

AVIALL INC
Form 10-Q
April 28, 2004

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

FORM 10-Q

(Mark One)

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

For the quarterly period ended **March 31, 2004**

OR

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

For the transition period from _____ to _____

Commission file number **1-12380**

AVIALL, INC.

(Exact name of registrant as specified in its charter)

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Delaware
(State or other jurisdiction of
incorporation or organization)

65-0433083
(I.R.S. Employer
Identification No.)

2750 Regent Boulevard

DFW Airport, Texas
(Address of principal executive offices)

75261-9048
(Zip Code)

(972) 586-1000

(Registrant's telephone number, including area code)

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

Indicate by check mark whether the registrant is an accelerated filer (as defined in Rule 12b-2 of the Exchange Act). Yes No

The number of shares of common stock, par value \$0.01 per share, outstanding at April 26, 2004 was 32,204,257.

PART I FINANCIAL INFORMATION
Item 1: Financial Statements**AVIALL, INC.****CONSOLIDATED STATEMENTS OF OPERATIONS****(Dollars in thousands, except share data)****(Unaudited)**

| | Three Months Ended | |
|--|---------------------------|-------------|
| | March 31, | |
| | 2004 | 2003 |
| Net sales | \$ 283,532 | 251,490 |
| Cost of sales | 236,434 | 209,150 |
| Gross profit | 47,098 | 42,340 |
| Selling and administrative expense | 27,599 | 25,243 |
| Operating income | 19,499 | 17,097 |
| Interest expense | 4,345 | 5,863 |
| Earnings before income taxes | 15,154 | 11,234 |
| Provision for income taxes | 5,177 | 4,064 |
| Net earnings | 9,977 | 7,170 |
| Less preferred stock dividends | | (1,109) |
| Net earnings applicable to common shares | \$ 9,977 | 6,061 |
| Basic net earnings per share | \$ 0.31 | 0.22 |
| Weighted average common shares | 31,744,620 | 19,385,713 |
| Diluted net earnings per share | \$ 0.30 | 0.22 |
| Weighted average common and potentially dilutive common shares | 33,242,755 | 29,113,963 |

See accompanying notes to consolidated financial statements.

AVIALL, INC.

CONSOLIDATED BALANCE SHEETS

(Dollars in thousands, except share data)

| | March 31, 2004 <u>(Unaudited)</u> | December 31, 2003 <u></u> |
|---|---|---------------------------------|
| Assets | | |
| Current assets: | | |
| Cash and cash equivalents | \$ 11,429 | 23,424 |
| Receivables | 149,607 | 139,279 |
| Inventories | 321,442 | 327,860 |
| Prepaid expenses and other current assets | 3,759 | 2,501 |
| Deferred income taxes | 19,075 | 19,075 |
| | <u>505,312</u> | <u>512,139</u> |
| Total current assets | | |
| Property and equipment | 31,370 | 32,029 |
| Goodwill | 46,843 | 46,843 |
| Intangible assets | 50,944 | 51,908 |
| Deferred income taxes | 31,423 | 35,749 |
| Other assets | 12,171 | 12,524 |
| | <u>678,063</u> | <u>691,192</u> |
| Total assets | | |
| Liabilities and Shareholders' Equity | | |
| Current liabilities: | | |
| Current portion of long-term debt | \$ 2,920 | 3,293 |
| Revolving line of credit | 473 | 509 |
| Accounts payable | 112,705 | 138,437 |
| Accrued expenses | 42,460 | 39,567 |
| | <u>158,558</u> | <u>181,806</u> |
| Total current liabilities | | |
| Long-term debt | 204,299 | 203,411 |
| Other liabilities | 4,143 | 5,891 |
| Commitments and contingencies | | |
| Shareholders' equity: | | |
| Common stock (\$0.01 par value per share, 80,000,000 shares authorized; 34,169,353 shares and 33,950,107 shares issued at March 31, 2004 and December 31, 2003, respectively) | 342 | 339 |
| Additional paid-in-capital | 440,247 | 439,080 |
| Accumulated deficit | (95,322) | (105,299) |
| Treasury stock, at cost (2,035,124 shares and 2,012,743 shares at March 31, 2004 and December 31, 2003, respectively) | (28,218) | (27,867) |
| Unearned compensation - restricted stock | (1,336) | (1,519) |
| Accumulated other comprehensive loss | (4,650) | (4,650) |

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| | | |
|--|------------|---------|
| Total shareholders' equity | 311,063 | 300,084 |
| Total liabilities and shareholders' equity | \$ 678,063 | 691,192 |

See accompanying notes to consolidated financial statements.

AVIALL, INC.

CONSOLIDATED STATEMENTS OF CASH FLOWS

(Dollars in thousands)

(Unaudited)

| | Three Months Ended | |
|--|--------------------|----------|
| | March 31, | |
| | 2004 | 2003 |
| Operating activities: | | |
| Net earnings | \$ 9,977 | 7,170 |
| Depreciation and amortization | 4,293 | 4,624 |
| Deferred income taxes | 4,328 | 4,261 |
| Paid-in-kind interest | | 202 |
| Compensation expense on restricted stock awards | 183 | 158 |
| Changes in: | | |
| Receivables | (10,328) | (6,455) |
| Inventories | 6,418 | 20,958 |
| Accounts payable | 12,258 | 6,927 |
| Accrued expenses | 2,893 | (5,897) |
| Other, net | (1,625) | (1,530) |
| Net cash provided by operating activities | 28,397 | 30,418 |
| Investing activities: | | |
| Capital expenditures | (1,432) | (1,365) |
| Purchase of distribution rights | (800) | |
| Sales of property, plant and equipment | 6 | |
| Net cash used for investing activities | (2,226) | (1,365) |
| Financing activities: | | |
| Cash overdrafts | (37,990) | (27,521) |
| Issuance of common stock | 1,170 | |
| Debt repaid | (860) | (648) |
| Purchase of treasury stock | (351) | |
| Debt issuance cost paid | (99) | |
| Net change in revolving credit facility | (36) | (1,578) |
| Other | | (1) |
| Net cash used for financing activities | (38,166) | (29,748) |
| Change in cash and cash equivalents | (11,995) | (695) |
| Cash and cash equivalents, beginning of period | 23,424 | 4,997 |
| Cash and cash equivalents, end of period | \$ 11,429 | 4,302 |
| Cash paid (received) for interest and income taxes: | | |
| Interest | \$ 431 | 4,831 |

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| | | |
|--|----------|-------|
| Income taxes | \$ (266) | 250 |
| Noncash investing and financing activities: | | |
| Dividends on redeemable preferred stock | \$ | 1,108 |

See accompanying notes to consolidated financial statements.

AVIALL, INC.

NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

NOTE 1 BASIS OF PRESENTATION

The accompanying unaudited financial statements have been prepared in accordance with generally accepted accounting principles for interim financial information and with the instructions to Form 10-Q and Article 10 of Regulation S-X. Accordingly, these financial statements do not include all of the information and footnotes required by generally accepted accounting principles for complete financial statements. In the opinion of management, all adjustments (consisting only of normal recurring adjustments) considered necessary for a fair presentation have been included. Operating results for the three month period ended March 31, 2004 are not necessarily indicative of the results that may be expected for the year ending December 31, 2004. For further information, refer to the consolidated financial statements and footnotes thereto included in our Annual Report on Form 10-K for the year ended December 31, 2003.

NOTE 2 STOCK-BASED COMPENSATION

We account for our stock-based compensation plans in accordance with the recognition and measurement principles of Accounting Principles Board Opinion No. 25, or APB 25, Accounting for Stock Issued to Employees, and related interpretations. All options granted under our plans have an exercise price equal to the market value of the underlying common stock on the date of grant. Therefore, no compensation cost related to these plans is included in net earnings. We also make the appropriate disclosures as required by Statement of Financial Accounting Standards No. 123, or SFAS 123, Accounting for Stock-Based Compensation, and Statement of Financial Accounting Standards No. 148, or SFAS 148, Accounting for Stock-Based Compensation Transition and Disclosure an Amendment of FAS 123. Awards of restricted stock are valued at the market price of our common stock on the date of grant and recorded as unearned compensation within shareholders' equity. The unearned compensation is amortized to compensation expense over the vesting period of the restricted stock.

The following table illustrates the effect on net earnings and earnings per share, or EPS, if we had applied the fair-value recognition provisions of SFAS 123 to stock-based employee compensation (in thousands, except share data):

| | Three Months Ended | |
|---|--------------------|-------|
| | March 31, | |
| | 2004 | 2003 |
| | _____ | _____ |
| Net earnings, as reported | \$ 9,977 | 7,170 |
| Deduct: Total stock-based employee compensation expense determined under fair-value-based method for all awards, net of related tax effects | (451) | (310) |
| Pro forma net earnings | \$ 9,526 | 6,860 |
| Earnings per share: | | |
| Basic as reported | \$ 0.31 | 0.22 |
| Basic pro forma | \$ 0.30 | 0.21 |
| Diluted as reported | \$ 0.30 | 0.22 |

Diluted pro forma

\$ 0.29

0.21

NOTE 3 NEW ACCOUNTING PRONOUNCEMENTS

In December 2003, the Financial Accounting Standards Board, or FASB, issued a revised Interpretation No. 46, or FIN 46R, Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51, replacing the original interpretation issued in January 2003. FIN 46R requires certain entities to be consolidated by enterprises that lack majority voting interest when equity investors of those entities have insignificant capital at risk or they lack voting rights, the obligation to absorb expected losses, or the right to receive expected returns. Entities identified with these characteristics are called variable interest entities and the interests that enterprises have in these entities are called variable interests. These interests can derive from certain guarantees, leases, loans or other arrangements that result in risks and rewards that are disproportionate to the voting interests in the entities. We adopted FIN 46R as of March 31, 2004. Because we have no variable interest entities, the adoption of this statement did not have an effect on our consolidated financial position and results of operations.

In December 2003, the FASB issued a revised Statement of Financial Accounting Standards No. 132, or SFAS 132R, Employers Disclosures about Pensions and Other Postretirement Benefits, an Amendment of FASB Statements No. 87, 88, and 106, and a Revision of FASB Statement No. 132. This statement revises employers disclosures about pension plans and other postretirement benefit plans. It does not change the measurement or recognition of those plans required by FASB Statements No. 87, Employers Accounting for Pensions, No. 88, Employers Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits and No. 106, Employers Accounting for Postretirement Benefits Other Than Pensions. The new fiscal disclosure requirements have been included in Note 13 Pension Plans and Postretirement Benefits to the consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2003. The new interim disclosure requirements have been included in Note 6 Pension Plans and Postretirement Benefits.

NOTE 4 SEGMENT INFORMATION

The following tables present information by operating segment (in thousands):

| | Three Months Ended March 31, | |
|-------------------------------------|---|----------------|
| | 2004 | 2003 |
| Net Sales | | |
| Aviall Services | \$ 276,421 | 244,477 |
| ILS | 7,111 | 7,013 |
| Total net sales | \$ 283,532 | 251,490 |
| Profit | | |
| Aviall Services | \$ 20,266 | 17,108 |
| ILS | 2,548 | 2,368 |
| Reportable segment profit | 22,814 | 19,476 |
| Corporate | (3,315) | (2,379) |
| Interest expense | (4,345) | (5,863) |
| Earnings before income taxes | \$ 15,154 | 11,234 |

NOTE 5 EARNINGS PER SHARE

A reconciliation of the numerator and denominator of the basic and diluted net EPS calculations for net earnings follows:

| | Three Months Ended | |
|--|---------------------------|-------------|
| | March 31, | |
| | 2004 | 2003 |
| Numerator (In Thousands) | | |
| Net earnings | \$ 9,977 | 7,170 |
| Preferred stock dividends | | (1,109) |
| Net earnings available for distribution | 9,977 | 6,061 |
| Undistributed earnings allocated to participating preferred stockholders | | (1,847) |
| Net earnings for purposes of computing basic net EPS | 9,977 | 4,214 |
| Preferred stock dividends | | 1,109 |
| Undistributed earnings allocated to participating preferred stockholders | | 1,847 |
| Net earnings for purposes of computing diluted net EPS | \$ 9,977 | 7,170 |
| Denominator | | |
| Weighted average common shares outstanding for purposes of computing basic net EPS | 31,744,620 | 19,385,713 |
| Effect of dilutive securities: | | |
| Stock options | 931,338 | 90,752 |
| Restricted stock rights | 304,467 | 315,935 |
| Warrants | 262,330 | 821,391 |
| Convertible redeemable preferred stock | | 8,500,172 |
| Weighted average common shares outstanding for purposes of computing diluted net EPS | 33,242,755 | 29,113,963 |

For the three months ended March 31, 2004, basic EPS is computed by dividing net earnings by the weighted average number of common shares outstanding during the period and diluted EPS is computed by dividing net earnings by the weighted average number of common and dilutive potential common shares outstanding during the period.

For the three months ended March 31, 2003, basic EPS is computed by allocating net earnings available for distribution to the common and participating preferred shareholders using the two-class method prescribed by Statement of Financial Accounting Standards No. 128, or SFAS 128, Earnings per Share. Net earnings are reduced by dividends to preferred stockholders to arrive at net earnings available for distribution. Net earnings available for distribution are then allocated between the common and participating preferred stockholders based on the weighted average common and preferred shares outstanding, on an as-converted basis. For the three months ended March 31, 2003, diluted EPS is computed using the if-converted method by dividing net earnings by the weighted average number of common and dilutive potential common shares outstanding during the period.

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Diluted EPS was not dilutive, or lower than basic, for the three month period ended March 31, 2003 and is therefore presented equal to basic EPS.

NOTE 6 PENSION PLANS AND POSTRETIREMENT BENEFITS

The following table sets forth the components of net pension expense for all our plans (in thousands):

| | Three Months | |
|------------------------------------|---------------------|-------------------|
| | Ended | |
| | March 31, | |
| | 2004 | 2003 |
| | <u> </u> | <u> </u> |
| Service cost | \$ 615 | 430 |
| Interest cost | 969 | 886 |
| Expected return on plan assets | (963) | (910) |
| Transition obligation amortization | 35 | |
| Prior service cost amortization | 1 | 1 |
| Net loss recognition | 117 | 16 |
| | <u> </u> | <u> </u> |
| Net pension expense | <u>\$ 774</u> | <u>423</u> |

The following table sets forth the components of net postretirement benefit income for all our plans (in thousands):

| | Three Months | |
|-----------------------------------|---------------------|-------------------|
| | Ended | |
| | March 31, | |
| | 2004 | 2003 |
| | <u> </u> | <u> </u> |
| Service cost | \$ | |
| Interest cost | 22 | 24 |
| Net amortization and deferral | (34) | (32) |
| | <u> </u> | <u> </u> |
| Net postretirement benefit income | <u>\$ (12)</u> | <u>(8)</u> |

NOTE 7 GUARANTOR AND NONGUARANTOR FINANCIAL STATEMENTS

Our senior unsecured notes, or the Senior Notes, are fully and unconditionally and jointly and severally guaranteed on a senior unsecured basis by each direct and indirect domestic subsidiary of Aviall, Inc., each a guarantor subsidiary. Each guarantor subsidiary is directly or indirectly 100% owned by Aviall, Inc. The Senior Notes are not guaranteed by any direct or indirect foreign subsidiary of Aviall, Inc., each a nonguarantor subsidiary.

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The consolidating financial information presents the consolidating balance sheets as of March 31, 2004 and December 31, 2003, the related statements of operations for the three month periods ended March 31, 2004 and 2003 and the statements of cash flows for the three month periods ended March 31, 2004 and 2003 with separate columns for:

- a) Aviall, Inc., the parent;
- b) the guarantor subsidiaries on a combined basis;
- c) the nonguarantor subsidiaries on a combined basis; and
- d) total consolidated amounts.

The information includes elimination entries necessary to consolidate Aviall, Inc., the parent, with the guarantor and nonguarantor subsidiaries.

Investments in subsidiaries are accounted for by the parent using the equity method of accounting. The guarantor and nonguarantor subsidiaries are presented on a combined basis. The principal elimination entries eliminate investments in subsidiaries and intercompany balances and transactions. Separate financial statements for the guarantor and nonguarantor subsidiaries are not presented because management believes such financial statements would not be meaningful to investors.

Pursuant to the terms of our senior secured credit facility, or the Credit Facility, no subsidiary of Aviall other than Aviall Services may pay cash dividends to Aviall. Aviall Services may only pay cash dividends to Aviall for the purpose of funding (i) ordinary operating expenses and scheduled debt service and (ii) payments by Aviall of taxes in respect of Aviall and its subsidiaries, up to the amount that would be payable by Aviall Services, on a consolidated basis, if it were the taxpayer. Additionally, the Credit Facility restricts intercompany loans made to Aviall from its direct and indirect subsidiaries, with the exception of intercompany loans made by Aviall Services to fund required payments under the Senior Notes. The net assets of consolidating subsidiaries subject to these restrictions were \$711.0 million and \$707.4 million at March 31, 2004 and December 31, 2003, respectively.

CONSOLIDATED STATEMENT OF OPERATIONS

| | Three Months Ended March 31, 2004 | | | | |
|---|-----------------------------------|--------------|--------------|--------------|--------------|
| | | Guarantor | Nonguarantor | | Consolidated |
| | Parent | Subsidiaries | Subsidiaries | Eliminations | Total |
| (In Thousands) | | | | | |
| Net sales | \$ | 268,185 | 31,554 | (16,207) | 283,532 |
| Cost of sales | | 227,260 | 25,381 | (16,207) | 236,434 |
| Gross profit | | 40,925 | 6,173 | | 47,098 |
| Selling and administrative expense | | 24,292 | 3,307 | | 27,599 |
| Operating income | | 16,633 | 2,866 | | 19,499 |
| Interest expense (income) | (4,243) | 8,497 | 91 | | 4,345 |
| Equity in (earnings) loss of subsidiaries | (7,270) | (2,037) | | 9,307 | |
| Earnings (loss) before income taxes | 11,513 | 10,173 | 2,775 | (9,307) | 15,154 |
| Provision for income taxes | 1,536 | 2,903 | 738 | | 5,177 |
| Net earnings (loss) | \$ 9,977 | 7,270 | 2,037 | (9,307) | 9,977 |

CONSOLIDATED STATEMENT OF OPERATIONS

| | Three Months Ended March 31, 2003 | | | | |
|---|-----------------------------------|--------------|--------------|--------------|--------------|
| | | Guarantor | Nonguarantor | | Consolidated |
| | Parent | Subsidiaries | Subsidiaries | Eliminations | Total |
| (In Thousands) | | | | | |
| Net sales | \$ | 237,187 | 26,682 | (12,379) | 251,490 |
| Cost of sales | | 199,522 | 22,007 | (12,379) | 209,150 |
| Gross profit | | 37,665 | 4,675 | | 42,340 |
| Selling and administrative expense | | 21,713 | 3,530 | | 25,243 |
| Operating income | | 15,952 | 1,145 | | 17,097 |
| Interest expense (income) | (5,361) | 10,932 | 292 | | 5,863 |
| Equity in (earnings) loss of subsidiaries | (3,750) | (609) | | 4,359 | |

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| | | | | | |
|-------------------------------------|----------|-------|-----|---------|--------|
| Earnings (loss) before income taxes | 9,111 | 5,629 | 853 | (4,359) | 11,234 |
| Provision for income taxes | 1,941 | 1,879 | 244 | | 4,064 |
| Net earnings (loss) | \$ 7,170 | 3,750 | 609 | (4,359) | 7,170 |

CONSOLIDATED BALANCE SHEET

| | March 31, 2004 | | | | |
|---|-------------------|---------------------------|------------------------------|--------------------|-----------------------|
| | Parent | Guarantor Subsidiaries | Nonguarantor Subsidiaries | Eliminations | Consolidated Total |
| (In Thousands) | | | | | |
| Assets | | | | | |
| Current assets: | | | | | |
| Cash and cash equivalents | \$ 6 | 5,145 | 6,278 | | 11,429 |
| Receivables | | 125,338 | 24,269 | | 149,607 |
| Inventories | | 308,634 | 12,808 | | 321,442 |
| Prepaid expenses and other current assets | | 3,576 | 183 | | 3,759 |
| Deferred income taxes | | 19,035 | 40 | | 19,075 |
| Total current assets | 6 | 461,728 | 43,578 | | 505,312 |
| Property and equipment | | 30,638 | 732 | | 31,370 |
| Investment in subsidiaries | 753,859 | 32,830 | | (786,689) | |
| Intercompany receivables | | 258,730 | | (258,730) | |
| Goodwill | | 44,904 | 1,939 | | 46,843 |
| Intangible assets | | 50,944 | | | 50,944 |
| Deferred income taxes | | 31,040 | 383 | | 31,423 |
| Other assets | 7,220 | 4,948 | 3 | | 12,171 |
| Total assets | \$ 761,085 | 915,762 | 46,635 | (1,045,419) | 678,063 |
| Liabilities and Shareholders' Equity | | | | | |
| Current liabilities: | | | | | |
| Current portion of long-term debt | \$ | 2,909 | 11 | | 2,920 |
| Revolving line of credit | | | 473 | | 473 |
| Accounts payable | 1 | 111,671 | 1,033 | | 112,705 |
| Accrued expenses | 7,379 | 30,589 | 4,492 | | 42,460 |
| Total current liabilities | 7,380 | 145,169 | 6,009 | | 158,558 |
| Long-term debt | 200,000 | 4,282 | 17 | | 204,299 |
| Intercompany payables | 242,642 | | 16,088 | (258,730) | |
| Other liabilities | | 4,143 | | | 4,143 |
| Commitments and contingencies | | | | | |
| Shareholders' equity | | | | | |
| Common stock | 342 | 33 | 7,542 | (7,575) | 342 |
| Additional paid-in capital | 440,247 | 862,357 | 9,918 | (872,275) | 440,247 |
| Retained earnings (accumulated deficit) | (95,322) | (95,572) | 7,061 | 88,511 | (95,322) |
| Treasury stock, at cost | (28,218) | | | | (28,218) |
| Unearned compensation - restricted stock | (1,336) | | | | (1,336) |
| Accumulated other comprehensive loss | (4,650) | (4,650) | | 4,650 | (4,650) |
| Total shareholders' equity | 311,063 | 762,168 | 24,521 | (786,689) | 311,063 |
| Total liabilities and shareholders' equity | \$ 761,085 | 915,762 | 46,635 | (1,045,419) | 678,063 |

CONSOLIDATED BALANCE SHEET

| | December 31, 2003 | | | | Consolidated Total |
|---|-------------------|---------------------------|------------------------------|--------------------|-----------------------|
| | Parent | Guarantor Subsidiaries | Nonguarantor Subsidiaries | Eliminations | |
| | Parent | Subsidiaries | Subsidiaries | Eliminations | |
| (In Thousands) | | | | | |
| Assets | | | | | |
| Current assets: | | | | | |
| Cash and cash equivalents | \$ | 21,187 | 2,237 | | 23,424 |
| Receivables | | 118,972 | 20,307 | | 139,279 |
| Inventories | | 315,896 | 11,964 | | 327,860 |
| Prepaid expenses and other current assets | | 2,344 | 157 | | 2,501 |
| Deferred income taxes | | 19,036 | 39 | | 19,075 |
| Total current assets | | 477,435 | 34,704 | | 512,139 |
| Property and equipment | | 31,226 | 803 | | 32,029 |
| Investment in subsidiaries | 748,125 | 30,793 | | (778,918) | |
| Intercompany receivables | | 262,513 | | (262,513) | |
| Goodwill | | 44,904 | 1,939 | | 46,843 |
| Intangible assets | | 51,908 | | | 51,908 |
| Deferred income taxes | | 35,376 | 373 | | 35,749 |
| Other assets | 7,376 | 5,147 | 1 | | 12,524 |
| Total assets | \$ 755,501 | 939,302 | 37,820 | (1,041,431) | 691,192 |
| Liabilities and Shareholders' Equity | | | | | |
| Current liabilities: | | | | | |
| Current portion of long-term debt | \$ | 3,282 | 11 | | 3,293 |
| Revolving line of credit | | | 509 | | 509 |
| Accounts payable | 34 | 137,548 | 855 | | 138,437 |
| Accrued expenses | 3,567 | 32,756 | 3,244 | | 39,567 |
| Total current liabilities | 3,601 | 173,586 | 4,619 | | 181,806 |
| Long-term debt | 200,000 | 3,391 | 20 | | 203,411 |
| Intercompany payables | 251,816 | | 10,697 | (262,513) | |
| Other liabilities | | 5,891 | | | 5,891 |
| Commitments and contingencies | | | | | |
| Shareholders' equity | | | | | |
| Common stock | 339 | 33 | 7,542 | (7,575) | 339 |
| Additional paid-in capital | 439,080 | 862,357 | 9,918 | (872,275) | 439,080 |
| Retained earnings (accumulated deficit) | (105,299) | (101,306) | 5,024 | 96,282 | (105,299) |
| Treasury stock, at cost | (27,867) | | | | (27,867) |
| Unearned compensation - restricted stock | (1,519) | | | | (1,519) |
| Accumulated other comprehensive loss | (4,650) | (4,650) | | 4,650 | (4,650) |
| Total shareholders' equity | 300,084 | 756,434 | 22,484 | (778,918) | 300,084 |
| Total liabilities and shareholders' equity | \$ 755,501 | 939,302 | 37,820 | (1,041,431) | 691,192 |

CONSOLIDATED STATEMENT OF CASH FLOWS

Three Months Ended March 31, 2004

| | Guarantor | | Nonguarantor | | Consolidated |
|--|-----------|--------------|--------------|--------------|--------------|
| | Parent | Subsidiaries | Subsidiaries | Eliminations | Total |
| (In Thousands) | | | | | |
| Operating activities: | | | | | |
| Net earnings (loss) | \$ 9,977 | 7,270 | 2,037 | (9,307) | 9,977 |
| Depreciation and amortization | 255 | 3,968 | 70 | | 4,293 |
| Deferred income taxes | | 4,337 | (9) | | 4,328 |
| Compensation expense on restricted stock awards | 183 | | | | 183 |
| Changes in: | | | | | |
| Receivables | | (6,366) | (3,962) | | (10,328) |
| Inventories | | 7,262 | (844) | | 6,418 |
| Intercompany receivables and payables | (9,174) | 3,782 | 5,392 | | |
| Accounts payable | (33) | 12,122 | 169 | | 12,258 |
| Accrued expenses | 3,812 | (2,167) | 1,248 | | 2,893 |
| Other, net | 1,536 | (3,130) | (31) | | (1,625) |
| Net cash provided by (used for) operating activities | 6,556 | 27,078 | 4,070 | (9,307) | 28,397 |
| Investing activities: | | | | | |
| Capital expenditures | | (1,432) | | | (1,432) |
| Purchase of distribution rights | | (800) | | | (800) |
| Investment in subsidiaries | (7,270) | (2,037) | | 9,307 | |
| Sales of property, plant and equipment | | 5 | 1 | | 6 |
| Net cash provided by (used for) investing activities | (7,270) | (4,264) | 1 | 9,307 | (2,226) |
| Financing activities: | | | | | |
| Debt issue costs paid | (99) | | | | (99) |
| Issuance of common stock | 1,170 | | | | 1,170 |
| Purchase of treasury stock | (351) | | | | (351) |
| Net change in revolving credit facility | | | (36) | | (36) |
| Cash overdrafts | | (37,999) | 9 | | (37,990) |
| Debt repaid | | (857) | (3) | | (860) |
| Net cash provided by (used for) financing activities | 720 | (38,856) | (30) | | (38,166) |
| Change in cash and cash equivalents | 6 | (16,042) | 4,041 | | (11,995) |
| Cash and cash equivalents, beginning of period | | 21,187 | 2,237 | | 23,424 |
| Cash and cash equivalents, end of period | \$ 6 | 5,145 | 6,278 | | 11,429 |

CONSOLIDATED STATEMENT OF CASH FLOWS

Three Months Ended March 31, 2003

| | Guarantor | | Nonguarantor | | Consolidated |
|--|-----------|--------------|--------------|--------------|--------------|
| | Parent | Subsidiaries | Subsidiaries | Eliminations | Total |
| (In Thousands) | | | | | |
| Operating activities: | | | | | |
| Net earnings (loss) | \$ 7,170 | 3,750 | 609 | (4,359) | 7,170 |
| Depreciation and amortization | | 4,590 | 34 | | 4,624 |
| Deferred income taxes | | 4,286 | (25) | | 4,261 |
| Paid-in-kind interest | | 202 | | | 202 |
| Compensation expense on restricted stock awards | 158 | | | | 158 |
| Changes in: | | | | | |
| Receivables | | (7,296) | 841 | | (6,455) |
| Inventories | | 21,320 | (362) | | 20,958 |
| Intercompany receivables and payables | (5,514) | 5,986 | (462) | (10) | |
| Accounts payable | 8 | 6,623 | 296 | | 6,927 |
| Accrued expenses | 1,929 | (7,917) | 91 | | (5,897) |
| Other, net | | (1,545) | 15 | | (1,530) |
| Net cash provided by (used for) operating activities | 3,751 | 29,999 | 1,037 | (4,369) | 30,418 |
| Investing activities: | | | | | |
| Capital expenditures | | (1,181) | (184) | | (1,365) |
| Investment in subsidiaries | (3,750) | (619) | | 4,369 | |
| Net cash provided by (used for) investing activities | (3,750) | (1,800) | (184) | 4,369 | (1,365) |
| Financing activities: | | | | | |
| Cash overdrafts | | (27,624) | 103 | | (27,521) |
| Net change in revolving credit facility | | (1,693) | 115 | | (1,578) |
| Debt repaid | | (645) | (3) | | (648) |
| Other | (1) | | | | (1) |
| Net cash provided by (used for) financing activities | (1) | (29,962) | 215 | | (29,748) |
| Change in cash and cash equivalents | | (1,763) | 1,068 | | (695) |
| Cash and cash equivalents, beginning of period | | 3,330 | 1,667 | | 4,997 |
| Cash and cash equivalents, end of period | \$ | 1,567 | 2,735 | | 4,302 |

Item 2: Management's Discussion and Analysis of Financial Condition and Results of Operations

Executive Overview

We are the largest independent global provider of new parts, supply-chain management and other related value-added services to the aerospace aftermarket. The aerospace aftermarket consists of parts needed for the scheduled and unscheduled maintenance, repair and modification of aircraft already in use but does not include parts used in the construction of new aircraft or engines. We serve this market through our two wholly-owned subsidiaries, Aviall Services, Inc., or Aviall Services, and Inventory Locator Service, LLC, or ILS. Aviall Services provides new parts and related supply-chain management services to the aerospace industry, and ILS operates electronic marketplaces for buying and selling parts, equipment and services for the aerospace, defense and marine industries.

Aviall Services purchases a broad range of new parts, components and supplies from over 200 original equipment manufacturers, or OEMs, and resells them to over 17,500 government/military, general aviation/corporate and commercial airline customers, including over 290 airlines. Aviall Services also provides value-added services to our customers and suppliers, such as repair and assembly services, supply-chain management services and information-gathering and delivery services.

ILS operates electronic marketplaces for buying and selling parts, equipment and services for the global aerospace, defense and marine industries. With more than 13,000 users in more than 82 countries, ILS's electronic marketplaces contain more than 53 million line items representing over five billion parts for sale. ILS also maintains databases of over 112 million cross-referenced United States, or U.S., government records, allowing users to research manufacturers and prices for specific parts, locate alternate parts, find additional uses and markets for parts and review U.S. government procurement histories.

Our first quarter 2004 net earnings of \$10.0 million or \$0.30 diluted earnings per share increased 39% compared to \$7.2 million net earnings or \$0.22 diluted earnings per share in the first quarter of 2003. Our positive results reflect a general strengthening in sales across all our market and geographic sectors, the incremental impact of new Honeywell products added in 2003 and a continuing increase in military-related parts sales. In addition, while our selling and administrative expense increased \$2.4 million in the first quarter of 2004 compared to the first quarter of 2003, we continue to benefit from leveraging selling and administrative expense as a percentage of sales. Our first quarter 2004 selling and administrative expense as a percentage of sales was 9.7% compared to 10.0% in the first quarter of 2003.

Our future strategy will continue to focus on the acquisition of new long-term supplier contracts, delivering superior customer service, expanding the supplier base and product offerings and investing in technology and infrastructure to increase supplier and customer efficiencies. We will also continue to evaluate potential strategic acquisitions. We believe our ability to grow at a pace similar to that which we experienced since 2000 will depend on the award of one or a series of new long-term scalable contracts, the expansion of our supplier base and product offerings and/or completion of a strategic acquisition. The timing and length of the process to procure a new long-term agreement or relationship or a strategic acquisition is unpredictable. We are pursuing a number of opportunities for additional growth. In addition, the economies of scale derived from these recent contracts may not be indicative of our future results.

We previously announced that net earnings from continuing operations in 2004 would be in the range of approximately \$34.5 million to \$36.0 million or equivalent to approximately \$1.06 to \$1.10 per diluted share based upon the current number of diluted shares. While earnings for the first quarter of 2004 were above expectations, we have not revised our previous earnings estimates at this time.

Critical Accounting Policies

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For a discussion of our critical accounting policies refer to Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations Critical Accounting Policies included in our Annual Report on Form 10-K for the year ended December 31, 2003. There have been no material changes to the critical accounting policies discussed in our Annual Report on Form 10-K for the year ended December 31, 2003.

Results of Operations-Three Months Ended March 31, 2004 Compared to Three Months Ended

March 31, 2003

Net Sales. Net sales for Aviall Services were \$276.4 million, an increase of \$31.9 million or 13.1% from the \$244.5 million recorded in the first quarter of 2003. Sales for Aviall Services improved in each geographic region: the Americas region increased \$24.4 million or 11.9%; Europe increased \$2.8 million or 16.4%; and the Asia-Pacific region increased \$4.7 million or 21.3%. Sales also improved in all markets with a general strengthening seen across all sectors. Sales in the government/military sector increased \$12.0 million or 9.1% and sales in the general aviation/corporate sector increased \$6.2 million or 10.1% primarily as the overall market strengthened. Sales in the commercial airline sector increased \$13.7 million or 26.8% due primarily to the addition of the new Honeywell product lines and stronger sales volumes in the sector. Sales of products under the Rolls-Royce T56 distribution agreement were \$126.0 million and \$122.5 million in the first quarter of 2004 and 2003, respectively. Aggregate sales of products supplied by Rolls-Royce and Honeywell were \$185.9 million and \$165.1 million in the first quarter of 2004 and 2003, respectively.

Net sales for ILS were \$7.1 million, an increase of \$0.1 million or 1.4% from the \$7.0 million recorded in the first quarter of 2003.

Gross Profit. Gross profit of \$47.1 million increased \$4.8 million or 11.3% in the first quarter of 2004 compared to \$42.3 million in the first quarter of 2003. Gross profit as a percentage of net sales was 16.6% in the first quarter of 2004 as compared to 16.8% in the first quarter of 2003. The increased gross profit amount was due to higher sales volumes as the mix of products and prices were substantially similar year-over-year.

Selling and Administrative Expense. Selling and administrative expense increased \$2.4 million to \$27.6 million in the first quarter of 2004 but decreased as a percentage of net sales to 9.7% from 10.0% in the first quarter of 2003. Selling and administrative expense increased due to higher salary and benefit costs and Sarbanes-Oxley implementation costs.

Interest Expense. Interest expense decreased \$1.5 million to \$4.4 million in the first quarter of 2004 from \$5.9 million in the first quarter of 2003. Noncash interest expense amounted to \$0.4 million and \$1.3 million in 2004 and 2003, respectively. Our interest expense declined due to the refinancing completed in June 2003 and the interest swap put in place in the fourth quarter of 2003.

Income Tax Expense. Income tax expense for the first quarter of 2004 was \$5.2 million, and our effective tax rate was 34.2%. In the first quarter of 2003, our income tax expense was \$4.1 million, and our effective tax rate was 36.2%.

Cash refunds received for federal, state and foreign income taxes were \$0.3 million in the first quarter of 2004. Cash payments made for federal, state and foreign income taxes were \$0.3 million in the first quarter of 2003. Our cash income tax expense is primarily comprised of Alternative Minimum Tax, or AMT, and foreign taxes on our foreign operations. Our cash income tax expense continues to be substantially lower than U.S. federal statutory rate through the use of our U.S. federal net operating loss.

Preferred Stock Dividend. The noncash preferred stock dividend of \$1.1 million in March 2003 resulted from the issuance of 1,108 shares of Series D Redeemable Preferred Stock as payment of the quarterly payable-in-kind dividend on the Series D Redeemable Preferred Stock due March 31, 2003.

Liquidity and Capital Resources

Cash Flow. Net cash flow provided by operations was \$28.4 million in the first three months of 2004 compared to \$30.4 million in the first three months of 2003. The \$2.0 million decrease in cash provided by operating activities in 2004 compared to the same period in 2003 resulted primarily from the decline in cash generated from changes in Variable Working Capital, defined as receivables plus inventories less accounts payable. Aviall Services inventory turns improved from 3.1 turns in December 2003 to 3.2 turns in March 2004 due to higher sales volumes. The days sales outstanding for Aviall's receivables increased from 43 days at December 31, 2003 to 46 days at March 31, 2004.

Capital expenditures were \$1.4 million in the first three months of both 2004 and 2003. Capital spending in 2004 was primarily for upgrades and enhancements associated with both our systems and operations infrastructure at Aviall Services and ILS. Capital spending in 2003 was primarily for upgrades to the Aviall Services enterprise resource planning software, computer hardware and operations infrastructure. Based on capital projects currently approved by our board of directors, we expect to make capital expenditures, including noncash capital amounts, totaling approximately \$12.9 million in 2004. This assumes that no major distribution agreements are entered into in 2004. We review our capital expenditure program periodically and modify it as required to meet current business needs. Under the Credit Facility, our capital expenditure limit is approximately \$12.9 million, comprised of a \$11.0 million limit for 2004 plus \$1.9 million of carryover amounts from 2003.

Net cash flow used for financing activities was \$38.2 million in the first three months of 2004, resulting primarily from a decrease in our cash overdraft position, and \$29.7 million in the first three months of 2003, also resulting primarily from a decrease in our cash overdraft position.

Our cash provided by operating activities decreased by \$2.0 million to \$28.4 million during the three month period ended March 31, 2004 compared to the same period in 2003. This was after investing \$8.3 million in Variable Working Capital, in the aggregate, in 2004 as compared to \$21.4 million, in the aggregate, in 2003. Improved inventory management in the first quarter of 2004 compared to the same period in 2003 was the primary reason for the lower investment in Variable Working Capital. In 2004, we invested \$2.2 million in distribution rights and net capital expenditures compared to \$1.4 million in 2003. The combined cash provided in the first three months of 2004 of \$26.2 million for both operating and investing activities together with the \$1.2 million of common stock issued and the use of \$12.0 million of cash funded a decrease in our cash overdraft position. In the first three months of 2003, the combined cash of \$29.1 million from operating and investing activities also funded a decrease in our cash overdraft position with a negligible change in our cash balance. Overdraft positions arise when we settle our accounts payable by issuing checks at month end and the recipients of these checks have not presented them to our banks for payment before our cut-off for accounting purposes. Generally accepted accounting principles treats these amounts similar to debt in the statement of cash flows by presenting cash overdrafts as a financing activity; however, the balance sheet reflects these amounts as accounts payable. We expect to continue large month end settlements with our major suppliers but the overdrafts will change in accordance with the variable amounts of product shipped to us from time to time.

Assuming our current level of internal growth, profitability, and the present relationship between increased revenues, Variable Working Capital requirements and our annual capital expenditures, we expect to generate strong positive cash flows from operations although these may be offset by overdraft obligations when our business is growing. Assuming the foregoing, we project cash flow in 2004 for operating activities will exceed \$30.0 million. Our cash flow from operating activities does, however, depend on the timing of the delivery and payment for inventory as discussed in connection with the cash flow summary analysis. In some months, we receive much larger deliveries than the average of the preceding several months. These larger deliveries can significantly alter our cash flow for that month and on a cumulative basis for both the quarter and the fiscal year to date. In 2003 and 2002, we received large deliveries in November, which when paid for in December reduced our cash flow from operations for that quarter and twelve month period. As a result, in 2004, we expect to fund internal growth, working capital and capital expenditures from cash flow from operations. In 2004, we do not expect to borrow any material amounts under our Credit Facility nor to sell debt, equity or other securities on our behalf under our shelf registration statement to fund expected internal growth, working capital and capital expenditures. However, if we are awarded one or more long-term parts agreements in 2004 that require significant investments in distribution rights and inventory, if we enter into a strategic acquisition or if our current projections prove to be inaccurate, we may be required to borrow significant amounts under our Credit Facility or to sell debt, equity or other securities under our shelf registration statement.

Senior Unsecured Debt. We have \$200.0 million of Senior Notes outstanding. The Senior Notes bear interest at 7.625% per annum and mature on July 1, 2011, unless previously redeemed at our option. We may redeem some or all of the Senior Notes at specified redemption prices at any time after July 1, 2007. In addition, prior to July 1, 2006, we may redeem up to 35% of the Senior Notes from the proceeds of qualifying equity offerings.

The Senior Notes are our senior unsecured obligations and are equal in right of payment to all of our senior indebtedness. The Senior Notes are guaranteed on a senior unsecured basis by each of our domestic subsidiaries.

In November 2003, we entered into an interest rate swap agreement to manage interest rate risk exposure on \$50.0 million of the \$200.0 million principal amount of Senior Notes. Under this agreement, we receive fixed rate amounts in exchange for floating rate interest payments without an exchange of the underlying principal amount.

Senior Secured Debt. Our Credit Facility consists of a \$200.0 million revolving credit and letter of credit facility due as a balloon payment in 2006, with availability determined by reference to a borrowing base calculated using our eligible accounts receivable and inventory and after deducting reserves required by the lenders. As of March 31, 2004, we had no borrowings outstanding under the Credit Facility and had issued letters of credit for \$1.0 million. We had \$199.0 million available for additional borrowings under the Credit Facility and our borrowing base was \$203.2 million as of March 31, 2004. Borrowings under the Credit Facility bear interest, at our option, based upon either: a Eurodollar Rate plus an applicable margin ranging from 2.5% to 3.0% depending upon our financial ratios or a Base Rate plus an applicable margin ranging from 1.5% to 2.0% depending upon the same financial ratios. We utilize both of these interest rate options. As of March 31, 2004, the interest rate on the Credit Facility was 5.50%. A commitment fee of 0.5% is payable quarterly in arrears on the daily unused portion of the Credit Facility. Obligations under the Credit Facility are collateralized by substantially all of our domestic assets and 65% of the stock of each of our foreign subsidiaries. The Credit Facility also contains default clauses that permit the acceleration of all amounts due following an event of default at the discretion of the lenders, and lock-box provisions that apply our cash collections to outstanding borrowings. Based on the terms of the Credit Facility and pursuant to EITF Issue No. 95-22, Balance Sheet Classification of Revolving Credit Agreement Obligations Involving Lock-Box Arrangements, we have classified amounts outstanding under the Credit Facility as current.

We also maintain a revolving credit facility in Canada with a total availability of Canadian \$6.0 million. We had an outstanding balance at March 31, 2004 equivalent to U.S. \$0.5 million.

Debt Covenants. The Credit Facility contains various restrictive operating and financial covenants, including several that are based on earnings before interest, taxes, depreciation, amortization, extraordinary gains or losses, and one-time items, or Adjusted EBITDA.

We must comply with a maximum leverage ratio covenant that measures the ratio of our outstanding debt to our Adjusted EBITDA for the trailing four quarters. This maximum leverage ratio covenant was 3.0 to 1 at March 31, 2004 and periodically declines until it reaches 2.50 to 1 for December 31, 2004 and all periods thereafter. We must also comply with a minimum interest coverage ratio covenant that measures the ratio of our Adjusted EBITDA for the trailing four quarters to our interest expense during the trailing four quarters. The minimum interest coverage ratio covenant was 3.0 to 1 at March 31, 2004 and periodically increases until it reaches 3.50 to 1 for December 31, 2004 and all periods thereafter. Furthermore, we must maintain a tangible net worth at or above certain levels. As of March 31, 2004, the required tangible net worth was \$201.9 million. Our tangible net worth covenant will periodically increase until it reaches \$315.3 million on December 31, 2006, at which time it will expire. Finally, we must limit our capital expenditures to no more than \$12.9 million for 2004, which includes \$1.9 million of allowed carryover spending from 2003, and \$11.0 million for each of 2005 and 2006 plus any carryover from each prior year.

The Senior Notes also contain various restrictive covenants. We may not incur additional indebtedness unless we maintain a consolidated interest coverage ratio of at least 2.0 to 1.0 or unless the debt is otherwise permitted under the indenture. The consolidated interest coverage ratio measures the ratio of our EBITDA, as defined in the indenture relating to the Senior Notes, for the trailing four quarters to our interest expense for such quarters. Subject to specified exceptions, we may not make payments on or redeem our capital stock, make certain investments or make other restricted payments unless we maintain a consolidated interest coverage ratio of at least 2.0 to 1.0 and otherwise have available 50% of cumulative consolidated net income or capital stock sale proceeds from which such payments may be made. We are unable to incur liens unless expressly permitted under the Senior Notes or unless the Senior Notes are equally and ratably secured. We may not sell or otherwise dispose of any of the capital stock of our subsidiaries unless specifically authorized. We must receive fair market value for any asset sales and the consideration must be paid at least 75% in cash, cash equivalents or assumed liabilities. To the extent such proceeds are received, we must reinvest any proceeds exceeding \$10 million in additional assets within a period of 365 days or thereafter repay senior debt or repurchase Senior Notes. Additionally, we must repurchase the Senior Notes at a price equal to 101% of the principal amount of the Senior Notes upon a change of control. The indenture relating to the Senior Notes also contains additional covenants.

We are currently, and expect to remain, in compliance for at least the next twelve months in all material respects with the covenants in the Credit Facility and the Senior Notes.

The following table presents a reconciliation of our EBITDA and Adjusted EBITDA, as defined in the Credit Facility, to net earnings (loss) for the trailing four quarters ended March 31, 2004:

| | Second Quarter 2003 | Third Quarter 2003 | Fourth Quarter 2003 | First Quarter 2004 | Total |
|--|---------------------------|--------------------------|---------------------------|--------------------------|---------|
| (In Thousands) | | | | | |
| Net earnings (loss) | \$ (3,964) | 8,166 | 9,406 | 9,977 | 23,585 |
| Earnings from discontinued operations | | | 125 | | 125 |
| Earnings (loss) from continuing operations | (3,964) | 8,166 | 9,281 | 9,977 | 23,460 |
| Plus: | | | | | |
| Income tax expense (benefit) | (2,395) | 3,366 | 3,770 | 5,177 | 9,918 |
| Interest and related expense | 22,924 | 4,938 | 4,565 | 4,345 | 36,772 |
| Depreciation and amortization expense | 3,531 | 3,732 | 3,804 | 3,842 | 14,909 |
| EBITDA | 20,096 | 20,202 | 21,420 | 23,341 | 85,059 |
| Noncash gains | (534) | (146) | (418) | (125) | (1,223) |
| Adjusted EBITDA | \$ 19,562 | 20,056 | 21,002 | 23,216 | 83,836 |

The Adjusted EBITDA calculation above is prepared in accordance with the terms of the Credit Facility. The noncash gains, which are included in the Adjusted EBITDA calculation in accordance with the terms of the Credit Facility, may occur again in the future. Depreciation and amortization expense above excludes debt issue cost and debt discount amortization. Interest and related expense above includes the \$17.3 million loss on extinguishment of debt recorded in the second quarter of 2003. Adjusted EBITDA is presented solely to provide information on our debt covenants, and EBITDA and Adjusted EBITDA should not be considered an alternative to operating results or cash flows calculated in accordance with generally accepted accounting principles.

Contractual Obligations. There have been no material changes in our contractual obligations as set forth in Item 7: Management's Discussion and Analysis of Financial Condition and Results of Operations Contractual Obligations in our Annual Report on Form 10-K for the year ended

December 31, 2003.

New Accounting Pronouncements. In December 2003, the FASB issued a revised Interpretation No. 46, or FIN 46R, Consolidation of Variable Interest Entities, an Interpretation of ARB No. 51, replacing the original interpretation issued in January 2003. FIN 46R requires certain entities to be consolidated by enterprises that lack majority voting interest when equity investors of those entities have insignificant capital at risk or they lack voting rights, the obligation to absorb expected losses, or the right to receive expected returns. Entities identified with these characteristics are called variable interest entities and the interests that enterprises have in these entities are called variable interests. These interests can derive from certain guarantees, leases, loans or other arrangements that result in risks and rewards that are disproportionate to the voting interests in the entities. We adopted FIN 46R as of March 31, 2004. Because we have no variable interest entities, the adoption of this statement did not have an effect on our consolidated financial position and results of operations.

In December 2003, the FASB issued a revised Statement of Financial Accounting Standards No. 132, or SFAS 132R, Employers Disclosures about Pensions and Other Postretirement Benefits, an Amendment of FASB Statements No. 87, 88, and 106, and a Revision of FASB Statement No. 132. This statement revises employers disclosures about pension plans and other postretirement benefit plans. It does not change the measurement or recognition of those plans required by FASB Statements No. 87, Employers Accounting for Pensions, No. 88, Employers Accounting for Settlements and Curtailments of Defined Benefit Pension Plans and for Termination Benefits and No. 106, Employers Accounting for Postretirement Benefits Other Than Pensions. The new fiscal disclosure requirements have been included in Note 13 Pension Plans and Postretirement Benefits to the consolidated financial statements included in our Annual Report on Form 10-K for the year ended December 31, 2003. The new interim disclosure requirements have been included in Note 6 Pension Plans and Postretirement Benefits.

Forward-Looking Statements

This report contains certain forward-looking statements (as such term is defined in the Private Securities Litigation Reform Act of 1995) that are based on the beliefs of our management, as well as assumptions and estimates made by, and information currently available to, our management. When used in this report, the words anticipate, believe, estimate, expect, intend and similar expressions, as they relate to us or our management, identify forward-looking statements. Such statements reflect our current views with respect to future events and are subject to risks, uncertainties and assumptions relating to our operations and results of operations as well as those of our customers and suppliers, including as a result of competitive factors and pricing pressures, shifts in market demand, general economic conditions and other factors including, among others, those that effect flight activity in the commercial, business, government/military, and general/corporate aviation segments, the business activities of our customers and suppliers and developments in information and communication technology. Additional risks are set forth in our Annual Report on Form 10-K for the year ended December 31, 2003. Should one or more of these risks or uncertainties materialize, or should underlying assumptions or estimates prove incorrect, actual results may vary materially from those described in the forward-looking statements.

Item 3: Quantitative and Qualitative Disclosures About Market Risk

We are exposed to market risk from changes in interest rates and foreign exchange rates. From time to time, we have used financial instruments to offset these risks. These financial instruments are not used for trading or speculative purposes. We did not experience any significant changes in market risk during the first three months of 2004. Our market risk is described in more detail in Item 7A: Quantitative and Qualitative Disclosures About Market Risk in our Annual Report on Form 10-K for the year ended December 31, 2003.

Item 4: Controls and Procedures

The term disclosure controls and procedures is defined in Rules 13a-15(e) and 15d-15(e) of the Securities Exchange Act of 1934, or the Exchange Act. This term refers to the controls and procedures of a company that are designed to ensure that information required to be disclosed by a company in the reports that it files or submits under the Exchange Act is recorded, processed, summarized and reported within the time periods specified by the Securities and Exchange Commission. Our management, including our Chief Executive Officer and Chief Financial Officer, has evaluated the effectiveness of our disclosure controls and procedures as of the end of the period covered by this quarterly report. Based upon that evaluation, our Chief Executive Officer and Chief Financial Officer have concluded that our disclosure controls and procedures were effective as of the end of the period covered by this quarterly report.

Based on management's determination in the fourth quarter of 2003 that ILS had not properly followed internal control procedures, beginning on April 1, 2004, the accounting functions for ILS were moved to Aviall's headquarters to ensure proper application of our internal controls and increase the efficiencies of our processes.

There were no changes to our internal control over financial reporting during our first fiscal quarter of 2004 that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting. At all times and even given the foregoing, we believe our disclosure controls and procedures provided reasonable assurance that information required to be disclosed in our reports under the Exchange Act was recorded, processed, summarized and reported within the time periods specified by the SEC.

PART II OTHER INFORMATION**Item 1: Legal Proceedings**

Not applicable.

Item 2: Changes in Securities and Use of Proceeds

| <u>Period</u> | <u>Total Number of Shares Purchased</u> | <u>Average Price Paid per Share</u> | <u>Total Number of Shares Purchased as Part of Publicly Announced Plans or Programs</u> | <u>Maximum Number (or Approximate Dollar Value) of Shares that May Yet be Purchased Under the Plans or Program</u> |
|----------------------------------|---|---|---|--|
| January 1 - January 31, 2004 (1) | 22,381 | \$ 15.70 | | |
| Total | 22,381 | \$ 15.70 | | |

- (1) In January 2001, we issued 104,657 shares of restricted stock to certain of our employees. In connection with the lapsing of restrictions on these shares of restricted stock, we withheld 22,381 of the shares to satisfy tax withholding obligations of those employees.

Item 3: Defaults Upon Senior Securities

Not applicable.

Item 4: Submission of Matters to a Vote of Security Holders

Not applicable.

Item 5: Other Information

Not applicable.

Item 6: Exhibits and Reports on Form 8-K

(a) Exhibits

31.1 Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934

31.2 Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934

32.1 Certifications pursuant to Rule 13a-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

(b) Reports on Form 8-K

None.

SIGNATURES

Pursuant to the requirements of the Securities Exchange Act of 1934, the registrant has duly caused this report to be signed on its behalf by the undersigned thereunto duly authorized.

AVIALL, INC.

April 27, 2004

By: /s/ Colin M. Cohen

Colin M. Cohen
Vice President and Chief Financial Officer
(Principal Financial Officer)

INDEX TO EXHIBITS

| Exhibit No. | Description |
|--------------------|---|
| 31.1 | Certification of Chief Executive Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934 |
| 31.2 | Certification of Chief Financial Officer pursuant to Rule 13a-14(a) of the Securities Exchange Act of 1934 |
| 32.1 | Certifications pursuant to Rule 13a-14(b) of the Securities Exchange Act of 1934 and 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 |