base commercial lending rate as published from time to time ("PNC Rate") plus 2.00% or (b) the greater of the sum of the Eurodollar rate plus 3.5. The revolving loan had an interest rate of 5.50% per annum at both September 30, 2012 and December 31, 2011, and an outstanding balance of $12,507,000 and $10,880,000, respectively. The maturity date of the revolving loan was extended from November 15, 2013 to November 30, 2016.

Each day, the Company's cash collections are swept directly by the bank to reduce the revolving loans and we then borrow according to a borrowing base. As such, the Company generally has no cash on hand. Because the revolving loans contain a subjective acceleration clause which could permit PNC to require repayment prior to maturity, the loans are classified with the current portion of notes and capital lease obligations.

The Company borrowed an additional $3,900,000 under the term loan as part of the acquisition of NTW. The maturity date of the term loan was extended from December 2013 to June 2015 and bears interest, at the option of the Company equal to (a) the greater of (i) the sum of the PNC Rate plus 6.5% and (ii) 11.5%, with respect to Domestic Rate Loans or (b) the greater of (i) the sum of the Eurodollar Rate plus 8.5% and (ii) 10.5%, with respect to Eurodollar Rate Loans. Repayment under the term loan shall consist of 36 consecutive monthly principal installments, the first 35 of which will be in the amount of $150,000 commencing on the first business day of July 2012, with the 36th and final payment of any unpaid balance of principal and interest payable on the first business day of June 2015. Additionally, there is a mandatory prepayment equal to 50% of Excess Cash Flow (as defined) for each fiscal quarter commencing with the fiscal quarter ended September 30, 2012, payable upon the delivery of the financial statements to PNC for such fiscal period, but no later than 45 days after the end of the fiscal period. As of September 30, 2012, the amount due for the Excess Cash Flow was calculated as $752,000. At September 30, 2012 and December 31, 2011, the balance due under the term loan was $4,950,000 and $2,000,000, respectively.

To the extent that the Company disposes of collateral used to secure the Loan Facility, other than inventory, the Company must promptly repay the draws on the credit facility in the amount equal to the net proceeds of such sale.

The terms of the Loan Facility require that, among other things, the Company maintain certain financial ratios and levels of working capital. As of September 30, 2012 and December 31, 2011, the Company was in compliance with all terms of its credit facility with PNC.

The Loan Facility also is secured by all assets of the Company and the Company's receivables are payable directly into a lockbox controlled by PNC (subject to the terms of the Loan Facility). PNC may use some elements of subjective business judgment in determining whether a material adverse change has occurred in the Company's condition, results of operations, assets, business, properties or prospects allowing it to demand repayment of the Loan Facility.

As of September 30, 2012 the future minimum principal payments for the term loan are as follows

For the twelve months ending	Amount
September 30, 2013	$ 2,552,000
September 30, 2014	1,800,000
September 30, 2015	598,000
PNC Term Loan Payable	4,950,000
Less: Current portion	(2,552,000)
Long-term portion	$ 2,398,000

Interest expense related to these credit facilities amounted to approximately $314,000 and $219,000 for the three months ended September 30, 2012 and 2011, respectively, and $723,000 and $695,000 for the nine months ended September 30, 2012 and 2011, respectively

On July16, 2012, the Company entered into the 18th amendment to our Credit Facility with PNC. This amendment allowed for the repayment of $115,000 of our Junior Subordinated Notes (see discussion below).

Capital Leases Payable – Equipment

The Company is committed under several capital leases for manufacturing and computer equipment. All leases had bargain purchase options exercisable at the termination of each lease. Capital lease obligations totaled $1,444,000 and $1,871,000 as of September 30, 2012 and December 31, 2011, respectively, with various interest rates ranging from 7.7% to 9.5%.

As of September 30, 2012, the aggregate future minimum lease payments, including imputed interest, with remaining terms of greater than one year are as follows:

For the twelve months ending	Amount
September 30, 2013	$ 711,000
September 30, 2014	550,000
September 30, 2015	207,000
September 30, 2016	155,000
Total future minimum lease payments	1,623,000
Less: imputed interest	(179,000)
Less: current portion	(598,000)
Total Long Term Portion	$ 846,000

Notes Payable - Sellers

As of September 30, 2012 and December 31, 2011, the balance owed to the sellers of Welding is:

	September 30, 2012 (Unaudited)	December 31, 2011
Former Welding Stockholders	$ 1,530,000	$ 1,976,000
Less: Current Portion	(633,000)	(601,000)
Total long-term portion	$ 897,000	$ 1,375,000

In connection with the acquisition of Welding on August 24, 2007, the Company incurred a note payable ("Note") to the former stockholders of Welding. Our obligation under the Note is subordinate to our indebtedness to PNC.

The Note and payment terms were adjusted and/or amended several times. On October 1, 2010, the Company entered into letter agreement with the former stockholders of Welding. It was agreed that all interest that had been accrued and not yet paid under prior arrangements would be capitalized into the principal balance of the note, making the new balance of the note $2,397,967. Payments on the note began on October 1, 2010. It was further agreed that payments would be made according to the following schedule: equal monthly installments of $40,000 on the first business day of each month until December 31, 2011, followed by equal monthly installments of $60,000 on the first business day of each month commencing on January 1, 2012 and continuing until the entire principal amount of the obligation is paid in full, which is estimated to be in January 2015. Interest shall accrue at the rate of 7% per annum, and each payment will first apply to interest and then to principal. At September 30, 2012 and December 31, 2011, the balance owed under the note was $1,530,000 and $1,976,000 respectively.

As of September 30, 2012, the future minimum payments for the note payable to the former stockholders of Welding are as follows:

For the twelve months ending	Amount
September 30, 2013	$ 633,000
September 30, 2014	679,000
September 30, 2015	218,000
Former WMI Stockholders Notes Payable	1,530,000
Less: Current portion	(633,000)
Long-term portion	$ 897,000

Interest expense related to notes payable to the former stockholders was $29,000 and $37,000 for the three months ended September 31, 2012 and 2011, respectively and $93,000 and $114,000 for the nine months ended September 30, 2012 and 2011 respectively.

Junior Subordinated Notes

In 2008, the Company sold in a series of private placements to accredited investors $5,545,000 of principal in junior subordinated notes, together with 983,324 shares of its common stock and 207,600 shares of Series B Convertible Preferred Stock (“Series B Preferred”), for a total purchase price of $5,545,000. The notes bear interest at the rate of 1% per month (or 12% per annum).

In the first quarter ended March 31, 2009, the Company sold in a private placement to accredited investors, an additional $445,000 of principal in notes together with 35,600 shares of our Series B Preferred for a total purchase price of $445,000.

In connection with the offering of the Company's junior subordinated notes and Series B Preferred which commenced in September 2008, the Company issued to Taglich Brothers, Inc. ("Taglich"), as placement agent, a junior subordinated note in the principal amount of $510,000 and 39,640 shares of Series B Preferred. The terms of the note issued to Taglich are identical to the notes. In addition, the Company issued a warrant to purchase 137,138 shares of its Series B Preferred to Taglich. In connection with the amounts raised in 2009, the Company issued Taglich 3,560 shares of Preferred Series B and will issue to Taglich a note on the same terms as the Junior Subordinated Notes referred to above for commission of $44,500.

In conjunction with the Private Placement of our common stock to raise money for the acquisition of NTW, we solicited the holders of our Junior Subordinated Notes to convert their notes to Common Stock at a price of $6.00 per share. On June 29, 2012, we issued 867,461 shares of our common stock in exchange for approximately $5,204,000 of our Junior Subordinated Notes. On July 26, 2012, we repaid $115,000 of our Junior Subordinated Notes along with the accrued interest thereon of approximately $1,000.

The due date of the remaining notes were extended from November 18, 2013 to mature on November 30, 2016 and are subordinated to the Company's obligations to PNC.

The balance owed at September 30, 2012 and December 31, 2011 amounted to $1,000,000 and $6,320,000, respectively.

Interest expense amounted to $30,000 and $196,000 for the three months ended September 30, 2012 and 2011, respectively and $409,000 and $583,000 for the nine months ended September 30, 2012 and 2011 respectively.

Note 9. STOCKHOLDERS' EQUITY

Common Stock Issuances

During June and July of 2012, the Company issued 1,185,851 shares of its Common Stock in a Private Placement to Accredited Investors. The Company received $6,528,000 net of commissions and expenses.

Our agent, Taglich, received commissions in the amount of approximately $569,000, along with 12,000 shares of common stock, and Warrants to purchase approximately 119,000 shares of Common Stock at $6.30. The Company also paid approximately $18,000 of legal fees on behalf of Taglich.

The proceeds from the sale of the Common Stock were used to finance the acquisition of NTW.

Note 10. COMMITMENTS AND CONTINGENCIES

Lease Impairment

A former subsidiary was located in our Plant Avenue facility and following the discontinuance of its operations, a portion of the facility was vacant. The Company recorded a charge for $579,000 at December 31, 2009 representing the estimated discounted future cost of part of the Plant Avenue facility.

As of September 30, 2012, the estimated discounted future cost will be charged to expense as follows:

For the twelve months ending	Amount
September 30, 2013	$ 88,000
September 30, 2014	75,000
September 30, 2015	60,000
September 30, 2016	12,000
Total future minimum lease payments	235,000
Less: current portion	(88,000)
Total Long-Term Portion	$ 147,000

Litigation

Sigma Metals, Inc ("Sigma"): Several former vendors to Sigma had commenced legal action against Sigma seeking to recover amounts owed to them. All of these have been settled except for one that is still deciding to commence litigation seeking the recovery of approximately $71,000. Settlement discussions have commenced with this vendor but there is not yet a definitive resolution. Such amount is included in accounts payable and accrued expenses at September 30, 2012 and December 31, 2011.

Note 11. INCOME TAXES

The provision for income taxes at September 30, 2012 and 2011 is as follows:

	2012 (Unaudited)	2011 (Unaudited)
Current		
Federal	$ 778,000	$ -
Federal AMT	-	57,000
State	258,000	-
Total Expense	1,036,000	57,000
Deferred		
Federal	-	-
State	-	-
Total Deferred Taxes	-	-
Net Expense for Income Taxes	$ 1,036,000	$ 57,000

The components of net deferred tax assets as of September 30, 2012 and December 31, 2011 are set forth below:

	September 30, 2012 (Unaudited)	December 31, 2011
Deferred tax assets:		
Net operating loss carry forwards	$ -	$ 289,000
Capital loss carry forwards	1,088,000	1,088,000
Bad debts	244,000	380,000
Stock based compensation - options and restricted stock	501,000	466,000
Capitalized engineering costs	416,000	356,000
Account payable, accrued expenses and reserves	9,000	9,000
Deferred rent	418,000	390,000
Amortization - NTW Transaction	74,000	-
Inventory - 263A adjustment	629,000	-
Lease Impairment	94,000	-
Deferred gain on sale of real estate	213,000	224,000
Section 1231 loss carryover	86,000	86,000
Total deferred tax assets before valuation allowance	3,772,000	3,288,000
Valuation allowance	(2,568,000)	(1,217,000)
Total deferred tax assets after valuation allowance	1,204,000	2,071,000
Deferred tax liabilities:		
Property and equipment	(612,000)	(801,000)
Amortization - Welding Transaction	(592,000)	(643,000)
Inventory - 263A adjustment	-	(627,000)
Total Deferred Tax Liability	(1,204,000)	(2,071,000)
Net deferred tax asset	$ -	$ -

Realization of deferred tax assets is dependent on future earnings. Due to the uncertainty of realization of the net deferred tax assets, the Company has provided a 100% valuation allowance.

Note 12. SEGMENT REPORTING

In accordance with FASB ASC 280, “Segment Reporting”, the Company discloses financial and descriptive information about its reportable operating segments. Operating segments are components of an enterprise about which separate financial information is available and regularly evaluated by the chief operating decision maker in deciding how to allocate resources and in assessing performance.

Financial information about the Company's operating segments for the three and nine months ended September 30, 2012 and 2011 are as follows:

Three Months Ended September 30,	2012 (Unaudited)	2011 (Unaudited)
Air Industries Machining		
Net Sales	$ 9,587,000	$ 10,325,000
Gross Profit	1,788,000	2,015,000
Pre Tax Income	996,000	889,000
Assets	23,946,000	28,677,000
Nassau Tool Works		
Net Sales	3,080,000	-
Gross Profit	1,196,000	-
Pre Tax Income	499,000	-
Assets	13,863,000	-
Welding Metallurgy		
Net Sales	2,891,000	2,930,000
Gross Profit	850,000	820,000
Pre Tax Income	140,000	430,000
Assets	8,986,000	8,491,000
Corporate		
Net Sales	-	-
Gross Profit	-	-
Pre Tax Loss	(634,000)	(586,000)
Assets	15,478,000	8,840,000
Consolidated		
Net Sales	15,558,000	13,255,000
Gross Profit	3,834,000	2,835,000
Pre Tax Income	1,001,000	733,000
Provision for Taxes	387,000	31,000
Net Income	614,000	702,000
Elimination of Assets	(12,082,000)	(8,326,000)
Assets	50,191,000	37,682,000

Nine Months Ended September 30,	2012 (Unaudited)	2011 (Unaudited)
Air Industries Machining		
Net Sales	$ 33,314,000	$ 31,063,000
Gross Profit	6,227,000	5,649,000
Pre Tax Income	3,291,000	2,588,000
Assets	23,946,000	28,677,000
Nassau Tool Works		
Net Sales	3,592,000	-
Gross Profit	1,394,000	-
Pre Tax Income	655,000	-
Assets	13,863,000	-
Welding Metallurgy		
Net Sales	9,929,000	7,915,000
Gross Profit	2,919,000	2,217,000
Pre Tax Income	994,000	1,022,000
Assets	8,986,000	8,491,000
Corporate		
Net Sales	-	-
Gross Profit	-	-
Pre Tax Loss	(2,149,000)	(1,991,000)
Assets	15,478,000	8,840,000
Consolidated		
Net Sales	46,835,000	38,978,000
Gross Profit	10,540,000	7,866,000
Pre Tax Income	2,791,000	1,619,000
Provision for Taxes	1,036,000	57,000
Net Income	1,755,000	1,562,000
Elimination of Assets	(12,082,000)	(8,326,000)
Assets	50,191,000	37,682,000