HURCO ANNUAL REPORT 2002

IT'S A DOG EAT DOG WORLD OUT THERE.

HERE'S WHY HURCO CUSTOMERS ARE WELL-FED.

THEY'RE WORKING HARDER, FASTER, SMARTER, WITH HURCO MACHINE TOOLS.

THE MACHINE SHOP ENVIRONMENT IN THE NEW MILLENNIUM IS NOTHING IF NOT TOUGH. OUR CUSTOMERS MUST DECREASE SET UP TIME, INCREASE SPEED OF MANUFACTURE AND REACT MORE QUICKLY TO A MULTITUDE OF EVER CHANGING CRITERIA. LEAD TIMES ARE SHORT. COMPETITION IS STIFF. THE LINE BETWEEN SUCCESS AND FAILURE IS THINNING. OUR CUSTOMERS NEED MACHINES THAT NOT ONLY HELP THEM CONFRONT THESE PROBLEMS BUT ARE EASIER TO OPERATE. **HURCO MACHINES AND CONTROLS DELIVER IN THIS DOG EAT DOG WORLD.** AND OUR CUSTOMERS ARE FIRST IN LINE AT THE LUNCH COUNTER.

DESPITE SIGNIFICANTLY LOWER REVENUES DUE TO THE WORLDWIDE ECONOMIC DOWNTURN, WE HAVE MAINTAINED A STRONG BALANCE SHEET AND CUT OUR BREAK EVEN POINT BY REDUCING OPERATING EXPENSES WHILE MAINTAINING OUR COMMITMENT TO R&D. WE STEP INTO THE FUTURE ENERGIZED AND INSPIRED.

PICTURED FROM LEFT TO RIGHT;
MICHAEL DOAR, CHAIRMAN & CEO
JAMES FABRIS, PRESIDENT & COO

LETTER TO THE SHAREHOLDERS

DEAR SHAREHOLDER, CUSTOMER AND EMPLOYEE,

2002 was played out against a backdrop of a weakened economy, corporate scandal and a variety of unsettling world events. Continuing the downward trend that began in 2001, the overall market for machine tools declined 30 percent, the most severe decline in 40 years. At Hurco, this decline resulted in a 23.5 percent decrease in revenue from 2001.

Still, as the front cover of this report suggests, we are fighters. We believe our products are the best in the world at increasing our customers' productivity. Through hard-earned customer loyalty, operational excellence, and continued innovation, Hurco will succeed — and so will our customers.

Last year, in my first letter to shareholders as Chairman and CEO of Hurco, I wrote that in 2002 we were going to focus on three things: our customers, our core competencies and profitability. In 2003, we will maintain focus on these three elements as we continue to build our business.

Customers In the recent past, companies in our industry talked about quality, price, and delivery. In today's world, these are all expected. At Hurco, every employee has dedicated himself or herself to making our customers winners. We are all committed to doing whatever it takes to help our customers succeed. Our job isn't just to satisfy the customer; our job is to WOW the customer so that he brags about our dedication to his friends and neighbors.

This is not a local or regional sentiment. The world has changed; we are part of a vast, complicated and global economy. Hurco customers are everywhere; over half of our machines are sold outside the U.S. As countries continue to enter this new global economy, Hurco will be there. We know the global market for machine tools and we know how to compete in it.

As part of our focus on core customers we successfully exited the OEM down acting press brake business, while concurrently strengthening our commitment to our Autobend™ control and back gauge systems.

Core Competencies Hurco's success has been built around our technically advanced, easy to use UltiMax control. Importantly, we can now say that our machine frames live up to the excellence of our controls. With the machine frame, control technology and software designed at our Indianapolis headquarters - and manufactured at Hurco owned sites globally, we control the complete product - a rarity in this industry. However, we have not rested on our laurels but continue to work hard on developing the "next generation" control, software and machine frame.

This focus has resulted in an unprecedented number of new product releases including: machines, software packages, a Windows™ - based control option, and the Max™ control.

Hurco's new VM1 is a true 6,800 pound machining center built around a solid cast iron frame and state-of-the-art UltiMax controls. With a work cube of 26" x 14 x 18" in a small footprint, the VM1 is a perfect fit for almost any shop for primary or secondary operations. The VM1's 15 hp, 8,000 rpm spindle, and 16 station swing arm Automatic Tool Changer provide fast throughput - improving overall shop profitability. The VM1 utilizes Hurco's new slim line touch screen color LCD Max control.

Several new models expanded Hurco's VMX high performance machining series. The VMX42 debuted with larger X and Y travels and an integrated chip conveyor standard. Our popular VMX50 is now available in a large tool (CAT50), 30 hp, 8000 rpm model the VMX50/50T and a high speed 40 hp, 15,000 rpm VMX50S. Our VMX50S machine utilizes Hurco's new Adaptive Surface Finishing software for full 3 axis contouring rates up to 600 ipm. The

TO SAY IT IS DIFFICULT TO HIRE AND RETAIN SKILLED MACHINISTS IN THE NEW ECONOMY IS LIKE SAYING THE SKY IS BLUE. HURCO HAS RESPONDED BY MAKING ITS EASY TO SET-UP AND CONTROL MACHINES EVEN EASIER TO SET-UP AND CONTROL. THE RESULT? SIGNIFICANT AND ONGOING OWNER SAVINGS. WE ARE NOT JUST REINVENTING OUR PRODUCT, WE ARE REINVENTING THE EXISTING STANDARD OF EXCELLENCE IN MACHINE TOOL DESIGN.



in-line spindle on our VMX50S incorporates high torque, low vibration design technology.

We also previewed several new products at IMTS (International Manufacturing Technology Show) that will be released in 2003 including our new WinMax™ CNC control option.

Additionally, we purchased advanced soft motion technology from a private development company, which will be key in developing our next generation control technology, further enhancing our core competency in machine tool controls.

Hurco's new products will keep our global customers competitive in today's challenging manufacturing environment by increasing productivity, increasing part accuracy, and reducing part cost.

Profitability We know we have to make a profit. With the adjustments made to our business in 2002, we are confident that we will be profitable in 2003. We have worked diligently on reducing our break-even point and with our recent new product launches we believe 2003 will be better in terms of revenue and profitability.

In 2002, Hurco did more than just survive the downturn. We focused on our core technologies and business while at the same time we reduced our operating expenses by 18.7 percent. Additionally we reduced our debt by 26%, positioning us well for 2003.

Thanks to the focus on our customers, core competencies, profitability and the resultant accomplishments listed above, Hurco is well positioned to take advantage of an improving business cycle. It truly is a "dog eat dog world" out there. But, as we say, Hurco customers are well fed. With our productivity enhancing machine tools, we expect them to continue to eat their competitors' lunch.

Sincerely,

Michael Doar, Chairman and CEO

THERE IS A THIN LINE BETWEEN SUCCESS AND FAILURE. HURCO MACHINE TOOLS MAKE US MORE PRODUCTIVE; MORE COMPETITIVE.

BOB KELSEY, TK & Associates

HURCO CUSTOMERS WIN

USER FRIENDLY, DEPENDABLE, AFFORDABLE

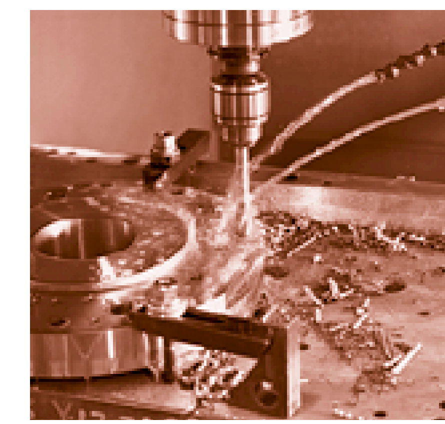
Bob Kelsey is accustomed to being successful, but you would never know it by his demeanor. He is soft-spoken, easy going and unfailingly polite. Still, there is no mistaking the fact that he is a serious business man, a hard-driver who for fifteen years has endured twelve hour days on the way to building TK & Associates into a top-notch tool, die, and precision machining house.

Kelsey's company, which began as a three - man proto-typing shop serving the needs of Bendix Brakes, is something of a prototype itself; it is a model of organization, focused energy and efficiency. One gets the feeling that when Bob Kelsey talks, he means what he says. He doesn't seem like the type of person to waste anything – even words. So, when he says he has built his company on fostering great relationships between himself, his employees and his clients - and on the strength of Hurco CNCs - you tend to believe him.

In the three years prior to the manufacturing down-turn of 2000, TK & Associates achieved an astounding 97% rate of growth and was named one of the United States' most successful "25 Fastest Growing Companies" by Industry Week magazine. Despite the obvious economic hurdles faced by U.S. manufacturing since then, TK is on solid financial footing and making money with annual revenues projected at approximately $6 million for 2002. Mr. Kelsey attributes much of his success to his six workhorse Hurco machining centers.

"There is no question in my mind that Hurco's conversational controls - their ease of use and the fact that they're easy to train people on - have helped us build our business. These are very high precision machines with very high precision controls that just happen to be easier to use than anything else I've seen," he said. "I frequently have one machinist operating two machines at the same time. Thanks to Hurco's dual screen controls they can be machining parts while concurrently programming or loading data for the next run keeping downtime between part runs to a minimum."

"My people love these machines and that, in and of itself, is a competitive advantage. The whole idea of 'conversational controls' was developed by Hurco and it shows," he continued. "Hurco processing is nearly flawless and the result for me is significant cost savings through reduction of the time it takes to



"THERE IS NO QUESTION IN MY MIND THAT HURCO'S CONVERSATIONAL CONTROLS – THEIR EASE OF USE AND THE FACT THAT THEY'RE EASY TO TRAIN PEOPLE ON – HAS HELPED US BUILD OUR BUSINESS."

manufacture the first part and time to convert from one part run to another."

TK machinists can sequence all the value added steps needed to machine a part - tool path generation, tool setup, part setup, and part inspection - quickly and easily. Whether the part information comes from a sketch, blueprint, or CAD generated DXF file, the English language prompts of UltiMax lead the machinist through a list of easy to understand machine part features that combine to create a part program. The standard graphics feature immediately verifies the tool path data and eliminates the need to dry run a part.

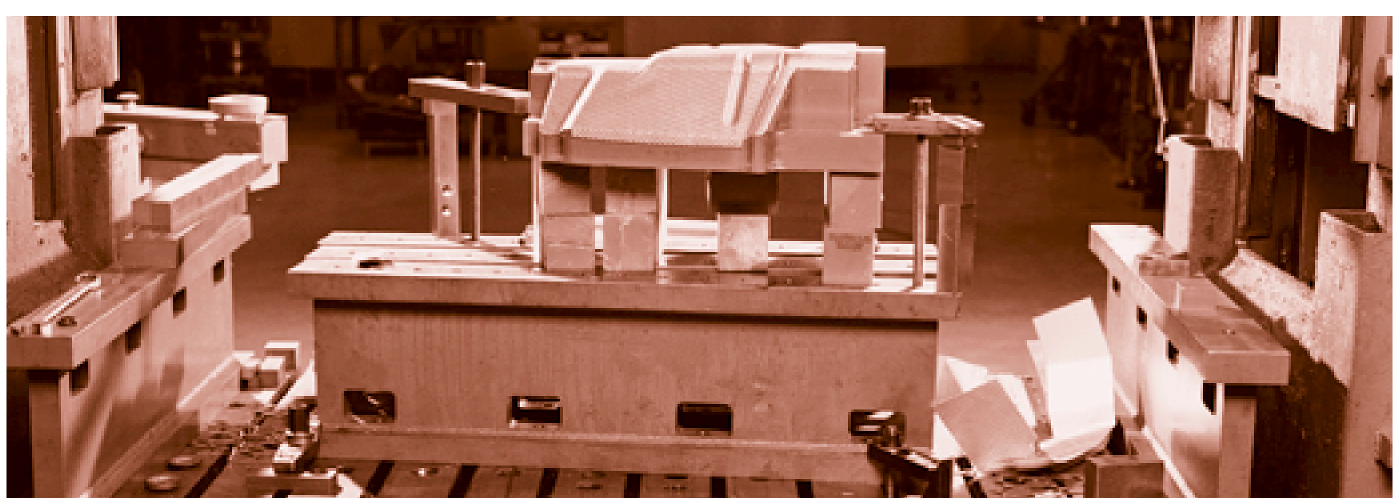
"We use the Hurco DXF translation software constantly, and it is quite a time saver. DXF allows us to download directly from CAD to the Hurco control. From there, our machinists use English language prompts to combine CAD features to make a part program without ever interacting with G-code. By using Hurco DXF at the machine, 100% dimensioning of hole locations and milling profiling at the CAD station is not necessary. That saves time, too," Kelsey said.

Kelsey also smartly added automatic and manual pallet changers to some of his CNCs that help decrease setup time for work like that for precision machining of inconel castings for aerospace and power generator turbines and segments. Kelsey's machinists preset castings outside the machine, which then drops set up time to zero and increases volume.

Kelsey is particularly enamored with Hurco's Conversational Probing System software.

"What I particularly like about our relationship with Hurco is that they listen to us - some of our shop floor experience and input helped them create a better probe," Kelsey said. "We really worked together on parts of its development. The reward for me is a better product that helps us deliver for our customers. It's truly a win/win situation."

The Hurco Conversational Probing Software played a key role in TK's work on the turbine projects mentioned previously. In order to accommodate the variations in castings for power generator turbines



"WHAT I PARTICULARLY LIKE ABOUT OUR RELATIONSHIP WITH HURCO IS THAT THEY LISTEN TO US - SOME OF OUR SHOP FLOOR EXPERIENCE AND INPUT HELPED THEM CREATE A BETTER PROBE. WE REALLY WORKED TOGETHER ON PARTS OF ITS DEVELOPMENT. THE REWARD FOR ME IS A BETTER PRODUCT THAT HELPS US DELIVER FOR OUR CUSTOMERS. IT'S TRULY A WIN/WIN SITUATION."

and segments, each work piece must be aligned before machining. Originally, dial indicators were used to true up each casting, fixture, and pallet to the machine's axes, which could take fifteen minutes to a half hour. With Hurco Conversational Probing, fixed points are set by the probe, then the software automatically adjusts the tool path to skew angles, thus minimizing setup time and eliminating program edits to accommodate the variations in castings.

For TK the addition of Hurco's Conversational Probing has meant improved part quality, elimination of data input errors, reduced scrap, increased part through-put, and a nine-week return on investment for the Probing Package.

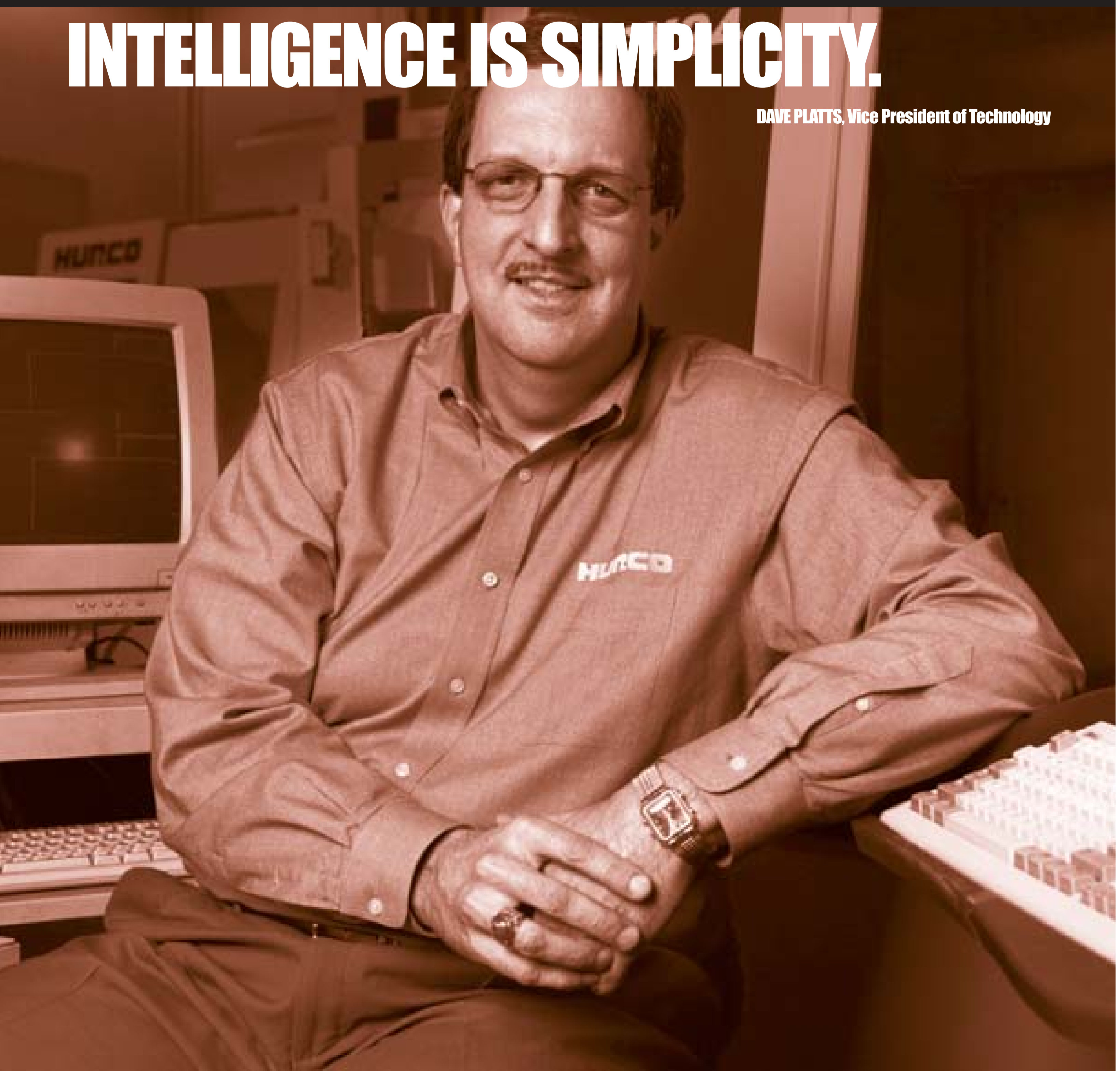
Customer service is another Hurco attribute that has Kelsey smiling.

"In the rare instances that we have a problem with a Hurco machine - and we have six machining centers – Hurco's people are here, they identify the problem, they get the necessary parts and they get us up and running again in no time. That is an incredible advantage for someone in my position because making deadlines is crucial."

It's the kind of advantage that means Bob Kelsey is taking a rare Saturday off on this fine early November weekend. He's looking forward to traveling to nearby South Bend, Indiana to watch his beloved Notre Dame Fighting Irish battle Rutgers. The furthest thing from his mind? Problems with his Hurco machines - they'll more than likely be humming along quite nicely back in LaPorte, in the capable hands of his machinists.

HURCO TECHNOLOGY GIVES OUR CUSTOMER THE RIGHT TOOL FOR THE RIGHT JOB. PLAIN & SIMPLE. INTELLIGENCE IS SIMPLICITY.

DAVE PLATTS, Vice President of Technology



HURCO TECHNOLOGY.

YOU HAVE QUESTIONS? WE HAVE ANSWERS.

Q: Why is manufacturing such a tough business now and how can Hurco help its customers win?

A: Due to relentless price competition, our customers are under constant pressure to lower their operating expenses. Hurco's easy to use equipment allows them to hire less-experienced operators and turn them into highly productive, Hurco-powered machinists. We should add that Hurco machines, in the hands of highly skilled, experienced operators create incredible efficiencies and help those operators become even more productive.

Our machines even allow smaller manufacturers to compete on price with larger ones for smaller-batch orders in today's "lean manufacturing" environment. Hurco customers are in a position to beat global competition through software automation, flexibility and speed of programming, setup, part machining, editing and just-in-time delivery - wherever in the world they operate.

Q: Why, specifically, are Hurco machines "easy to use?" How do they save owners money when training employees?

A: The Hurco UltiMax control is the leading "conversational - graphical control " in the world. It allows our customers to interact with the control and machine process intuitively - in his or her native language - using proprietary "soft keys" that implement a machine process oriented feature/function approach. In fact, Hurco pioneered conversational technology and its specific application to machining.

Q: How does Hurco affect process control and make machine shops more efficient?

A: Small batches of complex parts require custom programming and part specific process engineering each time a new design is received. This is tedious, time consuming engineering work and must

THE HURCO ULTIMAX CONTROL IS THE LEADING "CONVERSATIONAL – GRAPHICAL CONTROL " IN THE WORLD. IT ALLOWS OUR CUSTOMERS TO INTERACT WITH THE CONTROL AND MACHINE PROCESS INTUITIVELY.

SINCE 1996, OUR CUSTOMER SATISFACTION PROGRAM'S SUCCESS HAS BEEN OUTSTANDING. WARRANTY SERVICE CALLS HAVE DROPPED 74 PERCENT. WE ARE SHIPPING 34 PERCENT FEWER WARRANTY PARTS - WITH AN ASSOCIATED COST SAVINGS OF 49 PERCENT. WARRANTY LABOR COSTS WERE LOWERED BY 74 PERCENT.

Dave Skrzypczak, Manager, Customer Satisfaction

be executed by an experienced machinist who understands part fixturing design, tooling type selection, feed rate optimization, spindle speed optimization, toolpath optimization and machine capability knowledge – that is, unless the machine shop is Hurco-equipped. The Hurco UltiMax control has embedded knowledge of all these disciplines and "process assists" that are, essentially, *skills multipliers* that allow less-experienced machinists using color graphical verification to quickly, efficiently and accurately process small batch jobs. Essentially, our skills multipliers, amount to process engineering automation. Operators can maintain libraries of steel types, feed rates, tooling types, program code, process parameters and more. The knowledge in these libraries is retained for future jobs, regardless of who is operating the machine.

Q: How do Hurco machines bridge the gap between Applications and Process Engineering departments?

A: Most original M&G part code is created on CAM systems off-line, but the job of part process engineering cannot realistically be completed offline, or *away* from the machine tool. So, a disconnect often exists between the CAM system programmer/engineer and the shop floor machinist who has to fill in the blanks that inevitably exist in M&G code. The Hurco UltiMax bridges that gap by creating a CAM system environment, including color graphical representations that allows machinists to do final part design optimization and process engineering where all relevant variables can be identified - at the machine tool - the first time, error-free. This eliminates troublesome process engineering bottlenecks and redundant CAM staff editing. Even the smallest shop owners whose machines have embedded CAD/CAM software in PCs can create conversational Hurco part programs at the machine.

Q: What, specifically, are Hurco Data Blocks and why are they useful?

A: Data Blocks are pre-formatted instruction templates for execution by the machine. They allow a machinist to quickly generate tool paths by sequencing a series of easily identifiable cutting process steps from a small menu of "soft-key" options, and bring advanced CAM system programming and process engineering technology to mainstream tool usage.

Q: How much faster can Process Engineering changes be made conversationally on a Hurco as opposed to offline?

A: About 90% of 2.5D programming today is done offline in CAM. With Hurco's conversational Data Blocks, changes can be made approximately 4 times faster at the machine – and the changes are made by the operator, saving even more man hours.

Q: Are Hurco machines independently lab certified?

A: Yes. Hurco equipment is Met Lab Certified for UL listing, CSA and other national and local building code compliance. We are one of the few standard equipment builders to submit our equipment to this rigorous testing. Hurco owners find that, as a result, local code compliance and insurance is much easier to attain.

Q: What has Hurco done to increase customer satisfaction and cut warranty expenses?

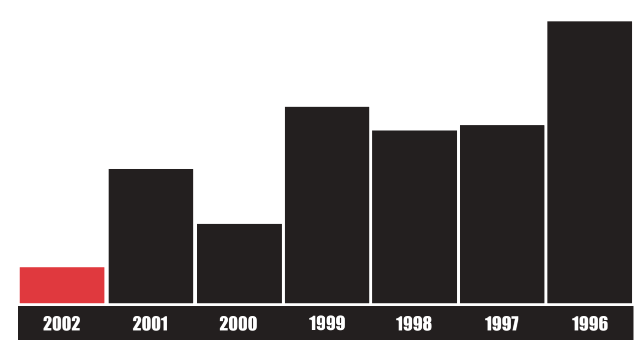
A: In 1996, Hurco established and committed to an aggressive Customer Satisfaction Program. The program's objectives are to continuously improve quality and reduce warranty costs via quantitative measurement of the frequency of service and part shipments during our products' warranty periods – and the resolution of identified problems by Hurco design, manufacturing, quality and sales officials. We wish to A) identify problem areas, and B) eliminate them.

A key component of this intensely analytical effort has been semi-annual world-wide service meetings attended by Hurco Service and Engineering Managers. Warranty issues are discussed, program progress is studied and new objectives are continually set. Program measurement is completed and reported on a quarterly basis to Hurco's Board and Sales Managers.

Finally, top Hurco executives are increasing the frequency of their site visits to increase their understanding of both how our machines operate at the customer level and the competitive landscape in which we operate. Customer satisfaction surveys are also periodically sent and analyzed by staff.

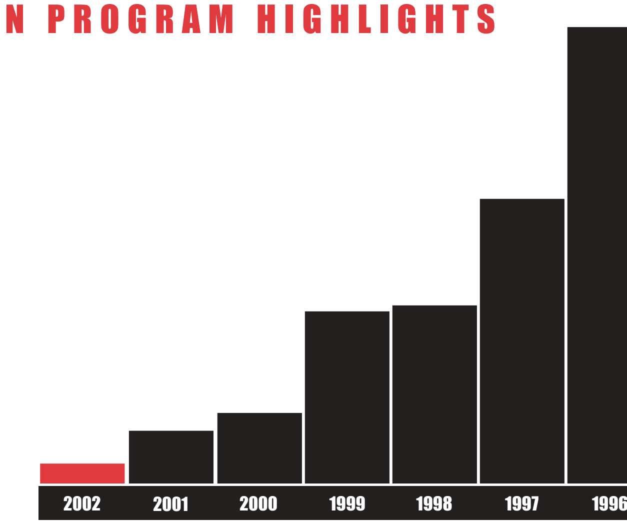
Since 1996, our progress has been nothing short of outstanding. The number of warranty service calls has dropped 74%. The number of warranty parts shipped has dropped 34% - a dollar value savings of 49%. The cost of warranty labor hours has dropped 74%.

HURCO'S U.S. CUSTOMER SATISFACTION PROGRAM HIGHLIGHTS



Warranty Parts Shipments

The number of warranty parts shipped has dropped 34% - a dollar value savings of 49% - in 2002.



Warranty Service Calls

The number of warranty service calls has dropped 74% in 2002.

THANKS TO HURCO'S NEARLY FLAWLESS PART PROCESSING, OUR MACHINES ARE THE SHOP FAVORITES OF MACHINISTS ALL OVER THE WORLD. THAT, IN AND OF ITSELF, IS A COMPETITIVE ADVANTAGE FOR OUR CUSTOMERS.

VMX30 Machining Center

Travels	(X,Y,Z) 30" x 20" x 24"
HP/RPM	17.6/10,000
Torque	185 ft-lbs @500 rpm
Rapids (X,Y)	1181 ipm
ATC	24, CAT 40 Pockets
Weight	9,800 lbs.

VMX42 Machining Center

Travels	(X,Y,Z) 42" x 24" x 24"
HP/RPM	24/10,000
Torque	210 ft-lbs @600 rpm
Rapids (X,Y)	1181 ipm
ATC	24, CAT 40 Pockets
Weight	14,000 lbs.

A FEW OF OUR MORE POPULAR MACHINING CENTERS.

VM1 Machining Center

Travel	(X,Y,Z) 26" x 14" x 18"
HP/RPM	15/8,000
Torque	54.3 ft-lbs@ 1450 rpm
Rapids (X,Y)	750 ipm
ATC	16, CAT 40 Pockets
Weight	6,800 lbs.

VMX24 Machining Center

Travels	(X,Y,Z) 24" x 20" x 24"
HP/RPM	12/10,000
Torque	85 ft-lbs @ 750 rpm
Rapids (X,Y)	1181 ipm
ATC	24, CAT 40 Pockets
Weight	9,300 lbs.

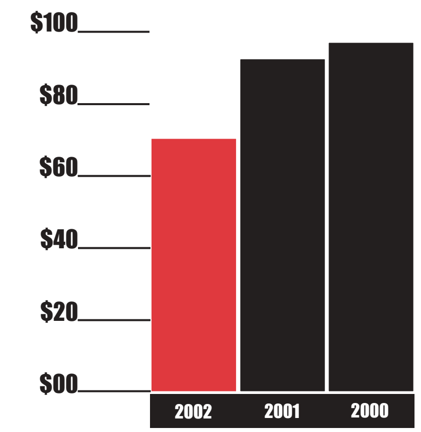
VMX50 Machining Center

Travels	(X,Y,Z) 50" x 26" x 24"
HP/RPM	24/10,000
Torque	219 ft. lbs. @ 600 rpm
Rapids (X,Y)	1181 ipm
ATC	24, CAT 40 Pockets
Weight	19,200 lbs.

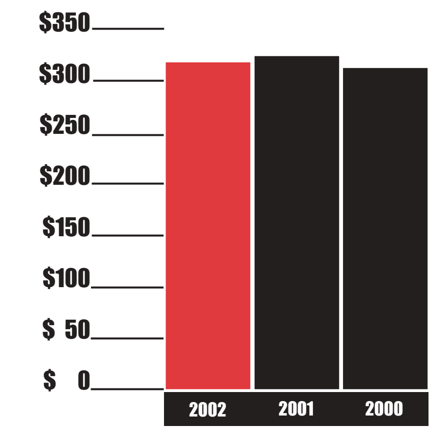
VMX64 Machining Center

Travels	(X,Y,Z) 64" x 34" x 30"
HP/RPM	24/10,000
Torque	252 ft-lbs @500 rpm
Rapids (X,Y)	705 ipm
ATC	40, CAT 40 Pockets
Weight	32,000 lbs.

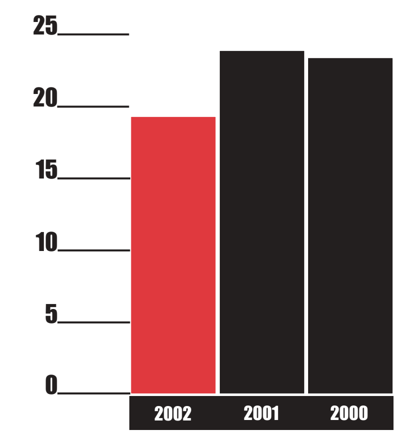
ALTHOUGH 2002 WAS A TOUGH YEAR IN THE MACHINE TOOL INDUSTRY, HURCO IS WELL-POSITIONED TO BE PROFITABLE IN 2003 THANKS TO DEBT REDUCTION, REDUCED OPERATING EXPENSES AND THE LIKELIHOOD OF A FRESHENING MARKET FOR OUR PRODUCTS...



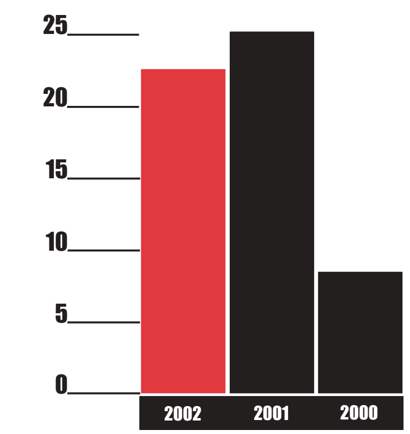
Sales and Service Fees
(in millions)
$70.5 million in 2002



Sales Per Employee
($ - in thousands)
$331 thousand in 2002



Operating Expenses
(millions)
$19.7 million in 2002



Total Debt to Capital
24.1% in 2002

HURCO FINANCIAL HIGHLIGHTS 2002

As of October 31,
(Dollars in thousands, except per share amounts)

			2002		2001	% Change
Sales and service fees		$	**70,486**	$	92,267	(23.6%)
Operating income (loss), before special charges		$	**(3,329)**	$	(778)	N/A
Restructuring and other special charges, net		$	**3,838**	$	143	N/A
Net income (loss)		$	**(8,263)**	$	(1,597)	N/A
Earning (loss) per common share (diluted)		$	**(1.48)**	$	(0.28)	N/A
Order intake		$	**66,991**	$	89,363	(25.0%)
Backlog		$	**5,315**	$	9,146	(41.9%)
Working capital		$	**20,350**	$	31,293	(35.0%)
Total debt		$	**8,885**	$	12,000	(26.0%)
Shareholders' equity		$	**28,017**	$	35,468	(21.0%)
Number of employees			**240**		277	(13.4%)
Stock Price	October 31	$	**1.55**	$	2.14	(27.6%)
	High	$	**3.35**	$	4.19	(20.0%)
	Low	$	**1.45**	$	2.08	(30.3%)

HURCO ELEVEN–YEAR SELECTED FINANCIAL DATA

(In thousands except per share data and number of employees)

For the Fiscal Year Ended	2002	2001	2000	1999	1998	1997	1996	1995	1994	1993	1992
Sales and service fees	$ **70,486**	$ 92,267	$ 96,204	$ 88,238	$ 93,422	$ 95,729	$ 99,351	$ 89,632	$ 72,628	$ 72,230	$ 87,828
Cost of sales and service (2)	**55,240**	69,005	70,827	64,064	65,483	67,956	70,930	66,162	57,063	61,802	65,902
Operating expenses (SG&A)	**19,658**	24,040	23,538	21,259	21,786	21,047	21,343	19,002	18,129	22,001	24,489
Restructuring and other expenses, net	**2,755**	143	300	(103)	1,162					6,750	1,070
Operating income (loss)	**(7,167)**	(921)	1,539	3,018	4,991	6,726	7,078	4,468	(2,564)	(18,323)	(3,633)
License fee income, net	**163**	723	5,365	304	6,974	10,095	590				
Interest expense	**634**	790	939	1,293	876	1,938	3,211	4,250	3,301	2,828	2,722
Other income (expense)	**(36)**	168	(359)	25	99	(51)	(99)	(14)	74	7	63
Income before taxes	**(7,674)**	(820)	5,606	2,054	11,188	14,832	4,358	204	(5,791)	(21,144)	(6,292)
Income tax expense (benefit)	**589**	777	571	252	1934	1,028	94				(503)
Net income (loss)	$ **(8,263)**	$ (1,597)	$ 5,035	$ 1,802	$ 9,254	$ 13,804	$ 4,264	$ 204	$ (5,791)	(21,144)	(5,789)
Average shares outstanding											
Basic	**5,583**	5,670	5,952	5,980	6,498	6,536	5,786	5,418	n/a	n/a	n/a
Diluted/Primary (1)	**5,583**	5,670	6,020	6,061	6,670	6,704	5,907	5,536	5,407	5,438	5,492
Earnings per share											
Basic	$ **(1.48)**	$ (0.28)	$ 0.85	$ 0.30	$1.42	$2.11	$ 0.74	$0.04	n/a	n/a	n/a
Diluted/Primary (1)	$ **(1.48)**	$ (0.28)	$ 0.84	$ 0.30	$1.39	$2.06	$ 0.72	$0.04	$ (1.07)	$ (3.89)	$ (1.05)
Dividends per share - common	**–**	–	–	–	–	–	–	–	–	$0.02	$0.17
Capital expenditures	**1,718**	1,918	1,899	2,157	2,328	2,235	1,879	1,617	1,261	1,663	3,999
Depreciation and amortization	**1,929**	2,196	2,519	2,428	2,138	2,078	2,677	2,861	3,019	3,556	2,964
EBITDA	**(5,111)**	2,166	9,064	5,775	14,202	18,848	10,246	7,315	529	(14,760)	(606)
EBITDA, excluding license fees and restructuring charge	**(1,436)**	1,586	3,999	5,368	8,390	8,753	9,656	7,315	529	(8,010)	464
Free cash flow	**5,174**	(6,191)	10,849	(3,203)	3,264	13,497	6,473	2,294	2,480	(1,753)	(10,192)
Gross profit margin %	**21.6%**	25.2%	26.4%	27.4%	29.9%	29.0%	28.6%	26.2%	21.4%	14.4%	25.0%
Operating income as % of sales	**(10.2%)**	(1.0%)	1.6%	3.4%	5.3%	7.0%	7.1%	5.0%	(3.5%)	(25.4%)	(4.1%)
Net return on sales	**(11.7%)**	(1.7%)	5.2%	2.0%	9.9%	14.4%	4.3%	0.2%	(8.0%)	(29.2%)	(6.5%)
Return on average equity	**(26.0%)**	(4.3%)	13.4%	4.9%	27.4%	60.1%	36.1%	2.8%	(56.7%)	(88.5%)	(14.9%)
Stock price range											
High	$ **3.35**	4.19	$ 5.88	$ 6.63	$ 9.25	$ 9.44	$ 7.25	$ 7.13	$ 4.75	$ 10.00	$ 14.00
Low	$ **1.45**	$ 2.08	$ 3.00	$ 3.38	$ 6.25	$ 4.25	$ 3.25	$ 2.75	$ 2.00	$ 1.75	$ 5.25

At Fiscal Year End	2002	2001	2000	1999	1998	1997	1996	1995	1994	1993	1992
Working capital	$ **20,350**	$ 31,293	$ 26,071	$ 33,276	$ 29,349	$ 22,852	$ 20,772	$ 19,877	$ 26,111	$ 33,002	$ 46,183
Current ratio	**1.96**	2.72	2.13	2.70	2.14	2.18	1.89	1.75	2.54	3.02	4.01
Total assets	$ **57,152**	$ 66,217	$ 65,024	$ 69,632	$ 71,696	$ 58,748	$ 59,750	$ 61,421	$ 59,558	$ 67,287	$ 84,332
Total debt	**8,885**	12,000	3,736	14,172	8,358	10,043	22,110	33,599	34,813	37,533	35,114
Shareholder's equity	**28,017**	35,468	38,891	36,148	37,740	29,776	16,141	7,483	7,328	13,087	34,698
Total debt to capitalization %	**24.1%**	25.3%	8.8%	28.2%	18.1%	25.2%	57.8%	81.8%	82.6%	74.1%	50.3%
Shareholder's equity per share (3)	$ **5.02**	$ 6.36	$ 6.46	$ 5.99	$ 5.80	$4.44	$ 2.43	$ 1.35	$ 1.34	$2.40	$ 6.31
Net operating assets per $ revenue (4)	$ **0.462**	$ 0.476	0.408	$ 0.531	$ 0.458	$ 0.381	$ 0.366	$ 0.435	0.565	$ 0.680	$ 0.785
Number of employees	**240**	277	293	280	306	326	358	352	355	467	585

(1) Shares outstanding and EPS prior to 1995 are based on primary earnings per share.
(2) Cost of Sales in fiscal 2002 includes restructuring write-downs of inventory of $1.1 million and fiscal 1993 includes inventory adjustment of $3.4 million.
(3) Based on shares outstanding at fiscal year end - diluted.
(4) Excluding cash and short-term debt.

MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion should be read in conjunction with the Selected Financial Data and the Consolidated Financial Statements and Notes thereto appearing elsewhere herein. Certain statements made in this report may constitute "forward-looking statements" within the meaning of the Private Securities Litigation Reform Act of 1995. These forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. These factors include, among others, changes in general economic and business conditions that affect market demand for machine tools and related computer control systems, software products, and replacement parts, changes in manufacturing markets, adverse currency movements, innovations by competitors, quality and delivery performance by our contract manufacturers and governmental actions and initiatives including import and export restrictions and tariffs.

RESULTS OF OPERATIONS

The following table presents, for the fiscal years indicated, selected items from the Consolidated Statements of Operations expressed as a percentage of worldwide sales and service fees and the year-to-year percentage changes in the dollar amounts of those items.

	Percentage of Revenues			Year-to-Year % Change Increase (Decrease)	
	2002	2001	2000	02 vs. 01	01 vs. 00
Sales and service fees	**100.0%**	100.0%	100.0%	**(23.6%)**	(4.1%)
Gross profit	**21.6%**	25.2%	26.4%	**(34.5%)**	(8.3%)
Selling, general and administrative expenses	**27.9%**	26.1%	24.5%	**(18.2%)**	2.1%
Restructuring expense and other expenses, net	**3.9%**	0.2%	0.3%	**1,826%**	(52.3%)
Operating loss	**(10.2%)**	(1.0%)	1.6%	**NA**	NA
License fee income, net	**0.2%**	0.8%	5.6%	**(77.4%)**	(86.5%)
Interest expense	**0.9%**	0.9%	0.9%	**(19.7%)**	(15.9%)
Net income (loss)	**(11.7%)**	(1.7%)	5.2%	**NA**	NA

FISCAL 2002 COMPARED WITH FISCAL 2001

Our net loss for the year ended October 31, 2002, which was more than five times greater than that reported for fiscal 2001, was due primarily to substantially lower sales and service fees as result of a continuing decline in machine tool orders in both the U.S. and Europe. The Association for Manufacturing Technology, the machine tool industry's trade association, reported that in 2002, the U.S. dollar value of orders for machine tools decreased 25%, and there was a corresponding deterioration in our European markets.

Also contributing to the loss for fiscal 2002 were restructuring and other special charges totaling $3.8 million, which consisted primarily of: (a) non-cash inventory write-downs of $1.1 million, which were recorded as an increase in the cost of sales, and the write-off of capitalized software development costs of $1.0 million, which was recorded as a restructuring expense, (b) severance costs of $1.1 million related to personnel reductions, and (c) a reserve of $1.1 million (of which $896,000 was recorded in the fourth fiscal quarter) for potential expenditures that might be required pursuant to a disputed claim regarding a terminated facility lease in the United Kingdom, which is more fully discussed below.

During fiscal 2002, we discontinued several under-performing product lines, and sold the related assets, to enable us to focus our resources and technology development on our core products. These products, known as milling machines and vertical machining centers, consist primarily of general purpose computerized machine tools for the metal cutting industry into which our proprietary UltiMax® software and computer control systems have been fully integrated. Discontinued and sold were the Delta™ series computer control and related Dynapath™ milling machine product line, and related parts and service activities, along with press brake product lines and all tooling products related to press brake applications. These discontinued product lines were marketed exclusively in the United States.

During fiscal 2002, we also eliminated 53 domestic employee positions, which we expect will result in annual cost reductions of approximately $3.8 million, of which $2.1 million was realized in fiscal 2002. The positions that were eliminated were those related to the discontinued product lines as well as some positions associated with our realigned and consolidated domestic sales and service operations.

We previously occupied a facility located in England under a lease that expired in April 2002. The lease required that, following expiration of the lease, we make certain repairs to the facility resulting from deterioration of the facility during the lease term. The scope and cost of the repairs alleged by the lessor to be required evolved throughout fiscal 2002 as investigations and negotiations proceeded, and currently approximate $2.0 million. We do not agree with the amount of the lessor's claim and are vigorously contesting that claim. Our liability could be reduced by statutory limitations or by a negotiated settlement. Based upon facts presently available to us and the current status of our negotiations with the lessor, our best estimate of our ultimate liability is $1.1 million, and we have established a reserve in that amount, of which $896,000 was recorded in the fourth quarter of fiscal 2002.

The following tables set forth net sales by geographic region and product category for the years ended October 31, 2002 and 2001 (in thousands):

NET SALES AND SERVICE FEES BY GEOGRAPHIC REGION

	October 31,			
	2002		2001	
Americas	**$ 24,148**	**34.3%**	$ 34,779	37.7%
Europe	**44,509**	**63.1%**	54,977	59.6%
Asia Pacific	**1,829**	**2.6%**	2,511	2.7%
Total	**$ 70,486**	**100%**	$ 92,267	100%

NET SALES AND SERVICE FEES BY PRODUCT CATEGORY

	October 31,			
	2002		2001	
Continuing Products and Services				
Computerized Machine Tools	**$ 52,056**	**73.9%**	$ 69,631	75.4%
Computer Control Systems and Software	**3,194**	**4.5%**	4,782	5.2%
Service Parts	**7,240**	**10.3%**	8,038	8.7%
Service Fees	**3,240**	**4.6%**	3,749	4.1%
Total	**$ 65,730**	**93.3%**	$ 86,200	93.4%
Discontinued Products and Services	**4,756**	**6.7%**	6,067	6.6%
Total	**$ 70,486**	**100.0%**	$ 92,267	100.0%

Our total sales and service fees were $70.5 million in fiscal 2002, a $21.8 million, or 24% decline compared to fiscal 2001. Sales of computerized machine tools (other than discontinued products) declined $17.6 million, or 25%, compared to fiscal 2001, reflecting the continuing global weakness in industrial equipment spending and reduced consumption of machine tools by many manufacturing companies, with the decline comprising $6.8 million, $10.1 million and $671,000 in the United States, Europe and Southeast Asia, respectively. Non-machine tool revenues also declined due to reduced activity levels in our market sectors, with the decline being most pronounced in the U.S.

The following table sets forth machine unit volume and average net selling price for computerized machine tools by continuing and discontinued products:

COMPUTERIZED MACHINE TOOLS - UNITS SOLD

	2002		2001	
Continuing Products	**697**	**88.9%**	942	92.4%
Discontinuing Products	**87**	**11.1%**	77	7.6%
Total	**784**	**100.0%**	1,019	100.0%

AVERAGE NET SELLING PRICE - PER UNIT (IN THOUSANDS)

	2002	2001
Continuing Products	**$ 74.7**	$ 73.9
Discontinuing Products	**$ 39.6**	$ 47.5
Total	**$ 70.8**	$ 71.9

The average net selling price per machine units of continuing products increased due to the effect of stronger European currencies when translating foreign sales for financial reporting purposes which more than offset the effect of increased discounting due to weak market conditions.

New order bookings for continuing products in fiscal 2002 were $62.2 million compared to $83.3 million in fiscal 2001, a 25% decline. New orders for computerized machine tools (other than discontinued products) declined 27% in U.S. dollars worldwide. The decline, which was experienced in all of our geographic markets, reflected a sharp decrease in orders for vertical machining centers, our primary product line. Backlog was $5.3 million at October 31, 2002, compared to $9.1 million at October 31, 2001.

Gross margin for fiscal 2002, exclusive of inventory write-downs recorded in cost of sales, declined to 23.2%, from 25.2% in fiscal 2001, due to the decline in our sales of vertical machining centers and our sale of approximately $4.8 million in discontinued products at discounted prices. Gross margin did improve in the last three quarters of fiscal 2002 compared to the immediately preceding quarter, although the improvement was due primarily to the cost reductions implemented over the preceding eighteen months. Selling, general and administrative expenses for fiscal 2002 of $19.7 million were $4.4 million, or 18%, lower than those for fiscal 2001, due to our cost reduction programs. We expect operating expenses to be lower in 2003 as we experience a full year's benefit of cost reductions initiated in fiscal 2002.

Non-operating items consisted of interest expense of $634,000 in fiscal 2002, which was $156,000, or 20% lower than in fiscal 2001, primarily due to reduced borrowings. License fee income and litigation settlement fees in fiscal 2002 and 2001 consisted of several licenses that were granted during the year. The licensing program that resulted in these fees was effectively completed in the first quarter of fiscal 2002 and we do not expect additional license fee income in the foreseeable future. Earnings from equity investments are from our two affiliates which are accounted for using the equity method. Other expense in fiscal 2002 was not significant and in fiscal 2001, consisted primarily of the costs of typhoon-related flood damage at our manufacturing facility in Taiwan.

The provision for income taxes is related to the earnings of two foreign subsidiaries.

FISCAL 2001 COMPARED WITH FISCAL 2000

Net loss for the fiscal year ended October 31, 2001 was $1.6 million, or $.28 per share, on a diluted basis, compared to net income of $5.0 million, or $.84 per share, reported for the preceding year. The change in our year-to-year results was due primarily to a significant decline in license fee income in fiscal 2001 from that reported in fiscal 2000, and to a lesser extent, to a decrease in sales.

The following tables set forth net sales by geographic region and product category for the years ended October 31, 2001 and 2000 (in thousands):

NET SALES AND SERVICE FEES BY GEOGRAPHIC REGION

	October 31, 2001		2000	
Americas	**$ 34,779**	**37.7%**	$ 44,607	46.4%
Europe	**54,977**	**59.6%**	46,129	47.9%
Asia Pacific	**2,511**	**2.7%**	5,468	5.7%
Total	**$ 92,267**	**100.0%**	$ 96,204	100.0%

NET SALES AND SERVICE FEES BY PRODUCT CATEGORY

	October 31, 2001		2000	
Computerized Machine Tools	**$ 73,286**	**79.4%**	$ 71,708	74.5%
Computer Control Systems and Software	**5,716**	**6.2%**	9,605	10.0%
Service Parts	**9,516**	**10.3%**	10,649	11.1%
Service Fees	**3,749**	**4.1%**	4,242	4.4%
Total	**$ 92,267**	**100.0%**	$ 96,204	100.0%

Sales and service fees were $92.3 million, for fiscal 2001, a decrease of 4.1% from the $96.2 million reported for fiscal 2000. The decline in sales was due in major part to the adverse effects of a stronger U.S. dollar when translating foreign sales for financial reporting purposes, and by a decrease in domestic sales. When measured at constant exchange rates, sales for fiscal 2001 would have been essentially the same as 2000. Domestic sales in fiscal 2001 declined by $9.8 million, or 22.0%, as a result of a slowing economy in most industrial sectors that began near the end of the first fiscal quarter, while sales in Europe increased $8.8 million in spite of the strong dollar. Sales in Southeast Asia declined by $3.0 million, or 54.1%, due to weak economic conditions in that area during fiscal 2001.

Net sales of computerized machine tools increased in fiscal 2001 by $4.8 million compared to the prior year when measured in constant dollars but was offset by a $3.5 million decline in sales of stand-alone control systems. Net sales of computerized machine tools in the U.S. declined 17% for the full fiscal year 2001. In contrast, sales of computerized machine tools in Europe, measured in constant dollars, increased 30% for the full year. Parts and service fee revenues declined by $1.6 million, or 10.9%. The decrease was exclusively in the United States and further reflects the weakening economic environment.

International sales, including export sales from the United States, approximated 64.3% of consolidated sales and service fees for fiscal 2001 compared to 57.5% for fiscal 2000.

New order bookings for fiscal 2001 were $89.4 million, compared to $100.7 million for the prior year period, a decrease of 11.3%. Orders were $28.1 million in the first quarter of fiscal 2001 but declined to $21.1 million, $19.2 and $21.0 million during the second, third and fourth quarter, respectively. The decline in orders from the first quarter was the result of weak economic conditions in most industrial market sectors in the U.S. along with a softening in the German economy. The decline in orders was most pronounced in the United States where computerized machine tool orders declined 30.4% in dollars. This was partially offset by a 19% increase in computerized machine tool orders in Europe, measured in constant dollars. We experienced a further decline in orders in the first quarter of fiscal 2002 reflecting the recessionary environment in our primary markets. Backlog was $9.1 million at October 31, 2001, compared to $10.2 million at October 31, 2000.

Gross profit margin declined in fiscal 2001 to 25.2% from 26.4% in fiscal 2000, due primarily to the unfavorable effects of the stronger U.S. dollar.

Operating expenses increased 2.1% to $24.0 million in fiscal 2001 from $23.5 million in fiscal 2000, due primarily to increased costs for enhanced product development activities associated with our next generation computer control technology. The increased operating expense for the full fiscal year combined with reduced sales and gross profit margins, resulted in an operating loss of $921,000 for fiscal 2001 as compared to an operating profit of $1.5 million in the prior year.

Restructuring expense of $143,000 in fiscal 2001 included a reversal of $328,000 primarily related to sub-letting space in a leased facility for which a reserve was provided as part of a previous restructuring plan. In addition, a restructuring charge of $471,000 was recorded for severance costs related to reductions in our domestic operations. In fiscal 2000, we recorded a restructuring charge of $300,000 for severance costs related to the termination of employees at our Farmington Hills facility in connection with the consolidation of this operation into our North American sales and service business.

License fee income and litigation settlement fees in fiscal 2001 consisted of several licenses that were granted during the year, while the substantial license fees reported in fiscal 2000 were primarily the result of the settlement of a long-standing patent infringement claim. The licensing program that resulted in the license and litigation settlement fees has effectively been completed and we do not expect significant license fees in fiscal 2002.

Other expense in fiscal 2001 was $215,000 compared to $395,000 in fiscal 2000 and consisted primarily of typhoon-related flood damage at our manufacturing facility in Taiwan of which our insurers have denied coverage. Fiscal 2000 other expense consisted primarily of realized and unrealized currency losses associated with accounts receivable denominated in foreign currencies, primarily those linked to the Euro, which for the most part, were not hedged during fiscal 2000. In fiscal 2001, these accounts receivable were fully hedged.

The provision for foreign income tax in both fiscal 2001 and fiscal 2000 consists mostly of income tax expense related to the earnings of our foreign subsidiaries.

FOREIGN CURRENCY RISK MANAGEMENT

We manage our foreign currency exposure through the use of foreign currency forward exchange contracts (see Quantitative and Qualitative Disclosures about Market Risks). We enter into foreign currency forward exchange contracts periodically to hedge certain forecasted inter-company sales and forecasted inter-company and third party purchases denominated in foreign currencies (primarily the Pound Sterling, Euro and New Taiwan Dollar). We also enter into foreign currency forward exchange contracts to protect against the effects of foreign currency fluctuations on receivables and payables denominated in foreign currencies. We do not speculate in the financial markets and, therefore, do not enter into these contracts for trading purposes. We also moderate our currency risk related to significant purchase commitments with certain foreign vendors through price adjustment agreements that provide for a sharing of, or otherwise limit, the risk of currency fluctuations on the costs of purchased products.

LIQUIDITY AND CAPITAL RESOURCES

At October 31, 2002, we had cash and cash equivalents of $4.4 million compared to $3.5 million at October 31, 2001. Cash generated from operations totaled $6.2 million in fiscal 2002, compared to cash used by operations of $3.5 million in fiscal 2001.

Working capital, excluding short-term debt, was $21.7 million at October 31, 2002, compared to $31.5 million at October 31, 2001. The decrease in working capital is attributable to a decrease in inventory of $7.7 million and a decrease in accounts receivable of $1.6 million. The decrease in inventory related primarily to a planned reduction in vertical machining center units along with the reduction of discontinued models that were sold off at discounted prices. Accounts receivable decreased due to the reduction in sales combined with improved collections.

Capital investments during the year consisted of normal expenditures for software development projects and purchases of equipment. In addition, during the fourth quarter of fiscal 2002, we purchased patented technology for $1.8 million that will be incorporated in our proprietary computer control system. Cash used for investments was reduced by a $1.0 million resulting from repayment of an investment as a result of the termination of certain agreements. We funded these expenditures with cash flow from operations except for the acquisition of the patented technology, which was financed by the seller. On October 24, 2002, we issued a secured promissory note for $1,350,000 to the seller of the patented technology as partial payment for the purchase. The note bears interest at 2.75% per annum and is due in four equal installments of $337,500 on March 31, 2003, June 30, 2003, July 31, 2003 and December 31, 2003.

As of October 31, 2002, we amended our domestic bank credit agreement, extending the maturity date to December 15, 2003, reducing the bank's commitment to $7.0 million and revising some of the financial covenants. We must maintain a tangible net worth, exclusive of Accumulated Other Comprehensive Income (as set forth in our consolidated balance sheet), of not less than $32.3 million at October 31, 2002, $30.0 million at January 31, 2003, April 30, 2003 and July 31, 2003 and $30.5 million at October 31, 2003. Our adjusted EBITDA, as defined, for the twelve consecutive months then ending cannot be less than negative $2.15 million on October 31, 2002, negative $1.75 million on January 31, 2003, negative $600,000 on April 30, 2003, positive $280,000 on July 31, 2003 and positive $1.8 million on October 31, 2003. Other financial covenants were extended unchanged to December 15, 2003. A facility fee of $50,000 previously payable March 31, 2003 has been reduced to $35,000, payable June 30, 2003, unless we have obtained a replacement financing arrangement by then. There were no borrowings outstanding under this facility at October 31, 2002 and outstanding letters of credit were $1.1 million.

On April 30, 2002, we obtained a $4.5 million first mortgage loan on our Indianapolis corporate headquarters. The loan bears interest at a rate of 7 3/8 % and matures in April 2009. We are required to make principal payments over the seven-year term of the loan, based on a twenty-year amortization schedule. The proceeds from the first mortgage loan were used to repay bank debt.

On January 8, 2002 we entered into a 3.0 million Euro credit facility with a European bank, which matures November 30, 2003. Interest on the facility is payable at 7.16% per annum or, at the Company's option, 1.75% above EURIBOR for fixed rate borrowings. Although the facility is uncollaterlized, the bank reserves the right to require collateral in the event of increased risk evaluation. Borrowings outstanding under this facility at October 31, 2002 were $2.5 million.

Total debt at October 31, 2002 was $8.9 million representing 24% of total capitalization, compared to $12.0 million, or 25% of total capitalization, at October 31, 2001. We were in compliance with all loan covenants and had unused credit availability of $6.5 million at October 31, 2002.

Based on our business plan and financial projections for fiscal 2003, we believe that cash flow from operations and borrowings available to us under our credit facilities will be sufficient to meet our anticipated cash requirements in fiscal 2003. Although we believe that the assumptions underlying our 2003 business plan are reasonable and achievable, there are risks related to further declines in market demand and reduced sales in the U.S. and Europe and adverse currency movements that could cause our actual results to differ from our business plan. We are also currently in discussions with lenders to replace our existing credit facility (expires December 2003) with a long-term credit facility in conjunction with assessing our liquidity needs for fiscal 2004 and beyond. While we believe we will be able to obtain a replacement facility under acceptable terms, no such assurance can be given.

CONTRACTUAL OBLIGATIONS AND COMMITMENTS

The following is a table of contractual obligations and commitments as of October 31, 2002 (all amounts in thousands):

	Total	Less than 1 Year	1 - 3 Years	4 - 5 Years	After 5 Years
Long-Term Debt	$ 8,885	$ 1,313	$ 3,437	$ 262	$ 3,873
Operating Leases	2,664	964	1,136	512	52
Letters of Credit	1,100	1,100	-	-	-
Total	$ 12,649	$ 3,377	$ 4,573	$ 774	$ 3,925

In addition to the contractual obligations and commitments disclosed above, we also have a variety of other contractual agreements related to the procurement of materials and services and other commitments. With respect to these agreements, we are not subject to any contracts which commit us to material non-cancelable commitments. While some of these contractual agreements are long-term supply agreements, we are not committed under these agreements to accept or pay for requirements which are not needed to meet production needs. We have no material minimum purchase commitments or "take-or-pay" type agreements or arrangements.

With respect to capital expenditures, we expect capital spending in fiscal 2003 to approximate $1.5 million.

NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board issued Statement No. 141, "Business Combinations" (SFAS 141) and Statement No. 142, "Goodwill and Other Intangible Assets" (SFAS 142). SFAS 141 requires that all business combinations initiated after June 30, 2001 be accounted for under the purchase method of accounting. Under SFAS 142, amortization of goodwill will cease and the goodwill carrying values will be tested periodically for impairment. We are required to adopt SFAS 142, effective November 1, 2002 for goodwill and intangible assets acquired prior to July 1, 2001. Goodwill and intangible assets acquired after June 30, 2001 were subject immediately to the goodwill non-amortization and intangible provisions of this statement. We do not expect that the adoption of this standard will have a material effect on the Consolidated Financial Statements.

In August 2001, the Financial Accounting Standards Board issued Statement No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (SFAS 144), which is effective for the fiscal year beginning November 1, 2002. SFAS 144 establishes a single model to account for impairment of assets to be held or disposed of, incorporating guidelines for accounting and disclosure of discontinued operations. We do not expect that the adoption of this standard will have a material effect on the Consolidated Financial Statements.

In July 2002, the Financial Accounting Standards Board issued Statement No. 146, "Accounting for Costs Associated with Exit or Disposal Activities". This Standard, which is effective for disposal activities initiated after December 31, 2002, addresses significant issues regarding the recognition, measurement and reporting of costs associated with exit and disposal activities. We will comply with the provisions of the Standard with respect to exit and disposal activities initiated after the effective date, but do not expect adoption to have any material impact on the Consolidated Financial Statements.

In November 2002, the Financial Accounting Standards Board ("FASB" or the "Board") issued FASB Interpretation No. 45 ("FIN 45"), "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, an interpretation of FASB Statements No. 5, 57 and 107 and Rescission of FASB Interpretation No. 34." FIN 45 clarifies the requirements of FASB Statement No. 5, Accounting for Contingencies, relating to the guarantor's accounting for, and disclosure of, the issuance of certain types of guarantees. The disclosure provisions of FIN 45 are effective for financial statements of interim or annual periods that end after December 15, 2002. However, the provisions for initial recognition and measurement are effective on a prospective basis for guarantees that are issued or modified after December 31, 2002, irrespective of a guarantor's year-end. We do not expect the impact of adopting the interpretation to have a material effect on the Consolidated Financial Statements.

CRITICAL ACCOUNTING POLICIES

Our accounting policies, including those described below, require management to make significant estimates and assumptions using information available at the time the estimates are made. Such estimates and assumptions significantly affect various reported amounts of assets, liabilities, revenues and expenses. If our future experience differs materially from these estimates and assumptions, our results of operations and financial condition could be affected.

Revenue Recognition - We recognize product revenue at the time of shipment because ownership and risk of loss passes to the customer at that time and payment terms are fixed. Our computerized machine tools are general-purpose computer controlled machine tools that are typically used in stand-alone operations. Transfer of ownership and risk of loss are not contingent upon contractual customer acceptance. Prior to shipment, we test each machine to ensure the machine's compliance with standard operating specifications as listed in our sales literature.

Depending upon geographic location, the machine installation at the end user may be completed by a distributor, independent contractor or Hurco service technician. In most instances where a machine is sold through a distributor, we have no installation involvement. If sales are direct or through sales agents, we will typically complete the machine installation. The machine installation consists of the reassembly of certain parts that were removed for shipping and the re-testing of the machine to ensure that it is performing with the standard specifications. We consider the machine installation process inconsequential and perfunctory.

Service fees from maintenance contracts are deferred and recognized in earnings on a pro rata basis over the term of the contract. Sales related to software products are recognized when shipped in conformity with American Institute of Certified Public Accountants' Statement of Position 97-2 Software Revenue Recognition.

Inventories – We must determine at each balance sheet date how much, if any, of our inventory may ultimately prove to be unsaleable or unsaleable at its carrying cost. Reserves are established to effectively adjust any such inventory to net realizable value. To determine the appropriate level of valuation reserves, we evaluate current stock levels in relation to historical and expected patterns of demand for all of our products. Management evaluates the need for changes to valuation reserves based on market conditions, competitive offerings and other factors on a regular basis.

Deferred Tax Asset Valuation – As of October 31, 2002, we have deferred tax assets of $5.3 million for which we have recorded a valuation allowance of 100% resulting in zero net deferred tax asset on our balance sheet. These future tax benefits relate primarily to net operating loss carryforwards in the United States and certain foreign jurisdictions as well as Federal business tax credits carried forward in the United States. Some of these carryforward benefits expire at certain dates and utilization of certain others is limited to specific amounts each year. Realization of those benefits is entirely dependent upon generating sufficient future taxable earnings in the specific tax jurisdictions before they expire. Due to the recent losses in the United States and the applicable foreign tax jurisdictions, there is substantial uncertainty whether these tax benefits can be utilized before they expire. Therefore, we have established a full valuation allowance. The need for this allowance is reviewed periodically, and if reduced in future periods, the associated tax benefits will be recorded in future operations as a reduction of income tax expense.

Capitalized Software Development Costs – Costs incurred to develop new computer software products and significant enhancements to software features of existing products are capitalized as required by SFAS No. 86, "Accounting for the Costs of Computer Software to be Sold, Leased, or Otherwise Marketed" and amortized over the estimated product life of the related software. The determination as to when in the product development cycle technological feasibility has been established, and the expected product life, require judgments and estimates by management and can be affected by technological developments, innovations by competitors and changes in market conditions affecting demand. We capitalized $534,000 in fiscal 2002, $665,000 in fiscal 2001 and $706,000 in fiscal 2000 related to software development projects. Also in fiscal 2002 we wrote off $1.0 million of previously capitalized costs related to a discontinued product line. At October 31, 2002 we have an asset of $1.6 million for capitalized software development projects, a significant portion of which relates to projects currently in process and subject to development risk and market acceptance. We periodically review the carrying values of these assets and make judgments as to ultimate realization considering the above mentioned risk factors.

Derivative Financial Instruments – Critical aspects of our accounting policy for derivative financial instruments include conditions which require that critical terms of a hedging instrument are essentially the same as a hedged forecasted transaction. Another important element of the policy demands that formal documentation be maintained as required by the Statement of Financial Accounting Standards (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities." Failure to comply with these conditions would result in a requirement to recognize changes in market value of hedge instruments in earnings. We routinely monitor significant estimates, assumptions, and judgments associated with derivative instruments, and compliance with formal documentation requirements.

Stock Compensation – We apply the provisions of APB Opinion No. 25, "Accounting for Stock Issued to Employees," in accounting for stock-based compensation; therefore, no compensation expense has been recognized for stock options as options are granted at fair market value. Statement of Financial Accounting Standards No. 123, "Accounting for Stock-Based Compensation" provides an alternative method of accounting for stock options based on an option-pricing model, such as Black-Scholes. We have adopted the disclosure requirements of SFAS No. 123. Information and assumptions regarding compensation expense under the alternative method is provided in Note 8 to the Consolidated Financial Statements.

QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISKS

Interest Rate Risk

Our earnings are affected by changes in interest expense on our outstanding debt, all of which is subject to floating rates, either LIBOR or Prime. If market interest rates on our outstanding variable rate borrowings were to have increased by one percentage point (1%) (or 100 basis points) over the actual rates paid in that year, interest expense would have increased by $90,000 in fiscal 2002 and $110,000 in fiscal 2001. This sensitivity analysis assumes no changes in other factors affecting our financial statements that might result from changes in the economic environment which impact interest rates. Refer to Note 4 of the Consolidated Financial Statements for a discussion of the interest rates related to our current credit facilities. At October 31, 2002, outstanding borrowings under our bank credit facilities were $2.5 million and our total indebtedness was $8.9 million.

Foreign Currency Exchange Risk

In fiscal 2002, approximately 68% of our sales and service fees, including export sales, were derived from foreign markets. All of our computerized machine tools and computer control systems, as well as certain proprietary service parts, are sourced by our U.S.-based engineering and manufacturing division and re-invoiced to our foreign sales and service subsidiaries, primarily in their functional currencies.

Our products are sourced from foreign suppliers or built to our specifications by either our wholly-owned subsidiary in Taiwan, or overseas contract manufacturers. These purchases are predominantly in foreign currencies and in some cases our arrangements with these suppliers include foreign currency risk sharing agreements, which reduce (but do not eliminate) the effects of currency fluctuations on product costs. The predominant portion of our exchange rate risk associated with product purchases relates to the New Taiwan Dollar.

We enter into foreign currency forward exchange contracts from time to time to hedge the cash flow risk related to forecast inter-company sales, and forecast inter-company and third party purchases denominated in, or based on, foreign currencies. We also enter into foreign currency forward exchange contracts to protect against the effects of foreign currency fluctuations on receivables and payables denominated in foreign currencies. We do not speculate in the financial markets and, therefore, do not enter into these contracts for trading purposes.

Forward contracts for the sale or purchase of foreign currencies as of October 31, 2002 which are designated as cash flow hedges under SFAS No. 133 were as follows:

Forward Contracts	Notional Amount in Foreign Currency	Weighted Avg. Forward Rate	Contract Amount at Forward Rates in U.S. Dollars: Contract Date	Contract Amount at Forward Rates in U.S. Dollars: October 31, 2002	Maturity Dates
Sale Contracts:					
Euro	5,700,000	$ .9830	$ 5,603,100	$ 5,621,043	Nov 2002-Mar 2003
Sterling	600,000	$ 1.5421	$ 925,260	$ 935,697	Nov 2002-Feb 2003
Purchase Contracts:					
New Taiwan Dollar	175,000,000	33.95*	$ 5,154,639	$ 5,058,159	Nov 2002-Apr 2003

Forward contracts for the sale of foreign currencies as of October 31, 2002 which were entered into to protect against the effects of foreign currency fluctuations on receivables and payables denominated in foreign currencies were as follows:

Forward Contracts	Notional Amount in Foreign Currency	Weighted Avg. Forward Rate	Contract Amount at Forward Rates in U.S. Dollars: Contract Date	Contract Amount at Forward Rates in U.S. Dollars: October 31, 2002	Maturity Dates
Sale Contracts:					
Euro	1,938,989	$ .9805	$ 1,901,179	$ 1,913,155	Nov 2002-Jan 2003
Singapore Dollar	1,525,337	$ .5644	$ 860,900	$ 862,494	Nov 2002-Jan 2003
Sterling	742,830	$ 1.5491	$ 1,150,718	$ 1,158,640	Nov 2002-Jan 2003
Purchase Contracts:					
New Taiwan Dollar	50,000,000	34.63*	$ 1,443,835	$ 1,442,658	Nov 2002

* NT Dollars per U.S. dollars

FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

Report of Independent Accountants

To the Shareholders and
Board of Directors of
Hurco Companies, Inc.:

In our opinion, the consolidated balance sheet and the related consolidated statement of operations, shareholders' equity and cash flows for the year then ended present fairly, in all material respects, the financial position of Hurco Companies, Inc. and its subsidiaries at October 31, 2002, and the results of their operations and their cash flows for the year then ended in conformity with accounting principles generally accepted in the United States of America. These financial statements are the responsibility of the Company's management; our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit of these statements in accordance with auditing standards generally accepted in the United States of America, which require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audit provides a reasonable basis for our opinion. The financial statements of Hurco Companies, Inc. as of October 31, 2001, and for each of the two years in the period ended October 31, 2001, were audited by other independent accountants who have ceased operations. Those independent accountants expressed an unqualified opinion on those financial statements in their report dated January 15, 2002.

PRICEWATERHOUSECOOPERS LLP
Indianapolis, Indiana,
January 15, 2003.

REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

The following report is a copy of a report previously issued by Arthur Andersen LLP and has not been reissued by Arthur Andersen LLP.

To the Shareholders and
Board of Directors of
Hurco Companies, Inc.:

We have audited the accompanying consolidated balance sheets of Hurco Companies, Inc. (an Indiana corporation) and subsidiaries as of October 31, 2001 and 2000*, and the related consolidated statements of operations, changes in shareholders' equity and cash flows for each of the three years in the period ended October 31, 2001. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with auditing standards generally accepted in the United States. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the financial statements referred to above present fairly, in all material respects, the consolidated financial position of Hurco Companies, Inc. and subsidiaries as of October 31, 2001 and 2000*, and the consolidated results of their operations and their cash flows for each of the three years in the period ended October 31, 2001, in conformity with accounting principles generally accepted in the United States.

ARTHUR ANDERSEN LLP
Indianapolis, Indiana,
January 15, 2002.

* The 2000 consolidated balance sheet is not required to be presented in the 2002 annual report.

HURCO COMPANIES, INC.
CONSOLIDATED STATEMENTS OF OPERATIONS

	Year Ended October 31,		
	2002	2001	2000
Sales and service fees	**$ 70,486**	$ 92,267	$ 96,204
Cost of sales and service	**54,157**	69,005	70,827
Cost of sales - restructuring	**1,083**	--	--
Gross profit	**15,246**	23,262	25,377
Selling, general and administrative expenses	**19,658**	24,040	23,538
Restructuring expense and other expense, net (Note 15)	**2,755**	143	300
Operating income (loss)	**(7,167)**	(921)	1,539
Interest expense	**634**	790	939
License fee income and litigation settlement fees, net (Note 10 and 12)	**163**	723	5,365
Earnings from equity investments	**25**	383	36
Other expense, net	**61**	215	395
Income (loss) before income taxes	**(7,674)**	(820)	5,606
Provision for income taxes (Note 6)	**589**	777	571
Net income (loss)	**$ (8,263)**	$ (1,597)	$ 5,035
Earnings (loss) per common share - basic	**$ (1.48)**	$ (.28)	$ .85
Weighted average common shares outstanding - basic	**5,583**	5,670	5,952
Earnings (loss) per common share - diluted	**$ (1.48)**	$ (.28)	$ .84
Weighted average common shares outstanding - diluted	**5,583**	5,670	6,020

(Dollars in thousands, except per share amounts)

The accompanying notes are an integral part of the Consolidated Financial Statements.

HURCO COMPANIES, INC.
CONSOLIDATED BALANCE SHEETS

	As of October 31,	
	2002	2001
Current assets:		
Cash and cash equivalents	$ 4,358	$ 3,523
Accounts receivable, less allowance for doubtful accounts of $689 in 2002 and $907 in 2001	13,425	14,436
Inventories	22,548	30,319
Other	1,204	1,232
Total current assets	41,535	49,510
Property and equipment:		
Land	761	761
Building	7,203	7,187
Machinery and equipment	10,144	11,410
Leasehold improvements	396	1,059
	18,504	20,417
Less accumulated depreciation and amortization	(9,696)	(11,653)
	8,808	8,764
Software development costs, less accumulated amortization	1,604	3,066
Investments and other assets	5,205	4,877
	$ 57,152	$ 66,217

LIABILITIES AND SHAREHOLDERS' EQUITY

	2002	2001
Current liabilities:		
Accounts payable	$ 8,752	$ 7,601
Accounts payable-related parties	1,104	2,335
Accrued expenses and other	9,430	7,289
Accrued warranty expenses	586	792
Current portion of long-term debt	1,313	200
Total current liabilities	21,185	18,217
Non-current liabilities:		
Long-term debt	7,572	11,800
Deferred credits and other	378	732
	7,950	12,532
Commitments and contingencies (Notes 10 and 11)		
Shareholders' equity:		
Preferred stock: no par value per share; 1,000,000 shares authorized; no shares issued	--	--
Common stock: no par value; $.10 stated value per share; 12,500,000 shares authorized; 5,583,158 and 5,580,658 shares issued and outstanding in 2002 and 2001, respectively	558	558
Additional paid-in capital	44,717	44,714
Accumulated deficit	(10,173)	(1,910)
Accumulated other comprehensive income (loss)	(7,085)	(7,894)
Total shareholders' equity	28,017	35,468
	$ 57,152	$ 66,217

(Dollars in thousands, except per share amounts)

The accompanying notes are an integral part of the Consolidated Financial Statements.

HURCO COMPANIES, INC.
CONSOLIDATED STATEMENTS OF CASH FLOWS

	Year Ended October 31,		
	2002	2001	2000
Cash flows from operating activities:			
Net income (loss)	$ (8,263)	$ (1,597)	$ 5,035
Adjustments to reconcile net income (loss) to net cash provided by (used for) operating activities:			
Provision for doubtful accounts	133	547	185
Equity in income of affiliates	(25)	(383)	(36)
Depreciation and amortization	1,929	2,196	2,519
Restructuring charge (credit)	2,250	(195)	300
Change in assets/liabilities			
(Increase) decrease in accounts receivable	1,615	3,113	(2,286)
(Increase) decrease in inventories	7,720	(4,018)	2,717
Increase (decrease) in accounts payable	(141)	(3,521)	2,917
Increase (decrease) in accrued expenses	1,228	558	1,023
Other	(245)	(182)	476
Net cash provided by (used for) operating activities	6,201	(3,482)	12,850
Cash flows from investing activities:			
Proceeds from sale of property and equipment	154	38	36
Purchase of property and equipment	(1,184)	(1,253)	(1,193)
Software development costs	(534)	(665)	(706)
Purchase of intellectual property	(500)	--	--
Other proceeds (investments)	1,037	(829)	(138)
Net cash (used for) investing activities	(1,027)	(2,709)	(2,001)
Cash flows from financing activities:			
Advances on bank credit facilities	28,369	44,300	28,500
Repayments of bank credit facilities	(37,251)	(34,050)	(37,150)
Repayments of term debt	(200)	(1,986)	(1,786)
Proceeds from first mortgage	4,500	--	--
Repayment of first mortgage	(39)	--	--
Proceeds from exercise of common stock options	4	35	8
Purchase of common stock	--	(1,706)	--
Net cash provided by (used for) financing activities	(4,617)	6,593	(10,428)
Effect of exchange rate changes on cash	278	(263)	(532)
Net increase (decrease) in cash	835	139	(111)
Cash and cash equivalents at beginning of year	3,523	3,384	3,495
Cash and cash equivalents at end of year	$ 4,358	$ 3,523	$ 3,384
Supplemental disclosures:			
Cash paid for:			
Interest	$ 519	$ 682	$ 834
Income taxes	$ 442	$ 501	$ 739

Supplemental schedule of noncash investing and financial activities:

We purchased patented technology for $1.85 million. In connection therewith we issued a secured promissory note for $1.35 million.

Fair value of asset acquired	$ 1,850
Cash paid	500
Promissory note issued	$ 1,350

The accompanying notes are an integral part of the Consolidated Financial Statements.

(Dollars in thousands)

HURCO COMPANIES, INC.
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

	Common Stock					
	Shares Issued & Outstanding	Amount	Additional Paid-In Capital	Accumulated Deficit	Accumulated Other Comprehensive Income (loss)	Total
Balances, October 31, 1999	**5,951,859**	**$ 595**	**$ 46,340**	**$ (5,348)**	**$ (5,439)**	**$ 36,148**
Net income	--	--	--	5,035	--	5,035
Translation of foreign currency financial statements	--	--	--	--	(2,300)	(2,300)
Comprehensive Income						2,735
Exercise of common stock options	3,500	1	7	--	--	8
Balances, October 31, 2000	**5,955,359**	**$ 596**	**$ 46,347**	**$ (313)**	**$ (7,739)**	**$ 38,891**
Net loss	--	--	--	(1,597)	--	(1,597)
Translation of foreign currency financial statements	--	--	--	--	315	315
Unrealized loss of derivative instruments	--	--	--	--	(470)	(470)
Comprehensive loss						(1,752)
Exercise of common stock options	16,400	1	34	--	--	35
Repurchase of common stock	(391,101)	(39)	(1,667)	--	--	(1,706)
Balances, October 31, 2001	**5,580,658**	**$ 558**	**$ 44,714**	**$ (1,910)**	**$ (7,894)**	**$ 35,468**
Net income loss	--	--	--	(8,263)	--	(8,263)
Translation of foreign currency financial statements	--	--	--	--	981	981
Unrealized loss of derivative instruments	--	--	--	--	(172)	(172)
Comprehensive loss						(7,454)
Exercise of common stock options	2,500	--	3	--	--	3
Balances, October 31, 2002	**5,583,158**	**$ 558**	**$ 44,717**	**$ (10,173)**	**$ (7,085)**	**$ 28,017**

(Dollars in thousands)

The accompanying notes are an integral part of the Consolidated Financial Statements.

HURCO COMPANIES, INC.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

1. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Consolidation. The consolidated financial statements include the accounts of Hurco Companies, Inc. (an Indiana corporation) and our wholly owned and controlled subsidiaries. We have a 35% and 24% ownership interest in two affiliates accounted for using the equity method. Our combined investments are approximately $1.6 million and are included in Other Assets on the accompanying Consolidated Balance Sheets. Intercompany accounts and transactions have been eliminated.

Statements of Cash Flows. We consider all highly liquid investments purchased with a maturity of three months or less to be cash equivalents. Cash flows from hedges are classified consistent with the items being hedged.

Translation of Foreign Currencies. All balance sheet accounts of non-U.S. subsidiaries are translated at the exchange rate as of the end of the year. Income and expenses are translated at the average exchange rates during the year. Cumulative foreign currency translation adjustments of $6.4 million are included in Accumulated Other Comprehensive Income in shareholders' equity. Foreign currency transaction gains and losses are recorded as income or expense as incurred.

Hedging. On November 1, 2001, we adopted Statement of Financial Accounting Standard (SFAS) No. 133, "Accounting for Derivative Instruments and Hedging Activities." In accordance with the provisions of SFAS No. 133, we recorded a transition adjustment upon the adoption of the standard to recognize the difference between the fair value of the derivative instruments recorded on the balance sheet and the previous carrying amount of those derivatives. The effect of this transition adjustment was insignificant and is reflected in the Other Income (Expense) in the Condensed Consolidated Statement of Operations. We also recorded a transition adjustment of approximately $129,000 in Accumulated Other Comprehensive Income to recognize previously deferred net losses on derivatives designated as cash flow hedges.

We enter into foreign currency forward exchange contracts periodically to hedge certain forecasted inter-company sales and forecasted inter-company and third party purchases denominated in foreign currencies (primarily the Pound Sterling, Euro and New Taiwan Dollar). The purpose of these instruments is to mitigate the risk that the U.S. Dollar net cash inflows and outflows resulting from sales and purchases denominated in foreign currencies will be adversely affected by changes in exchange rates. These forward contracts have been designated as cash flow hedge instruments, and are recorded in the Consolidated Balance Sheet at fair value in Other Current Assets and Accrued Liabilities and Other. Gains and losses resulting from changes in the fair value of these hedge contracts are deferred in Accumulated Other Comprehensive Income and recognized as an adjustment to the related sale or purchase transaction in the period that the transaction occurs. Net losses on cash flow hedge contracts which we reclassified from Other Comprehensive Income to Cost of Sales in the fiscal years ended October 31, 2002 and 2001 were $617,000, and $261,000, respectively.

At October 31, 2002 we had $645,000 of realized and unrealized losses related to cash flow hedges deferred in Other Comprehensive Income, which we expect to recognize in Cost of Sales within the next twelve months. Cash flow hedge contracts mature at various dates through April 2003.

We also enter into foreign currency forward exchange contracts to protect against the effects of foreign currency fluctuations on receivables and payables denominated in foreign currencies. These derivative instruments are not designated as hedges under SFAS 133 and as a result, changes in fair value are reported currently as Other Income (Expense) in the Consolidated Statement of Operations consistent with the transaction gain or (loss) on the related foreign denominated receivable or payable. Such net transaction gains and (losses) were $(209,000), ($50,000) and ($638,000) for the years ended October 31, 2002, 2001, and 2000, respectively.

Inventories. Inventories are stated at the lower of cost or market, with cost determined using the first-in, first-out method.

Property and Equipment. Property and equipment are carried at cost. Depreciation and amortization of assets are provided primarily under the straight-line method over the shorter of the estimated useful lives or the lease terms as follows:

	Number of Years
Building	40
Machines	10
Shop and office equipment	5
Leasehold improvements	5

Total depreciation expense for the year ended October 31, 2002, was $1.1 million. Any impairment would be recognized based on an assessment of future operations (including cash flows) to insure that assets are appropriately valued.

Revenue Recognition. We recognize product revenue at the time of shipment because ownership and risk of loss passes to the customer at that time and payment terms are fixed. Our computerized machine tools are general-purpose computer controlled machine tools that are typically used in stand-alone operations. Transfer of ownership and risk of loss are not contingent upon contractual customer acceptance. Prior to shipment, we test each machine to ensure the machine's compliance with standard operating specifications as listed in our sales literature.

Depending upon geographic location, the machine installation at the end user may be completed by a distributor, independent contractor or Hurco service technician. In most instances where a machine is sold through a distributor, we have no installation involvement. If sales are direct or through sales agents, we will typically complete the machine installation. The machine installation consists of the reassembly of certain parts that were removed for shipping and the re-testing of the machine to ensure that it is performing with the standard specifications. We consider the machine installation process inconsequential and perfunctory.

Service fees from maintenance contracts are deferred and recognized in earnings on a pro rata basis over the term of the agreement. Sales related to software products are recognized when shipped in conformity with American Institute of Certified Public Accountants' Statement of Position 97-2 Software Revenue Recognition.

License Fee Income, Net. From time to time, our wholly owned subsidiary, IMS Technology, Inc. (IMS) enters into agreements for the licensing of its interactive computer control patents. License fees received or receivable under a fully paid-up license, for which there are no future performance requirements or contingencies, and litigation settlement fees are recognized in income, net of legal fees and expenses, if any, at the time the related agreement is executed. License fees received in periodic installments that are contingent upon the continuing validity of a licensed patent were recognized in income, net of legal fees and expenses, if any, over the life of the licensed patent, which expired in October 2001. As a result, we have no deferred license fee income at October 31, 2002 and do not expect any significant license fee income in the foreseeable future.

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

Research and Development Costs. The costs associated with research and development programs for new products and significant product improvements are expensed as incurred and are included in Selling, General and Administrative expenses. Research and development expenses totaled $2.4 million, $3.5 million and $3.2 million in fiscal 2002, 2001, and 2000, respectively.

Costs incurred to develop computer software products and significant enhancements to software features of existing products to be sold or otherwise marketed are capitalized, after technological feasibility is established. Software development costs are amortized to Cost of Sales on a straight-line basis over the estimated product life of the related software, which ranges from three to five years. We capitalized $534,000 in 2002, $665,000 in 2001 and $706,000 in 2000 related to software development projects. Amortization expense was $719,000, $925,000, and $1.3 million for the years ended October 31, 2002, 2001, and 2000, respectively. Any impairment could be recognized based on an assessment of future operations (including cash flows) to insure that assets are appropriately valued.

Earnings Per Share. Basic and diluted earnings per common share are based on the weighted average number of our shares of common stock outstanding. Diluted earnings per common share give effect to outstanding stock options using the treasury method. The impact of 12,000 potentially issuable shares for the year ended October 31, 2002 was excluded from the computation of diluted earnings per share because their effect would be anti-dilutive.

Income Taxes. We record income taxes under SFAS 109 "Accounting for Income Taxes". SFAS 109 utilizes the liability method for computing deferred income taxes and requires that the benefit of certain loss carryforwards be recorded as an asset and that a valuation allowance be established against the asset to the extent it is "more likely than not" that the benefit will not be realized.

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

2. BUSINESS OPERATIONS

Nature of Business. We design and produce computer control systems and software and computerized machine tools for sale through our own distribution system to the worldwide machine tool industry.

The end market for our products consists primarily of precision tool, die and mold manufacturers, independent job shops and specialized short-run production applications within large manufacturing operations. Industries served include: aerospace, defense, medical equipment, energy, transportation and computer industries. Our products are sold through independent agents and distributors in countries throughout North America, Europe and Asia. We also maintain direct sales operations in the United States, England, France, Germany, Italy and Singapore.

Credit Risk. We sell products to customers located throughout the world. We perform ongoing credit evaluations of customers and generally do not require collateral. Allowances are maintained for potential credit losses. Concentration of credit risk with respect to trade accounts receivable is limited due to the large number of customers and their dispersion across many geographic areas. Although a significant amount of trade receivables are with distributors primarily located in the United States, no single distributor or region represents a significant concentration of credit risk.

Manufacturing Risk. We contract with manufacturing contractors located in Taiwan for the manufacture and assembly of computerized machine tool systems, based on our designs and/or specifications. Any interruption from these sources would restrict the availability of our computerized machine tool systems and would affect operating results adversely.

3. INVENTORIES

Inventories as of October 31, 2002 and 2001 are summarized below (in thousands):

	2002	2001
Purchased parts and sub-assemblies	$ 6,677	$ 7,853
Work-in-process	2,251	1,256
Finished goods	13,620	21,210
	$ 22,548	$ 30,319

4. DEBT AGREEMENTS

Long-term debt as of October 31, 2002 and 2001, consisted of (in thousands):

	2002	2001
Domestic bank revolving credit facility	$ --	$ 11,200
European bank credit facility	2,475	--
First Mortgage	4,460	--
Installment Promissory Note	1,350	--
Economic Development Revenue Bonds, Series 1990	600	800
	8,885	12,000
Less current portion	1,313	200
	$ 7,572	$ 11,800

As of October 31, 2002, long-term debt was payable as follows (in thousands):

Fiscal 2003	$ 1,313
Fiscal 2004	3,120
Fiscal 2005	317
Fiscal 2006	126
Fiscal 2007	136
Thereafter	3,873
	$ 8,885

Domestic Bank Credit Facility. As of October 31, 2002 and 2001, we had $1.1 million and $2.1 million, respectively, of outstanding letters of credit issued to non-U.S. suppliers for inventory purchase commitments. As of October 31, 2002, we had unutilized credit facilities of $6.5 million available for either direct borrowings or commercial letters of credit.

Interest on the bank credit facility was payable at rates ranging from 4.28% to 5.25% at October 31, 2002 and from 3.5% to 5.5% at October 31, 2001.

As of October 31, 2002, our domestic bank credit agreement was amended, extending the maturity date to December 15, 2003 and reducing the bank's commitment to $7.0 million. Interest on all outstanding borrowings is payable at Libor, plus an applicable Eurodollar rate margin, or at our option, prime rate plus a specified margin, as follows:

	Libor margin	Prime margin
November 1, 2002 – June 30, 2003	3.5%	1.5%
June 30, 2003 – December 15, 2003	4.0%	2.0%

Our domestic credit agreement requires that we maintain a tangible net worth, exclusive of Accumulated Other Comprehensive Income (as set forth in our consolidated balance sheet), of not less than $32.3 million at October 31, 2002, $30.0 million at January 31, 2003, April 30, 2003 and July 31, 2003 and $30.5 million at October 31, 2003. Our adjusted EBITDA, as defined, for the twelve consecutive months then ending cannot be less than negative $2.15 million on October 31, 2002, negative $1.75 million on January 31, 2003, negative $600,000 on April 30, 2003, positive $280,000 on July 31, 2003 and positive $1.8 million on October 31, 2003. Other financial covenants were extended unchanged to December 15, 2003. A facility fee of $50,000 previously payable March 31, 2003 has been reduced to $35,000, payable June 30, 2003, unless we have obtained a replacement financing arrangement by then. The credit agreement provides the lender with a security interest in substantially all domestic assets and 67% of the common stock of our U.S. holding companies, which own our foreign subsidiaries. At October 31, 2002, our ability to repurchase shares of our common stock and pay cash dividends were restricted under the bank credit agreement. We were in compliance with all loan covenants at October 31, 2002. We are currently in discussion with other lenders for a long-term domestic credit facility, and while we believe that we will be able to obtain a replacement facility in fiscal 2003 under acceptable terms, no such assurance can be given.

Promissory Note. On October 24, 2002, we issued a secured promissory note for $1,350,000 to the seller of patented technology that we purchased. The note bears interest at 2.75% per annum and is due in four equal installments of $337,500 on March 31, 2003, June 30, 2003, July 31, 2003 and December 31, 2003.

First Mortgage. On April 30, 2002, we obtained a $4.5 million first mortgage loan on our Indianapolis corporate headquarters. The loan bears interest at a rate of 7 3/8 % and matures in April 2009. We are required to make principal payments over the seven-year term of the loan, based on a twenty-year amortization schedule. The proceeds from the first mortgage loan, together with other available cash, were used to repay bank debt.

European Bank Credit Facility. On January 8, 2002 we entered into a 3.0 million Euro credit facility with a European bank, which currently matures November 30, 2003. Interest on the facility is payable at 7.16% per annum or, at the Company's option, 1.75% above EURIBOR for fixed rate borrowings. Although the facility is uncollateralized, the bank reserves the right to require collateral in the event of increased risk evaluation. Borrowings outstanding under this facility at October 31, 2002 were $2.5 million.

Economic Development Revenue Bonds. The Economic Development Revenue Bonds are payable in three remaining equal annual installments due on September 1, 2003 thru 2005 and are secured by a letter of credit issued by our domestic bank. Interest rates on the bonds adjust weekly and, as of October 31, 2002 and 2001, interest was accruing at a rate of 2.10% and 2.40%, respectively.

5. FINANCIAL INSTRUMENTS

The carrying amounts for trade receivables and payables approximate their fair values. At October 31, 2002, the carrying amounts and fair values of our financial instruments, which include bank revolving credit facilities, senior notes and Economic Development Revenue Bonds, are not materially different. The fair value of long-term debt, including the current portion, is estimated based on quoted market prices for similar issues or on current rates offered to us for debt of the similar terms and maturities.

We also have financial instruments in the form of foreign currency forward exchange contracts as described in Note 1 to the Consolidated Financial Statements. The U.S. dollar equivalent notional amount of these contracts was $17.0 million at October 31, 2002. The net fair value of these derivative instruments recorded in accrued expenses at October 31, 2002 was $147,000. Current market prices were used to estimate the fair value of the foreign currency forward exchange contracts.

The future value of the foreign currency forward exchange contracts and the related currency positions are subject to offsetting market risk resulting from foreign currency exchange rate volatility. The counterparties to these contracts are substantial and creditworthy financial institutions. We do not consider either the risk of counterparty non-performance or the economic consequences of counterparty non-performance as material risks.

6. INCOME TAXES

Deferred income taxes reflect the effect of temporary differences between the tax basis of assets and liabilities and the reported amounts of those assets and liabilities for financial reporting purposes. Deferred income taxes also reflect the value of net operating losses and an offsetting valuation allowance. Our total deferred tax assets and corresponding valuation allowance at October 31, 2002 and 2001, consisted of the following (in thousands):

	October 31, 2002	October 31, 2001
Tax effects of future tax deductible items related to:		
Accrued inventory reserves	**$ 623**	$ 758
Accrued warranty expenses	**121**	211
Deferred compensation	**213**	359
Other accrued expenses	**521**	669
Total deferred tax assets	**1,478**	1,997
Tax effects of future taxable differences related to:		
Accelerated tax deduction and other tax over book deductions related to property, equipment and software	**(968)**	(1,422)
Other	**(698)**	(669)
Total deferred tax liabilities	**(1,666)**	(2,091)
Net tax effects of temporary differences	**(188)**	(94)
Tax effects of carryforward benefits:		
U.S. federal net operating loss carryforwards, expiring 2022	**2,745**	1,182
Foreign tax benefit carryforwards, expiring 2003-2007	**326**	296
Foreign tax benefit carryforwards, with no expiration	**1,435**	852
U.S. federal general business tax credits,expiring 2004-2012	**1,017**	828
U.S. Alternative Minimum Tax Credit with no expiration	--	426
Tax effects of carryforwards	**5,523**	3,584
Tax effects of temporary differences and carryforwards, net	**5,335**	3,490
Less valuation allowance	**(5,335)**	(3,064)
Net deferred tax asset	**$ --**	$ 426

Except as indicated above, our carryforwards expire at specific future dates and utilization of certain carryforwards is limited to specific amounts each year and further limitations may be imposed if an "ownership change" would occur. Realization is entirely dependent upon generating sufficient future earnings in specific tax jurisdictions prior to the expiration of the loss carryforwards.

Due to the uncertain nature of their ultimate realization based upon past performance and expiration dates, we have established a full valuation allowance against carryforward benefits. Alternative minimum tax credits may be carried forward indefinitely and as a result, are not provided with a valuation allowance. While the need for this valuation allowance is subject to periodic review, if the allowance is reduced, the tax benefits of the carryforwards will be recorded in future operations as a reduction of our income tax expense.

Income (loss) before income taxes (in thousands):	Year Ended October 31, 2002	2001	2000
Domestic	**$ (7,238)**	$ (2,980)	$ 5,459
Foreign	**(436)**	2,160	147
	$ (7,674)	$ (820)	$ 5,606

Differences between the effective tax rate and U.S. federal income tax rate were (in thousands):

	2002	2001	2000
Tax at U.S. statutory rate	**$ (2,686)**	$ (287)	$ 1,962
Federal Tax	**(95)**	95	--
Foreign withholding taxes	**--**	--	19
German tax settlement (Note 10)	**--**	--	275
Effect of tax rates of international jurisdictions in excess of U.S. statutory rates	**97**	155	39
State income taxes	**(6)**	--	46
Effect of losses without current year benefit	**3,279**	1,043	--
Utilization of net operating loss carryforwards	**--**	(229)	(1,770)
Provision for income taxes	**$ 589**	$ 777	$ 571

Foreign withholding taxes are the result of foreign dividends received during 2000. Our provision for income taxes in fiscal 2002, 2001 and 2000 represents taxes currently payable.

We have not provided any U.S. income taxes on the undistributed earnings of our foreign subsidiaries or equity method investments based upon our determination that such earnings will be indefinitely reinvested.

7. EMPLOYEE BENEFITS

We have defined contribution plans that include a majority of our employees worldwide, under which our contributions are discretionary. The purpose of these plans is generally to provide additional financial security during retirement by providing employees with an incentive to save throughout their employment. Our contributions to the plans are based on employee contributions or compensation. Our contributions totaled $263,640, $344,811, and $321,422 for the years ended October 31, 2002, 2001 and 2000, respectively.

We also have split-dollar life insurance agreements with our executive officers. Under the terms of the agreements, we pay all of the premiums on behalf of the officers. We will be repaid the premiums from the policies' cash surrender values when the policies are terminated in accordance with the provisions of the agreements.

8. STOCK OPTIONS

In March 1997, we adopted the 1997 Stock Option and Incentive Plan (the 1997 Plan) which allows us to grant awards of options to purchase shares of our common stock, stock appreciation rights, restricted shares and performance shares. The 1997 Plan was amended in fiscal 2000 to increase the number of shares of common stock that may be issued from 500,000 to 750,000 and to increase the maximum number of shares of common stock that may be granted to any individual during the term of the 1997 Plan from 100,000 to 200,000 shares. Options granted under the 1997 Plan are exercisable for a period up to ten years after date of grant and vest in equal annual installments as specified by the Compensation Committee of our Board of Directors at the time of grant. The option price of options intended to qualify as incentive stock options may not be less than 100% of the fair market value of a share of common stock on the date of grant. As of October 31, 2002, options to purchase 663,000 shares had been granted under the 1997 Plan.

In 1990, we adopted the 1990 Stock Option Plan (the 1990 Plan), which allowed us to grant options to purchase shares of our common stock and related stock appreciation rights and limited rights to officers and our key employees. Under the provisions of the 1990 Plan, the maximum number of shares of common stock, which could be issued under options and related rights, was 500,000. There was no annual limit on the number of such shares with respect to which options and rights could be granted. Options granted under the 1990 Plan are exercisable for a period up to ten years after date of grant and vested in equal installments over a period of three to five years from the date of grant. The option price could not be less than 100% of the fair market value of a share of common stock on the date of grant and no options or rights could be granted under the 1990 Plan after April 30, 2000. A summary of the status of the options under the 1990 and 1997 Plans as of October 31, 2002, 2001 and 2000 and the related activity for the year is as follows:

	Shares under option	Weighted average exercise price per share
Balance October 31, 1999	671,680	$ 5.07
Granted	180,600	3.76
Cancelled	(22,120)	6.15
Expired	-	-
Exercised	(3,500)	2.13
Balance October 31, 2000	826,660	$ 4.77
Granted	57,000	3.67
Cancelled	(82,000)	5.23
Expired	(20,000)	7.15
Exercised	(16,400)	2.14
Balance October 31, 2001	765,260	4.63
Granted	342,000	2.14
Cancelled	(266,900)	4.18
Expired	(7,700)	2.13
Exercised	(2,500)	2.13
Balance October 31, 2002	830,160	3.78

Stock options outstanding and exercisable on October 31, 2002 are as follows:

Range of exercise prices per share	Shares under option	Weighted average exercise price per share	Weighted average remaining contractual life in years
Outstanding			
$2.125-5.125	596,660	$ 2.84	7.0
5.813-8.250	233,500	6.16	5.4
$2.125-8.250	830,160	$ 3.78	6.2
Exercisable			
$2.125-5.125	331,567	$ 3.15	-
5.813-8.250	155,100	6.29	-
$2.125-8.250	486,667	$ 4.15	-

We apply Accounting Principles Board Opinion No. 25 "Accounting for Stock Issued to Employees" (APB25), and related interpretations in accounting for the plans, and, therefore, no compensation expense has been recognized for stock options issued under the plans. For companies electing to continue the use of APB25, SFAS No. 123 "Accounting for Stock-Based Compensation", requires pro forma disclosures determined through the use of an option-pricing model as if the provisions of SFAS No. 123 had been adopted.

The weighted average fair value at date of grant for options granted during fiscal 2002, 2001, and 2000 was $1.43, $2.07, and $2.72 per share, respectively. The fair value of each option grant was estimated on the date of the grant using the Black-Scholes option-pricing model with the following assumptions:

	2002	2001	2000
Expected dividend yield	**0.00%**	0.00%	0.00%
Expected volatility	**53.71%**	56.00%	56.33%
Risk-free interest rate	**4.99%**	5.18%	6.20%
Expected term in years	**9.05**	10	10

If we had adopted the provisions of SFAS No. 123, net income (loss) and earnings (loss) per share would have been as follows:

	2002	2001	2000
Net income (loss) (in thousands)	**($8,628)**	($1,928)	$ 4,726
Earnings (loss) per share			
Basic	**($1.55)**	($.34)	$ .79
Diluted	**($1.55)**	($.34)	$ .79

As of October 31, 2002, there were outstanding non-qualified options that had been granted outside of the 1990 and 1997 plans to current and former outside members of the Board of Directors to purchase 50,000 and 75,000 shares at $5.13 and $5.81 per share, respectively. These shares are exercisable as of October 31, 2002. The options expire at various dates between 2002 and 2008.

9. RELATED PARTY TRANSACTIONS

We own approximately 24% of one of our Taiwanese-based contract manufacturers. This investment of $504,054 is accounted for using the equity method and is included in Other Assets on the Consolidated Balance Sheet. Purchases of product from this contract manufacturer totaled $5.9 million, $12.2 million and $8.6 million for the years ended October 31, 2002, 2001 and 2000, respectively.

Trade payables to this contract manufacturer were $1.0 million at October 31, 2002, and $2.2 million at October 31, 2001. Trade receivables were $43,000 at October 31, 2002.

As of October 31, 2002, we owned 35% of Hurco Automation, Ltd. (HAL), a Taiwan based company. HAL's scope of activities includes the design, manufacture, sales and distribution of industrial automation products, software systems and related components, including control systems and components manufactured under contract for sale exclusively to us. We are accounting for this investment using the equity method. The investment of $1.1 million at October 31, 2002 is included in Other Assets on the Consolidated Balance Sheet. Purchases of product from this supplier amounted to $4.1 million, $4.1 million and $4.2 million in 2002, 2001 and 2000, respectively. Trade payables to HAL were $145,000 and $200,000 at October 31, 2002 and 2001, respectively. Trade receivables from HAL were $311,000 and $173,000 at October 31, 2002 and 2001, respectively.

Summary financial information for the two affiliates accounted for using the equity method of accounting are as follows:

(000's)	2002	2001	2000
Net Sales	**$ 25,751**	$ 42,691	$ 33,850
Gross Profit	**4,296**	7,305	6,303
Operating Income	**130**	2,047	2,179
Net Income	**438**	1,609	1,005
Current Assets	**$ 12,915**	$ 14,345	$ 16,025
Non-current Assets	**1,766**	1,535	1,490
Current Liabilities	**9,514**	11,335	14,249

10. CONTINGENCIES AND LITIGATION

We previously occupied a facility located in England under a lease that expired in April 2002. The lease required that, following expiration of the lease, we make certain repairs to the facility resulting from deterioration of the facility during the lease term. The scope and cost of the repairs alleged by the lessor to be required evolved throughout fiscal 2002 as investigations and negotiations proceeded, and currently approximate $2.0 million. We do not agree with the amount of the lessor's claim and are vigorously contesting that claim. Our liability could be reduced by statutory limitations or by a negotiated settlement. Based upon facts presently available to us and the current status of our negotiations with the lessor, our best estimate of our ultimate liability is $1.1 million and we have established a reserve in that amount.

Hurco and its subsidiary IMS Technology, Inc. (IMS) have been parties to a number of legal proceedings, which involved alleged infringement of a United States interactive machining patent (the Patent) owned by IMS. All actions have been settled through licensing arrangements or litigation settlements. On August 8, 2000, Hurco and IMS agreed to a settlement of the last major claim resulting in a one-time payment to IMS. We reported license fee income and litigation settlement fees, net of expenses, of approximately $5.4 million in the fourth quarter of fiscal 2000 primarily resulting from this settlement.

In the fourth quarter of fiscal 2000, we paid approximately $275,000, to settle a contested tax liability of our German subsidiary.

We are involved in various other claims and lawsuits arising in the normal course of business. We believe it is remote that any of these claims will have a material adverse effect on our consolidated financial position or results of operations.

11. OPERATING LEASES

We lease facilities, certain equipment and vehicles under operating leases that expire at various dates through 2007. Future payments required under operating leases as of October 31, 2002, are summarized as follows (in thousands):

2003	$ 964
2004	701
2005	435
2006	256
2007	256
Thereafter	52
Total	$ 2,664

Rent expense for the years ended October 31, 2002, 2001, and 2000 was $1.8 million, $1.6 million and $1.7 million, respectively.

12. LICENSE FEE INCOME AND LITIGATION SETTLEMENT FEES, NET

License fee income and litigation settlement fees, net for fiscal 2002, 2001 and 2000 were attributable to agreements entered into by IMS, pursuant to which IMS granted fully paid-up licenses of its interactive patents in exchange for cash and other consideration. License fee payments received that were contingent upon the continued validity of the patent were deferred and recognized over the life of the patent, which expired in October 2001. As a result, we have no deferred license fee income at October 31, 2002 and do not expect any significant license fee income in the foreseeable future.

13. QUARTERLY HIGHLIGHTS (Unaudited)

2002 (In thousands, except per share data)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Sales and service fees	$ 18,520	$ 14,995	$ 18,204	$ 18,767
Gross profit	4,003	1,883(a)	4,381	4,979
Gross profit margin percentage	21.6%	12.6%(a)	24.1%	26.5%
Restructuring expense and other expense, net (Note 15)	356	1,395	--	1,004
Selling, general and administrative expenses	5,214	4,535	4,672	5,237
Operating loss	(1,567)	(4,047)	(291)	(1,262)
Net loss	(1,614)	(4,211)	(651)	(1,760)
Loss per common share - basic	$ (.29)	$ (.75)	$ (.12)	$ (.32)
Loss per common share - diluted	$ (.29)	$ (.75)	$ (.12)	$ (.32)

2001 (In thousands, except per share data)	First Quarter	Second Quarter	Third Quarter	Fourth Quarter
Sales and service fees	$ 25,933	$ 23,432	$ 21,678	$ 21,224
Gross profit	6,615	5,972	5,287	5,388
Gross profit margin percentage	25.5%	25.5%	24.4%	25.4%
Restructuring expense and other expense, net (Note 15)	--	(328)	395	76
Selling, general and administrative expenses	6,086	5,959	5,896	6,099(b)
Operating income (loss)	529	341	(1,004)	(787)
Net income	567	323	(1,329)	(1,158)
Earnings per common share - basic	$ .10	$ .06	$ (.24)	$ (.21)
Earnings per common share - diluted	$ .10	$ .06	$ (.24)	$ (.21)

a. Includes $1.1 million restructuring charge to inventory write-downs related to under-performing product lines that were discontinued.

b. Includes $550,000 of fourth quarter adjustments related to write down of product development assets no longer being used, increased provisions for un-collectable accounts, reserves for termination of a European sales agent, vacating a leased facility and a health insurance claim.

14. SEGMENT INFORMATION

We operate in a single segment: industrial automation equipment. We design and produce interactive computer control systems and software and computerized machine tools for sale through our own distribution network to the world-wide metal working market. We also provide software options, control upgrades, accessories and replacement parts for our products, as well as customer service and training support.

Our computerized metal cutting machine tools are manufactured to our specifications by manufacturing contractors in Taiwan including our wholly owned subsidiary, Hurco Manufacturing Limited (HML). Our executive offices and principal design, engineering, and manufacturing management operations are headquartered in Indianapolis, Indiana. We sell our products through approximately 346 independent agents and distributors in 35 countries throughout North America, Europe and Asia. We also have our own direct sales and service organizations in the United States, England, France, Germany, Italy and Singapore. During fiscal 2002, no customer accounted for more than 5% of our sales and service fees.

The following table sets forth the contribution of each of our product groups to our total sales and service fees during each of the past three fiscal years (in thousands):

NET SALES AND SERVICE FEES BY PRODUCT CATEGORY

	Year Ended October 31,		
	2002	2001	2000
Computerized Machine Tools	**$ 55,503**	$ 73,286	$ 71,708
Computer Controls Systems and Software*	**3,632**	5,716	9,605
Service Parts	**8,111**	9,516	10,649
Service Fees	**3,240**	3,749	4,242
Total	**$ 70,486**	$ 92,267	$ 96,204

*Amounts shown do not include CNC systems sold as an integrated component of computerized machine systems.

Revenues by geographic area, based on customer location, for each of the past three fiscal years were (in thousands):

	Year Ended October 31,		
	2002	2001	2000
United States	**$ 22,782**	$ 32,935	$ 40,920
Germany	**22,863**	28,452	23,654
United Kingdom	**7,387**	8,814	10,128
Other Europe	**14,142**	17,847	12,932
Total Europe	**44,392**	55,113	46,714
Asia and Other	**3,312**	4,219	8,570
Total Foreign	**47,704**	59,332	55,284
	$ 70,486	$ 92,267	$ 96,204

Long-lived assets by geographic area were (in thousands):

	October 31,	
	2002	2001
United States	**$ 13,824**	$ 14,725
Foreign Countries	**1,793**	1,556
	$ 15,617	$ 16,281

15. RESTRUCTURING EXPENSE AND OTHER EXPENSE, NET

In the fourth quarter of fiscal 2000, we recorded a charge of $300,000 for severance costs related to the termination of employees. Fourteen employees received notice on October 31, 2000 that their positions were being eliminated in fiscal 2001. All employee severance related to the October 31, 2000 reserve has been paid.

Restructuring expense in fiscal 2001 included a reversal of a of $328,000 reserve for sub-letting the final year of the excess building space of a subsidiary and finding alternative uses for a previously reserved asset. Also, in fiscal 2001, a provision of $471,000 was recorded for severance costs related to a domestic cost reduction program in which 59 positions were eliminated. All employee severance related to the October 31, 2001 reserve has been paid.

During fiscal 2002, we discontinued several under-performing product lines, sold the related assets and discontinued a software development project to enable us to focus our resources and technology development on our core products, which consist primarily of general purpose computerized machine tools for the metal cutting industry (vertical machining centers) into which our proprietary UltiMax® soft-ware and computer control systems have been fully integrated. As a result of these actions, we recorded restructuring charges totaling $3.1 million consisting primarily of:

(a) non-cash write downs of inventories of $1.1 million recorded in cost of sales and capitalized software development costs of $1.0 million recorded as restructuring expense, and (b) severance costs of $934,000, related to personnel reductions.

Also included in restructuring expense and other expense, net is a $1.1 million provision for potential expenditures related to a disputed claim in the United Kingdom, regarding a terminated facility lease (Note 10) and a $277,000 credit due to a refund of software development fees resulting from the termination of a software development agreement during the second fiscal quarter (Note 17).

The severance accrual of $264,000 at October 31, 2002 represents costs related to employees that will be paid in future periods. The severance provision represents 53 positions that have been eliminated or will be eliminated in fiscal 2003. At October 31, 2002, 38 employees had been paid the full amount of their severance while the remaining 15 employees will be paid at various times through the second quarter of fiscal 2003.

Description	Balance 10/31/99	Provision (Credit)	Charges to Accrual	Balance 10/31/00
Excess Building Capacity	$ 286	--	--	$ 286
Equipment Leases	77	--	(23)	54
Severance Costs	--	300	--	300
	$ 363	$ 300	$ (23)	$ 640

	Balance 10/31/00	Provision (Credit)	Charges to Accrual	Balance 10/31/01
Excess Building Capacity	$ 286	$ (286)	--	--
Equipment Leases	54	(42)	(12)	--
Severance Costs	300	471	(637)	133
	$ 640	$ 143	$ (649)	$ 133

	Balance 10/31/01	Provision (Credit)	Charges to Accrual	Balance 10/31/02
Cost of sales - restructuring:				
Inventory write-down	$ --	$ 1,083	$ 1,083	$ --
Restructuring expense:				
Capitalized software development cost write-off	--	1,036	1,036	--
Severance costs	133	934	803	264
Other expense (credit):				
Foreign lease termination liability (Note 10)	51	1,062	--	1,113
Termination of software development agreement (Note 17)	--	(277)	(277)	--
Total restructuring and other expense, net	184	2,755	1,562	1,377
Total	$ 184	$ 3,838	$ 2,645	$ 1,377

16. STOCK REPURCHASE

In fiscal 2001, we repurchased 391,101 shares of our common stock for approximately $1.7 million of which 278,001 were purchased from a related party for $1.2 million. The repurchase of shares is reflected as a reduction in common stock.

17. SOFTWARE DEVELOPMENT AGREEMENTS AND LOAN AGREEMENT

During fiscal 2001, we entered into agreements with a private software company to fund development costs related to the integration of patented, open architecture technology into our computer control products. We agreed to fund an aggregate of $405,000, over a fifteen-month period ending in July 2002 of which $180,000 was paid and recorded as a research and development expense in fiscal 2001. We also agreed to fund a secured term loan payable in installments through February 2002, of $1.0 million which is due April 1, 2003. In addition, the company granted us warrants to purchase an equity interest, which were exercisable on or before December 31, 2002, and 2003.

As of October 31, 2001, our combined investment in the secured loan and warrants was $672,000, and is reflected in Investments and Other Assets in the accompanying consolidated balance sheet.

During fiscal 2002, we terminated these agreements. In connection therewith, we received repayment of our investment in a secured loan and warrants. We were also reimbursed for software development fees previously paid and expensed, resulting in a credit of $277,000 which is reflected in Restructuring Expense and Other Expense. Neither party has any future obligations to the other under the termination agreement.

We had an agreement with another private software company to fund $683,000 of development costs, which was recorded as a research and development expense in fiscal 2002 and fiscal 2001. In October 2002, we exercised an option to purchase the core technology owned by the software company for $1.8 million which is recorded in Investments and Other Assets at October 31, 2002. The core technology consists of patented software-based computer control technology that will be incorporated in our proprietary computer control system.

18. NEW ACCOUNTING PRONOUNCEMENTS

In June 2001, the Financial Accounting Standards Board issued Statement No. 141, "Business Combinations" (SFAS 141) and Statement No. 142, "Goodwill and Other Intangible Assets" (SFAS 142). SFAS 141 requires that all business combinations initiated after June 30, 2001 be accounted for under the purchase method of accounting. Under SFAS 142, amortization of goodwill will cease and the goodwill carrying values will be tested periodically for impairment. We are required to adopt SFAS 142, effective November 1, 2002 for goodwill and intangible assets acquired prior to July 1, 2001. Goodwill and intangible assets acquired after June 30, 2001 were subject immediately to the goodwill non-amortization and intangible provisions of this statement. We do not expect that the adoption of this standard will have a material effect on the Consolidated Financial Statements.

In August 2001, the Financial Accounting Standards Board issued Statement No. 144, "Accounting for the Impairment or Disposal of Long-Lived Assets" (SFAS 144), which is effective for the fiscal year beginning November 1, 2002. SFAS 144 establishes a single model to account for impairment of assets to be held or disposed of, incorporating guidelines for accounting and disclosure of discontinued operations. We do not expect that the adoption of this standard will have a material effect on the Consolidated Financial Statements.

In July 2002, the Financial Accounting Standards Board issued Statement No. 146, "Accounting for Costs Associated with Exit or Disposal Activities". This Standard, which is effective for disposal activities initiated after December 31, 2002, addresses significant issues regarding the recognition, measurement and reporting of costs associated with exit and disposal activities. We will comply with the provisions of the Standard with respect to exit and disposal activities initiated after the effective date, but do not expect adoption to have any material impact on the Consolidated Financial Statements.

In November 2002, the Financial Accounting Standards Board ("FASB" or the "Board") issued FASB Interpretation No. 45 ("FIN 45"), "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others, an interpretation of FASB Statements No. 5, 57 and 107 and Rescission of FASB Interpretation No. 34." FIN 45 clarifies the requirements of FASB Statement No. 5, Accounting for Contingencies, relating to the guarantor's accounting for, and disclosure of, the issuance of certain types of guarantees. The disclosure provisions of FIN 45 are effective for financial statements of interim or annual periods that end after December 15, 2002. However, the provisions for initial recognition and measurement are effective on a prospective basis for guarantees that are issued or modified after December 31, 2002, irrespective of a guarantor's year-end.

We do not expect the impact of adopting the interpretation to have a material effect on the Consolidated Financial Statements.

LEADERSHIP

Board of Directors

Robert W. Cruickshank (2, 3), President, R.W. Cruickshank Company

Michael Doar (1), Chief Executive Officer, Hurco Companies, Inc.

Richard T. Niner (1), General Partner, Brynwood Partners; General Partner, Wind River Associates

O. Curtis Noel (3), Independent Business Consultant

Charles E. Mitchell Rentschler (2), Independent Business Consultant

Gerald V. Roch (2), Independent Business Consultant

1 – Executive/Nominating Committee

2 – Audit Committee

3 – Compensation Committee

Corporate Officers and Division Executives

Michael Doar, Chairman and Chief Executive Officer

James D. Fabris, President and Chief Operating Officer

Roger J. Wolf, Senior Vice President, Secretary, Treasurer and Chief Financial Officer

David E. Platts, Vice President, Technology

Stephen J. Alesia, Corporate Controller and Assistant Secretary

James D. Kawaguchi, General Manager, Hurco U.S.A.

Gerhard Kohlbacher, President, Hurco Germany

David Waghorn, General Manager, Hurco United Kingdom

Philippe Chevalier, General Manager, Hurco France

Paolo Casazza, General Manager, Hurco Italy

William Chan, General Manager, Hurco Southeast Asia

Charlie Tsai, General Manager, Hurco Manufacturing Limited (Taiwan)

CORPORATE INFORMATION

Annual Meeting

All shareholders are invited to attend our annual meeting, which will be held on Thursday, April 3, 2003 at 10:00 a.m. Eastern Time at Hurco's Corporate Offices, One Technology Way, Indianapolis, Indiana.

Transfer Agent

Boston Equiserve Division, Equiserve Limited Partnership, 150 Royall Street, Canton Massachusetts 02021

Legal Counsel

Corporate Law: Baker & Daniels; Weil, Gotshal & Manges LLP

Patent Law: Baker & Daniels; Woodard, Emhart, Naughton, Moriarty, and McNett LLP

Independent Auditors

PricewaterhouseCoopers LLP, Indianapolis, Indiana

Investor Relations

Roger J. Wolf, Senior Vice President, Secretary, Treasurer and Chief Financial Officer, One Technology Way, Indianapolis, Indiana 46264, Telephone: (317) 293-5309

Stock Market Information

Hurco Common Stock is traded on the Nasdaq National Market under the ticker symbol HURC. Stock price quotations are printed daily in major newspapers.

The following table sets forth the high and low sales prices of the shares of Common Stock for the periods indicated, as reported by the Nasdaq National Market.

	2002			2001		
Fiscal Quarter Ended	**High**		**Low**	**High**		**Low**
January 31	**$2.780**	**-**	**$2.050**	$3.875	-	$3.250
April 30	**$3.350**	**-**	**$2.030**	$4.188	-	$3.150
July 31	**$2.950**	**-**	**$1.500**	$3.666	-	$2.150
October 31	**$2.220**	**-**	**$1.450**	$2.990	-	$2.080

The Company does not currently pay dividends on its Common Stock and intends to continue to retain earnings for working capital, capital expenditures and debt reduction.

There were approximately 408 holders of record of Hurco Common Stock as of January 2, 2003.

Concerning Forward-Looking Statements

This annual report contains forward looking statements which involve known and unknown risks, uncertainties and other factors that may cause our actual results, performance or achievement to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. These factors include, among others, changes in general economic and business conditions that affect market demand for machine tools and related computer control systems, software products, and replacement parts, changes in manufacturing markets, the success of our plans to reduce inventory and operating costs, adverse currency movements, innovations by competitors, quality and delivery performance by our contract manufacturers and governmental actions and initiatives including import and export restrictions and tariffs. A full discussion of these and other factors are made in Hurco's 10-K, 10-Q and other Security and Exchange Commission filings.

Hurco Companies, Inc.
One Technology Way, PO Box 68180, Indianapolis IN 46268, 800 634 2416, www.hurco.com