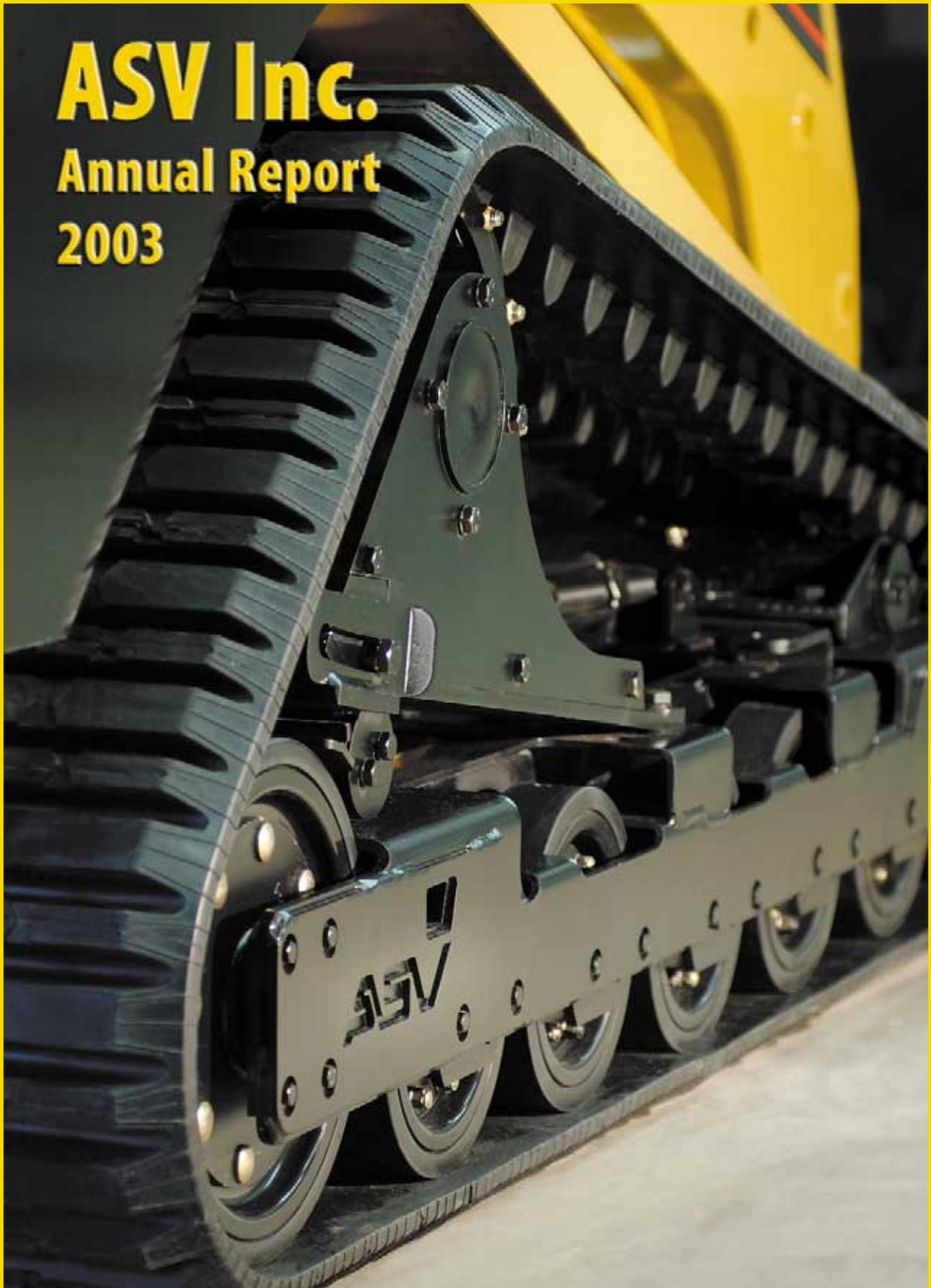


ASV Inc.
Annual Report
2003







A.S.V., Inc. designs, manufactures and sells a variety of rubber track loaders along with related components, accessories and attachments.

ASV's patented rubber track undercarriage technology is unique and leads a rapidly growing industry of rubber track loaders. Rubber track loaders are widely used within industries such as construction, utility, landscaping, agriculture and the military.

ASV's undercarriage technology gives users a unique combination of benefits. It offers mobility superior to traditional rubber tire vehicles, plus flotation and traction surpassing that of steel track machines. The result is a highly versatile work platform that can effectively operate in virtually any environment.

ASV machines are often the only machines able to work in extreme conditions such as soft, wet, swampy, rough and hilly terrains. Very low ground pressure and non-destructive tracks also make ASV equipment an ideal solution for work on finished surfaces, such as concrete or asphalt pavements, sod and landscaping because they do not cause damage. Turf Edition All Surface Loaders with unique smooth surface rubber tracks give turf professionals ultimate protection against damage to finished turf and landscaped surfaces.

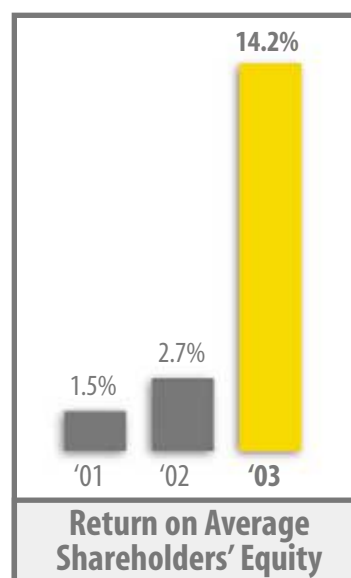
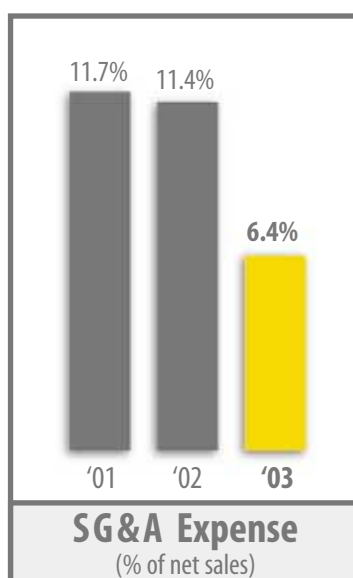
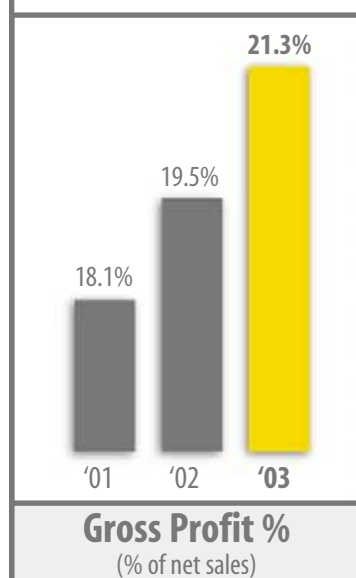
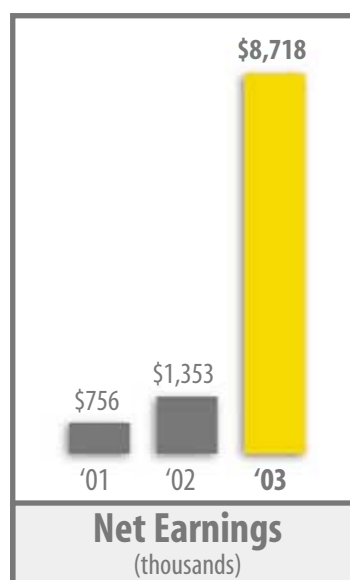
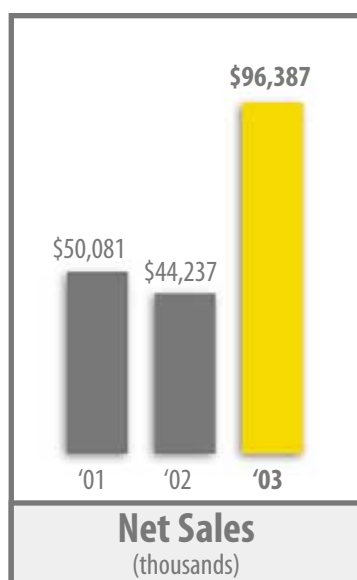
A complete line of performance-match attachments, called Posi-Tools, help complete the ASV All Surface Loader package and provide users with optimized solutions for virtually every machine application.

ASV is an affiliate of Caterpillar Inc. ASV rubber track undercarriages are a primary component on Caterpillar® Multi Terrain Loaders. Five second-generation Cat® B-Series Multi Terrain Loader models are now available through the Caterpillar worldwide distribution network.

ASV sells ASV-branded products primarily through independent equipment dealers in the United States, Canada, Australia, New Zealand and Portugal.

Financial Highlights

(Dollar amounts in thousands, except per share data)	Years ended December 31,				
	2003	2002	2001	2000	1999
Net Sales	\$ 96,387	\$ 44,237	\$ 50,081	\$ 43,860	\$ 36,168
Net Earnings	8,718	1,353	756	1,451	1,412
Net Earnings Per Share - Diluted	.78	.13	.07	.15	.14
Working Capital	67,994	47,366	47,790	47,224	36,497
Total Assets	82,624	57,210	57,941	55,006	48,650
Long-Term Liabilities, Less Current Portion	1,845	1,980	2,013	2,117	2,197
Shareholders' Equity	72,280	50,467	50,571	49,763	39,096
Diluted Weighted Average Shares Outstanding	11,185,683	10,229,057	10,352,468	9,966,661	9,941,616



To Our Shareholders

This past year was one of momentum and growth, one that saw the marketplace further accept ASV's technology while also giving strong signals that such acceptance is only the beginning. ASV's long held leadership in the rubber track loader market has proven to be a catalyst for the creation of an entirely new class of equipment.

Indeed, rubber track loaders clearly established a strong foothold in the \$2 billion skid-steer equipment market in 2003. For example, in the January 2004 issue of Diesel Progress magazine, industry analyst Charles Yengst wrote: "Sales are soaring Nothing else in the equipment business compares to [rubber track loader] growth lately."

In addition to significant sales momentum, this past year also saw changes in ASV's relationship with Caterpillar. On Jan. 22, 2004, ASV bought back the existing warrant held by Caterpillar. This allows ASV to continue its growth pattern, while also eliminating the potential of future earnings dilution. We also announced plans to enter into additional agreements for the use of ASV undercarriages on other Caterpillar products. In these two steps, ASV continued the free-

dom, independence and entrepreneurial energy that has fueled our growth, while at the same time providing for ASV's long term stability.

As we move into the second half of this decade, we anticipate we will continue manufacturing and supplying Caterpillar with our proprietary rubber track undercarriages for use on their line of Multi Terrain Loaders and other products. Caterpillar has become the top seller of rubber track loaders in the industry, and with the market still in its early stages in America and debuting in Europe, Caterpillar sales are expected to only increase. We believe this will continue to benefit ASV by increasing market awareness of rubber track loaders.

In 2003, ASV's R-Series Posi-Tracks experienced incredible growth, with sales increasing more than 100% over 2002. ASV continues to build on the success of the R-Series, with the introduction of the RC-60 and RC-85. These models bring the total of new R-Series introductions to four in the past two years alone. With five models in the R-Series product line, ASV has the most extensive model line in the industry, from 30 to 100 horsepower. No one is better



To Our Shareholders

continued

equipped for market share growth than ASV with the R-Series Posi-Tracks. Combined with Caterpillar, our rubber track technology represented approximately 60% of all rubber track loader sales in 2003.

We continued to build our nationwide R-Series dealer network in 2003 and that will remain a focus as we direct sales efforts in that direction in 2004. In addition, we continue to work with one of our dealers to place RC-30 All Surface Loaders as rental units at



Home Depot stores across the country. The RC-30 is the perfect machine for residential homeowners, and we're excited about the potential of this arrangement.

We have also taken steps to assure that we keep up with demand. In January 2004, we purchased a 110,000 square foot, state-of-the-art manufacturing facility near Grand Rapids for necessary expansion and additional capacity. With moves such as this, along with new ASV products, new undercarriages for Caterpillar and growing acceptance of our rubber track technology in the marketplace, we hope you share our optimism of the future.

I want to finish with a special thanks to our employees, to our shareholders and to all those who have supported ASV's vision of changing the way the world works. That's exactly what we're doing.

Sincerely,

A handwritten signature in black ink, reading 'Gary Lunde'.

Chairman & President



Management's Discussion and Analysis of Financial Condition and Results of Operations

Overview

ASV designs, manufactures and sells rubber track loaders and related accessories and attachments. ASV also manufactures rubber track undercarriages, which are a primary component on Caterpillar's Multi Terrain Loaders. ASV's products are able to traverse nearly any terrain with minimal damage to the ground, making it effective in industries such as construction, landscaping and agriculture. ASV distributes its products through an independent dealer network in the United States, Canada, Australia, New Zealand and Portugal. The undercarriages sold to Caterpillar are incorporated by Caterpillar in their Multi-Terrain Loader products and sold exclusively through the Caterpillar dealer network, primarily in North America.

ASV experienced a significant increase in sales in 2003 due to several reasons as explained below:

- The Company believes there is a greater acceptance of rubber track machines in the marketplace as users experience the benefits that a rubber track machine can provide over a standard wheeled machine.
- The number of companies entering into the rubber track machine market has increased in the last few years, thereby contributing to the increased awareness and market acceptance of the products.
- ASV has increased its number of product offerings over the past few years, such that it has become easier to attract prospective dealers to carry the R-Series Posi-Track product line.
- Caterpillar has increased the number of MTL models it offers to its dealers, from two models in 2001 to five in 2003. In addition, the number of Caterpillar dealers that are able to carry the MTL product line has increased from 16 pilot dealers in 2001 to all North American dealers (approximately 65) in 2003.
- The current low interest rate environment has provided for easier financing by end users.
- Recent tax legislation has provided increased depreciation allowances allowing end users to depreciate a greater portion of machine purchases in the first year of ownership, thereby potentially reducing the cost of machine ownership in the first year of operation.

Critical Accounting Policies

The following discussion and analysis of the Company's financial condition and results of operations is based upon its financial statements, which have been prepared in accor-

dance with accounting principles generally accepted in the United States. The preparation of these financial statements requires management to make estimates and judgments that affect the reported amounts of assets, liabilities and expenses, and related disclosures. On an on-going basis, management evaluates its estimates and judgments, including those related to accounts receivable, inventories and warranty obligations. By their nature, these estimates and judgments are subject to an inherent degree of uncertainty. Management bases its estimates and judgments on historical experience, observance of trends in the industry, information provided by customers and other outside sources and on various other factors that are believed to be reasonable under the circumstances, the results of which form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions.

Management believes the following critical accounting policies, among others, affect its more significant judgments and estimates used in the preparation of the Company's consolidated financial statements.

Revenue Recognition and Accounts Receivable

Revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable and collectibility is reasonably assured. The Company generally obtains oral or written purchase authorizations from customers for a specified amount of product at a specified price and considers delivery to have occurred at the time of shipment. ASV maintains an allowance for doubtful accounts for estimated losses resulting from the inability of its customers to make required payments. If the financial condition of ASV's customers were to deteriorate, resulting in an impairment of their ability to make payments, additional allowances may be required.

Inventories

Inventories are stated at the lower of cost or market, cost being determined on the first-in, first-out method. Adjustments to slow moving and obsolete inventories to the lower of cost or market are provided based on historical experience and current product demand. The Company does not believe its inventories are subject to rapid obsolescence. The Company evaluates the adequacy of the inventories' carrying value quarterly.

Warranties

ASV provides for the estimated cost of product warranties at the time revenue is recognized. While ASV engages in extensive product quality programs and

Management's Discussion and Analysis

continued

processes, including actively monitoring and evaluating the quality of its component suppliers, ASV's warranty obligation is affected by product failure rates, material usage and service delivery costs incurred in correcting a product failure. Should actual product failure rates, material usage or service delivery costs differ from ASV's estimates, revisions to the estimated warranty liability may be required.

Results of Operations

The following table sets forth, for the periods indicated, certain Statements of Earnings data as a percentage of net sales:

	Years Ended December 31,		
	2003	2002	2001
Net sales	100.0%	100.0%	100.0%
Gross profit	21.3	19.5	18.1
Selling, general & administrative	6.4	11.4	11.7
Research & development ..	0.8	4.1	5.3
Operating income	14.0	4.0	1.1
Net earnings	9.0	3.1	1.5

Net Sales

For the year ended December 31, 2003, net sales totaled \$96.4 million, a 118% increase over net sales for the year ended December 31, 2002 due to several factors. First, the Company had increased shipments of undercarriages to Caterpillar for use on Caterpillar's MTL product line. Shipments increased as Caterpillar had more models available to sell during 2003 (five) compared with 2002 (two). In addition, during 2002, Caterpillar was unable to sell two models of its MTLs due to production issues unrelated to ASV's undercarriages. These production issues were resolved in 2003 and these two models were placed back into production, which resulted in increased sales of these models by Caterpillar in 2003. Second, ASV introduced a new model to its R-Series product line, the RC-100, in the first quarter of 2003. This model replaced the model 4810 Posi-Track and the RC-100 experienced three times the unit volume in 2003 that the 4810 had in 2002. Also, the Company believes the addition of the RC-100 Posi-Track has aided the sales of the Company's other models, the RC-30 and RC-50, as the increased number of product offerings has attracted an increased number of dealers that wish to carry the Company's products. Also contributing to the increased sales in 2003 was the increase in the sale of service parts, as the number of machines and MTL undercarriages continues to increase.

For the year ended December 31, 2002, net sales totaled \$44.2 million, an 11.7% decrease over net sales for the year ended December 31, 2001 due to several offsetting factors. First, the Company had no machine sales of the private label version of the RC-30 All Surface Loader under its alliance with Polaris, the ASL-300, in 2002, which had accounted for \$7.9 million of sales in 2001. Second, the Company had decreased sales of its 4810 and 2800 series Posi-Tracks, due to the introduction of additional MTL models in 2002 and the continued softness in the overall construction equipment sales market. Partially offsetting these decreases were increased MTL undercarriage sales of \$3.3 million, as ASV began supplying undercarriages for two additional MTL models that were introduced by Caterpillar in 2002. The Company also experienced increased sales of \$8.0 million from its R-Series product line due to the introduction of the RC-50 and R-50 products in the first quarter of 2002. In addition, sales of service parts increased in 2002 as the number of machines and undercarriages in the field continued to increase.

Gross Profit

Gross profit for the year ended December 31, 2003 was \$20.5 million, or 21.3% of net sales, compared with \$8.6 million, or 19.5% of net sales for 2002. The increase in gross profit was due to a combination of increased sales in 2003 as discussed above and an increase in the gross profit percentage. The increase in gross profit percentage was due to two primary factors. First, the increased sales of ASV branded machines, which generally carry a higher gross profit percentage than MTL undercarriages, help increase the gross profit percentage in 2003. Second, the Company's mix of MTL undercarriages sold in 2003 contained a greater number of higher margin undercarriages than was sold in 2002. In 2002, the Company primarily sold one model of MTL undercarriage to Caterpillar, which had the lowest gross profit percentage of the MTL undercarriages.

For the year ended December 31, 2002, gross profit was \$8.6 million, or 19.5% of net sales, compared with \$9.1 million, or 18.1% of net sales, for 2001. The decrease in gross profit was due primarily to the decreased sales for 2002. The increase in the gross profit percentage was due to the following offsetting factors. First, as discussed above, the Company had no Polaris ASL-300 sales in 2002, which carry a lower gross profit than the Company's other products, thereby causing an increase in the gross profit percentage for 2002 compared to 2001. Second, the Company had increased sales of service parts in 2002, which generally carry a higher gross profit than finished goods. Offsetting these increases, the Company sold a greater concentration of lower margin MTL undercarriages in 2002 as compared to 2001 as Caterpillar was not able to produce its two larger MTL models for the majority of 2002 due to a production issue unre-

lated to ASV's undercarriage. In addition, the Company experienced fewer sales of its higher margin model 4810 Posi-Track as discussed above.

Selling, General and Administrative Expenses

Selling, general and administrative expenses increased to \$6.2 million for the year ended December 31, 2003, compared with \$5.0 million for the year ended December 31, 2002. The increase was due primarily to several factors. First, commissions to ASV's sales force increased in 2003 due to the increased sales. Second, in the second quarter of 2002, selling, general and administrative expenses were lower than historical levels due primarily to the reversal of a portion of a remarketing reserve during the second quarter of 2002. The Company had previously established a remarketing reserve of \$250,000 for any expected costs associated with remarketing existing machines at one customer's locations, some of which were ultimately returned to the Company. ASV had originally anticipated these machines would be remarketed to other dealers, but instead chose to have certain of these machines returned to ASV for use in its new rental program which began in the second quarter of 2002. As these machines were returned to ASV and reflected as sales returns with a corresponding decrease in gross profit of approximately \$184,000, a portion of the remarketing reserve was no longer needed. The Company reversed the portion of the remarketing reserve that related to the returned machines, which decreased selling, general and administrative expenses by approximately \$184,000. Third, payroll taxes increased in 2003 due to the exercise of non-qualified stock options by employees which required the payment of the employer portion of payroll taxes by the Company. In 2002, there were no non-qualified stock options exercised due to the lower price of the Company's common stock.

For the year ended December 31, 2002, selling, general and administrative expenses decreased 14.1% to \$5.0 million compared with \$5.9 million for the year ended December 31, 2001. The decreased level of expenses was due to the following two items. First, in 2001, the Company established a remarketing reserve of \$250,000 as discussed above. The Company reversed the portion of the remarketing reserve that related to the returned machines, which decreased selling, general and administrative expenses by approximately \$184,000 in 2002. Second, the Company had decreased commissions to Caterpillar as the number of commissionable products sold to Caterpillar dealers decreased in 2002.

Research and Development

Research and development expenses decreased to \$795,000 for the year ended December 31, 2003 compared with \$1,803,000 for the year ended December 31, 2002. The decrease was due to the completion of the development, testing and integration of the fifth undercarriage used in

Caterpillar's MTL product line in 2002. In 2002, ASV incurred research and development expenses of \$1 million related to the undercarriages used in Caterpillar's MTL product line.

For the year ended December 31, 2002, research and development expenses decreased \$843,000 to \$1,803,000, compared with \$2,645,000 for the year ended December 31, 2001. This decrease was due primarily to the completion of the development, testing and integration of the fifth undercarriage used in Caterpillar's MTL product line in the third quarter of 2002.

The Company anticipates its research and development expenses will be in the range of 0.5% to 1% of net sales in the future and will be focused on improvements to its existing products and extensions of its product lines.

Other Income (Expense)

Interest expense remained relatively unchanged in 2003 compared with 2002 as debt levels and interest rates were similar in 2003 and 2002.

Other income for the year ended December 31, 2003 decreased to \$178,000, compared with \$264,000 for the year ended December 31, 2002. The decrease was due to lower interest income from lower interest rates available for the Company's cash equivalents and a reduction in royalty revenues received from one of the Company's vendors as the royalty agreement expired in 2003.

For the year ended December 31, 2002, interest expense decreased to approximately \$126,000, compared with approximately \$146,000 for the year ended December 31, 2001. The decrease was due to the Company refinancing approximately \$784,000 of its long-term debt from 9.0% to 6.5% for a five-year term in December 2001.

Other income was approximately \$264,000 for 2002, compared with approximately \$529,000 for 2001. The decrease in 2002 was due primarily to lower interest income from lower interest rates and decreased short-term investments as the Company used these investments to fund operations in 2002.

Net Earnings

Net earnings increased for the year ended December 31, 2003 to \$8.7 million, compared with \$1.4 million for the year ended December 31, 2002. The increase was due to the more than doubling of net sales in 2003, combined with an increased gross profit percentage, offset in part by slightly higher operating expenses, lower non-operating income and a higher effective income tax rate.

For the year ended December 31, 2002, net earnings increased to approximately \$1,353,000, compared with approximately \$756,000 in 2001. The increase in net earnings

Management's Discussion and Analysis

continued

was due to lower operating expenses and an increased gross profit percentage, offset in part by decreased sales and an increased effective income tax rate.

Liquidity and Capital Resources

For the year ended December 31, 2003, the Company generated total cash flows of approximately \$25 million, compared with a use of cash of approximately \$1 million for the year ended December 31, 2002. Approximately \$19 million of this increase related to cash flows generated from operations. Included in this figure was the significant increase in net earnings the Company experienced in 2003 due to a 118% increase in sales. The Company also recorded a tax benefit from the exercise of stock options and a warrant of approximately \$5.6 million in 2003. This was due to a large increase in the exercise of employee stock options, a result of the increase in the price of the Company's common stock in 2003. The Company was also able to reduce its inventories by \$5.1 million, the majority of which resulted from increased sales of the Company's RC-30 product in 2003. In addition, used equipment levels decreased \$1.4 million as a result of the Company holding its first used equipment auction in April 2003. The Company used \$1.7 million of cash to invest in property, plant and equipment. Financing activities generated an additional \$7.3 million as the Company received \$7 million of net proceeds from the exercise of stock options and a warrant in 2003.

For 2004, the Company anticipates sales in the range of \$130-155 million, with earnings expected to be in the range of \$.95-1.15 per share on a diluted basis. The Company anticipates its 2004 sales of MTL undercarriages to Caterpillar could exceed \$50 million. The Company's payment terms from Caterpillar are generally net 30 days.

Caterpillar Revenue Recognition/Gross Profit

The Company recognizes as sales its cost for the MTL undercarriages, as defined in the alliance agreement between the Company and Caterpillar, plus a portion of the anticipated gross profit that Caterpillar expects to recognize upon sale of the MTLs to Caterpillar dealers, when the Company ships undercarriages to Caterpillar. On January 1, 2005, the Company's portion of the anticipated gross profit that Caterpillar expects to recognize upon sale of the MTLs to Caterpillar dealers will be reduced by 33% for two of the three undercarriages the Company currently sells to Caterpillar. On January 1, 2006, the Company's portion of the anticipated gross profit that Caterpillar expects to recognize upon sale of the MTLs to Caterpillar dealers will be reduced by 33% for the other undercarriage the Company currently sells to Caterpillar. The Company believes these revisions will not cause its overall gross profit percentage generated on the sale of MTL undercarriages in 2005 to fall below the overall gross profit percentage it generated on the sale of MTL undercarriages for the year ended December 31, 2003. The MTL undercarriages are not a commissionable product under the Company's Commercial Alliance Agreement with Caterpillar.

Customer Note and Financing Arrangement

In December 2000, the Company made a sale to one customer totaling approximately \$4.0 million. During 2001, this customer did not make payments in accordance with the terms of its agreement with the Company, including approximately \$800,000 of machines and attachments sold by the customer for which payment was not remitted to the Company.

Table of Contractual Commitments

The following table represents the Company's contractual obligations at December 31, 2003:

Contractual Obligations	Payments due by period				
	Total	Less than 1 year	1-3 years	3-5 years	More than 5 years
Long-Term Debt	\$ 75	\$ 20	\$ 40	\$ 15	\$ --
Capital Lease Obligation	1,906	116	798	167	825
Operating Leases	27	9	18	\$ --	\$ --
Purchase Obligations	36,960	36,960	\$ --	\$ --	\$ --
Financing Guarantee	35	35	\$ --	\$ --	\$ --

Purchase obligations represent the total value of all open purchase orders for the purchase of raw materials and components used in the manufacture of the Company's products as of December 31, 2003. Financing guarantee is described in Note L to the financial statements filed in connection with this Annual Report.

In January 2002, the Company and the customer entered into a note agreement for the value of the machines that had been previously sold by the customer for which payment was not remitted to the Company. The initial amount of the note was \$800,000 and the note was due in 48 monthly installments plus interest at the prime rate plus 2%, beginning March 15, 2002. The customer made payments on this note through April 2003.

In December 2003, this customer closed on a private placement of debt and equity securities with non-affiliated investors. In connection with the closing of the private placement, the Company was paid \$285,000 which was applied against the trade accounts receivable owed by this customer. The Company agreed to transfer \$300,000 from the customer's accounts receivable balance to a new note. This \$300,000 amount was combined with the amount owed on the existing note owed to the Company of \$566,667 for a new note of \$866,667. The new note bears interest at the prime rate plus 2% and is due in 60 monthly installments beginning February 2004.

Also in December of 2003, this customer obtained financing from a non-affiliated finance company to pay its remaining accounts receivable balance owed to the Company of \$589,000. The Company has guaranteed the repayment of the \$589,000 to the finance company. The Company has computed the value of the guarantee at \$35,000 and has recorded this amount as a reduction of net sales for the year ended December 31, 2003. A similar amount has been included in other accrued liabilities at December 31, 2003.

Rental Program

In October 2002, the Company began a program to market its RC-30 and RC-50 products directly to rental facilities. Under this program, ASV identifies rental facilities that will lease ASV machines from an unaffiliated finance company. ASV records the sale of the machines to the finance company when they are delivered to the rental facility and collectibility is reasonably assured. At the end of the four-year lease, should the rental facility elect not to purchase the leased machines from the finance company, ASV has guaranteed to pay a residual value equal to 25% of the original selling price of the financed equipment. At that point, ASV would take possession of the equipment. As of December 31, 2003, the total amount of future residual payments the Company may be required to make in the event of nonpayment by rental facilities totaled approximately \$100,000. The Company believes the value of the related equipment will equal or exceed the amount of residual payment. Accordingly, the Company does not anticipate any loss will be incurred should any residual payments need to be made.

Through June 30, 2003, the lease agreement between the rental facility and the finance company provided the rental facility a 90-day period during which any rental income generated was split between the rental facility and ASV. After the 90-day period expired, the rental facility had the option of terminating the lease, in which case ASV was only responsible for the costs associated with transferring the machines to another rental facility. If the rental facility elected to continue the lease, ASV refunded any rental payments received during the 90-day period.

Beginning July 1, 2003, this rental program was revised to eliminate the lease termination option after the initial 90-day period. As of December 31, 2003, the Company was still responsible for the remarketing of approximately \$1.1 million of machines and attachments. The Company has accrued the estimated costs to remarket these machines and attachments as of December 31, 2003 and does not anticipate it will incur any loss as a result of marketing these machines and attachments.

Relationship with Finance Companies

The Company has affiliated itself with several finance companies that finance the sale of the Company's products. By using these finance companies, the Company receives payment for its products shortly after their shipment. The Company pays a portion of the interest cost associated with financing these shipments that would normally be paid by the customer, generally ranging from three to twelve months, depending on the amount of down payment made by the customer. The Company is also providing twelve-month terms for one machine to be used for demonstration purposes for each qualifying dealer. In addition, the Company does, from time to time, offer extended terms financing on the sale of certain products to its dealers for periods ranging from 90 days to two years.

Stock Repurchase Program

In October 2003, the Company announced a new stock buy-back program whereby ASV may repurchase up to \$10 million of its common stock in the open market. The Company intends to fund the repurchases with available funds. The term of the repurchase program is through October 2004 or until such amount of common stock is repurchased. As of February 27, 2004, the Company had not made any repurchases of its common stock under this program. Under previous programs, the most recent of which expired in September 2003, the Company repurchased 195,580 shares of its own common stock at an aggregate purchase price of approximately \$1,974,000.

Management's Discussion and Analysis

continued

Caterpillar Equity Transactions

In January 2004, the Company sold 1,040,069 shares of its common stock to Caterpillar at \$21.00 per share. These shares were subject to an acceleration notice issued to Caterpillar by the Company in October 2003 in connection with the warrant held by Caterpillar.

Also in January 2004, the Company repurchased the remaining warrant held by Caterpillar for a cash payment of \$7.2 million and the issuance of 500,000 shares of the Company's common stock. As of February 27, 2004, Caterpillar owned 24.8% of the Company's outstanding common stock.

Cash Requirements

The Company believes cash expected to be generated from operations, cash generated from the sale of stock to Caterpillar in January 2004, its existing cash and short-term investments, together with its available, unused \$10 million credit line, will satisfy the Company's projected working capital needs and other cash requirements for the next twelve months and for the foreseeable future.

Forward-Looking Statements

The statements set forth above under "Liquidity and Capital Resources" and elsewhere in this Annual Report regarding ASV's future sales levels, product mix, profitability, expense levels and liquidity are forward-looking statements based on current expectations and assumptions, and entail various risks and uncertainties that could cause actual results to differ materially from those expressed in such forward-looking statements. Certain factors may affect whether these anticipated events occur including ASV's ability to successfully manufacture the machines, unanticipated delays, costs or other difficulties in the development and manufacture of the machines, market acceptance of the machines, general market conditions, corporate developments at ASV or Caterpillar and ASV's ability to realize the anticipated benefits from its alliances with Caterpillar. Any forward-looking statements provided from time-to-time by the Company represent only management's then-best current estimate of future results or trends. Additional information regarding these risk factors and uncertainties is detailed in the Risk Factors filed as Exhibit 99 to the Company's Current Report on Form 10-Q for the period ended June 30, 2003.

Off-Balance Sheet Arrangements

The Company has the following off-balance sheet arrangement as of December 31, 2003:

To assist one of its customers in obtaining financing from a non-affiliated finance company to pay a portion of its accounts receivable balance owed to the Company, the Company has guaranteed the repayment of a \$589,000 note to the finance company. The Company has computed the value of the guarantee at \$35,000 and has recorded this amount as a reduction of net sales for the year ended December 31, 2003. A similar amount has been included in other accrued liabilities at December 31, 2003.

Quantitative and Qualitative Disclosures About Market Risk

The Company has no history of, and does not anticipate in the future, investing in derivative financial instruments, derivative commodity instruments or other such financial instruments. Transactions with international customers are entered into in US dollars, precluding the need for foreign currency hedges. Additionally, the Company invests in money market funds and fixed rate U.S. government and corporate obligations, which experience minimal volatility. Thus, the exposure to market risk is not material.

Consolidated Balance Sheets

A.S.V., Inc. • December 31, 2003 and 2002

ASSETS	<u>2003</u>	<u>2002</u>
CURRENT ASSETS		
Cash and cash equivalents	\$ 29,402,756	\$ 4,058,091
Short-term investments	305,662	739,307
Accounts receivable (net of allowance for doubtful accounts of \$150,000 in 2003; \$75,000 in 2002)	16,484,603	14,397,958
Inventories	26,686,707	31,834,620
Other current assets	<u>3,614,506</u>	<u>1,099,685</u>
Total current assets	76,494,234	52,129,661
PROPERTY AND EQUIPMENT, net	<u>6,129,922</u>	<u>5,080,536</u>
	<u>\$ 82,624,156</u>	<u>\$ 57,210,197</u>
LIABILITIES AND SHAREHOLDERS' EQUITY		
CURRENT LIABILITIES		
Current portion of long-term liabilities	\$ 136,414	\$ 129,550
Accounts payable	6,004,890	2,838,370
Accrued liabilities		
Compensation	372,027	265,649
Warranty reimbursements	491,100	555,200
Warranties	850,000	600,000
Other	<u>645,346</u>	<u>374,707</u>
Total current liabilities	8,499,777	4,763,476
LONG-TERM LIABILITIES, less current portion	1,844,858	1,979,798
COMMITMENTS AND CONTINGENCIES	-	-
SHAREHOLDERS' EQUITY		
Capital stock, \$.01 par value:		
Preferred stock, 11,250,000 shares authorized; no shares issued or outstanding	-	-
Common stock, 33,750,000 shares authorized; shares issued and outstanding - 11,053,588 in 2003; 10,063,901 in 2002	110,536	100,639
Additional paid-in capital	51,751,723	38,666,925
Retained earnings	<u>20,417,262</u>	<u>11,699,359</u>
	<u>72,279,521</u>	<u>50,466,923</u>
	<u>\$ 82,624,156</u>	<u>\$ 57,210,197</u>

The accompanying notes are an integral part of these financial statements

Consolidated Statements of Earnings

A.S.V., Inc. • December 31, 2003, 2002 and 2001

	<u>2003</u>	<u>2002</u>	<u>2001</u>
Net sales	\$ 96,386,576	\$ 44,236,876	\$ 50,081,376
Cost of goods sold	<u>75,895,524</u>	<u>35,614,846</u>	<u>41,025,009</u>
Gross profit	20,491,052	8,622,030	9,056,367
Operating expenses			
Selling, general and administrative	6,177,324	5,029,307	5,857,867
Research and development	<u>794,729</u>	<u>1,802,960</u>	<u>2,645,476</u>
Operating income	13,518,999	1,789,763	553,024
Other income (expense)			
Interest expense	(129,359)	(126,098)	(146,031)
Interest income	140,366	119,712	400,202
Other, net	<u>37,897</u>	<u>144,752</u>	<u>128,473</u>
Income before income taxes	13,567,903	1,928,129	935,668
Provision for income taxes	<u>4,850,000</u>	<u>575,000</u>	<u>180,000</u>
NET EARNINGS	<u>\$ 8,717,903</u>	<u>\$ 1,353,129</u>	<u>\$ 755,668</u>
Net earnings per common share			
Basic	<u>\$.85</u>	<u>\$.13</u>	<u>\$.07</u>
Diluted	<u>\$.78</u>	<u>\$.13</u>	<u>\$.07</u>
Weighted average number of common shares outstanding			
Basic	<u>10,218,793</u>	<u>10,170,645</u>	<u>10,215,855</u>
Diluted	<u>11,185,683</u>	<u>10,229,057</u>	<u>10,352,468</u>

The accompanying notes are an integral part of these financial statements

Consolidated Statements of Changes in Shareholders' Equity

A.S.V., Inc. • Years ended December 31, 2003, 2002 and 2001

	Common stock		Additional paid-in capital	Retained earnings	Total
	Shares	Amount			
Balance at December 31, 2000	10,209,997	\$ 102,100	\$40,070,685	\$9,590,562	\$49,763,347
Exercise of stock options	21,863	219	129,609	-	129,828
Tax benefit from exercise of stock options	-	-	55,000	-	55,000
Cost of shares retired	(26,554)	(266)	(270,694)	-	(270,960)
Warrant earned	-	-	138,600	-	138,600
Net earnings	-	-	-	755,668	755,668
Balance at December 31, 2001	10,205,306	102,053	40,123,200	10,346,230	50,571,483
Exercise of stock options	18,000	180	64,449	-	64,629
Cost of shares retired	(159,405)	(1,594)	(1,520,724)	-	(1,522,318)
Net earnings	-	-	-	1,353,129	1,353,129
Balance at December 31, 2002	10,063,901	100,639	38,666,925	11,699,359	50,466,923
Exercise of stock options and warrant, net	1,230,192	12,302	13,753,231	-	13,765,533
Tax benefit from exercise of stock options and warrant	-	-	5,597,000	-	5,597,000
Cost of shares retired	(240,505)	(2,405)	(6,265,433)	-	(6,267,838)
Net earnings	-	-	-	8,717,903	8,717,903
Balance at December 31, 2003	<u>11,053,588</u>	<u>\$ 110,536</u>	<u>\$51,751,723</u>	<u>\$20,417,262</u>	<u>\$72,279,521</u>

The accompanying notes are an integral part of these financial statements

Consolidated Statements of Cash Flows

A.S.V., Inc. • Years ended December 31, 2003, 2002 and 2001

	2003	2002	2001
Cash flows from operating activities:			
Net earnings	\$ 8,717,903	\$ 1,353,129	\$ 755,668
Adjustments to reconcile net earnings to net cash provided by (used in) operating activities:			
Depreciation and amortization	687,363	474,583	441,684
Deferred income taxes	(747,000)	232,000	(25,000)
Warrant earned	-	-	138,600
Tax benefit from stock option exercises	5,597,000	-	55,000
Changes in assets and liabilities:			
Accounts receivable	(2,086,645)	2,430,531	(6,270,582)
Inventories	5,147,913	(3,220,567)	(549,055)
Other current assets	(1,767,821)	158,381	(256,818)
Accounts payable	3,166,520	389,226	626,232
Accrued liabilities	562,917	(500,899)	1,272,531
Income taxes	-	(238,284)	(201,959)
Net cash provided by (used in) operating activities	<u>19,278,150</u>	<u>1,078,100</u>	<u>(4,013,699)</u>
Cash flows from investing activities:			
Purchase of property and equipment	(1,736,749)	(760,541)	(580,144)
Purchase of short-term investments	(305,662)	(734,217)	(1,766,960)
Redemption of short-term investments	<u>739,307</u>	<u>720,159</u>	<u>2,319,993</u>
Net cash used in investing activities	<u>(1,303,104)</u>	<u>(774,599)</u>	<u>(27,111)</u>
Cash flows from financing activities:			
Proceeds from long-term liabilities	-	98,363	-
Principal payments on long-term liabilities	(128,076)	(107,675)	(80,328)
Proceeds from exercise of stock options and warrant	13,765,533	64,629	129,828
Retirement of common stock	<u>(6,267,838)</u>	<u>(1,522,318)</u>	<u>(270,960)</u>
Net cash provided by (used in) financing activities	<u>7,369,619</u>	<u>(1,467,001)</u>	<u>(221,460)</u>
Net increase (decrease) in cash and cash equivalents	<u>25,344,665</u>	<u>(1,163,500)</u>	<u>(4,262,270)</u>
Cash and cash equivalents at beginning of year	<u>4,058,091</u>	<u>5,221,591</u>	<u>9,483,861</u>
Cash and cash equivalents at end of year	<u>\$ 29,402,756</u>	<u>\$ 4,058,091</u>	<u>\$ 5,221,591</u>
Supplemental disclosure of cash flow information:			
Cash paid for interest	\$ 125,890	\$ 158,437	\$ 180,640
Cash paid for income taxes	\$ 1,588,252	\$ 1,112,000	\$ 390,765

The accompanying notes are an integral part of these financial statements

Notes to Consolidated Financial Statements

A.S.V., Inc. • Years ended December 31, 2003, 2002 and 2001

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The Company designs and manufactures track-driven, all-season vehicles and related accessories and attachments in northern Minnesota. The Company sells its products through Caterpillar dealers in the United States and Canada and independent dealers in the United States, Canada, Australia, New Zealand and Portugal.

A summary of the significant accounting policies consistently applied in the preparation of the accompanying consolidated financial statements follows:

Principles of Consolidation

The consolidated financial statements include the accounts of A.S.V., Inc. and its wholly-owned subsidiary. All intercompany accounts and transactions have been eliminated in consolidation.

Revenue Recognition

The Company generally recognizes revenue on its product sales when persuasive evidence of an arrangement exists, delivery has occurred, the price is fixed or determinable and collectibility is reasonably assured. The Company generally obtains oral or written purchase authorizations from customers for a specified amount of product at a specified price and considers delivery to have occurred at the time of shipment.

Fair Value of Financial Instruments

The financial statements include the following financial instruments: cash equivalents, short-term investments, accounts receivable, accounts payable and bank debt. At December 31, 2003 and 2002, the fair values of these financial instruments are not significantly different than their balance sheet carrying amounts.

Cash Equivalents

All highly liquid temporary cash investments with an original maturity of three months or less are considered to be cash equivalents. At December 31, 2003 and 2002, the Company had cash equivalents of approximately \$24,828,000 and \$3,992,000, which consisted of two money market accounts and various tax-exempt cash equivalents. The fair value of these investments approximates cost. The Company maintains cash balances at two financial institutions and, at times, these balances may be in excess of federally insured limits.

Accounts Receivable

The Company grants credit to customers in the normal course of business. Management performs on-going credit evaluations of customers. The Company determines its allowance by considering a number of factors, including the length of time trade accounts receivable are past due, the Company's previous loss history, the customer's current ability to pay its obligation to the Company, and the condition of the general economy and the industry as a whole. The Company writes-off accounts receivable when they become uncollectible, and payments subsequently received on such receivables are credited to the allowance for doubtful accounts.

Changes in the Company's allowance for doubtful accounts are as follows:

	<u>December 31,</u>	
	<u>2003</u>	<u>2002</u>
Balance, beginning of year	\$ 75,000	\$ 75,000
Bad debt expense	144,587	89,796
Accounts written off	<u>(69,587)</u>	<u>(89,796)</u>
Balance, end of year	<u>\$ 150,000</u>	<u>\$ 75,000</u>

Included in accounts receivable at December 31, 2003 is a note receivable for approximately \$867,000 from a customer. The note bears interest at prime plus 2% (effective rate of 6.0% at December 31, 2003) and is due in 60 monthly installments beginning February 2004.

Inventories

Inventories are stated at the lower of cost (determined using the first-in, first-out method) or market. Adjustments of slow moving and obsolete inventories to the lower of cost or market are provided based on historical experience and current product demand.

Property and Equipment

Property and equipment are carried at cost. Depreciation is provided in amounts sufficient to relate the cost of depreciable assets to operations over their estimated service lives. Buildings and improvements are depreciated over periods of 18 to 39 years using the straight-line method. Tooling, machinery and equipment, and vehicles are depreciated over periods of 3 to 20 years using straight-line and accelerated methods. Accelerated methods are used for income tax purposes.

Notes to Consolidated Financial Statements - continued

A.S.V., Inc. • Years ended December 31, 2003, 2002 and 2001

NOTE A - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES - Continued

Warranties

The Company provides a limited warranty to its customers. Provision for estimated warranty costs are recorded when revenue is recognized based on estimated product failure rates, material usage and service delivery costs incurred in correcting a product failure. Should actual failure rates, material usage or service delivery costs differ from the Company's estimates, revisions to the warranty liability may be required.

Changes in the Company's warranty liability are as follows:

	December 31,	
	2003	2002
Balance, beginning of year	\$ 600,000	\$ 500,000
Expense for new warranties issued	1,083,269	1,399,950
Warranty claims	<u>(833,269)</u>	<u>(1,299,950)</u>
Balance, end of year	<u>\$ 850,000</u>	<u>\$ 600,000</u>

During the fourth quarter of 2001, ASV negotiated a warranty reimbursement program with one of its suppliers, whereby the Company receives product at no cost over a three-year period to compensate for warranty claims incurred during 2001. During 2003 and 2002, ASV recognized a benefit of \$47,200 and \$324,700 under this program, recorded as an offset to warranty expense.

Advertising Expense

Advertising is expensed as incurred. Advertising expenses were approximately \$388,000, \$308,000 and \$295,000 for 2003, 2002 and 2001.

Shipping and Handling Costs

The Company includes shipping and handling (including warehousing) costs incurred in connection with the distribution of replacement parts in selling, general and administrative expenses. Shipping and handling costs were approximately \$1,018,000, \$838,000 and \$832,000 for 2003, 2002 and 2001.

Research and Development

All research and development costs are expensed as incurred.

Employee Savings and Profit Sharing Plan

The Company has an employee savings and profit sharing plan which permits participant salary deferrals up to certain limits set by law and provides for discretionary Company contributions. The Plan covers employees who have completed three months of service, as defined in the Plan, and who have attained the age of 20 and one-half. Company contributions were approximately \$49,000, \$42,000 and \$41,000 for 2003, 2002 and 2001.

Stock-Based Compensation

At December 31, 2003, the Company has three stock-based compensation plans, which are described more fully in Note I. The Company accounts for those plans under the recognition and measurement principles of APB Opinion No. 25, Accounting for Stock Issued to Employees, and related Interpretations. No stock-based employee compensation cost is reflected in net earnings, as all options granted under those plans had an exercise price equal to the market value of the underlying common stock on the date of grant.

The following table illustrates the effect on net earnings and earnings per share if the Company had applied the fair value recognition provisions of FASB Statement No. 123, Accounting for Stock-Based Compensation, using the assumptions described in Note I, to its stock-based compensation plans.

	Year ended December 31,		
	2003	2002	2001
Net earnings, as reported	\$8,717,903	\$1,353,129	\$755,668
Deduct: Total stock-based employee compensation determined under fair value based methods for all awards	<u>792,140</u>	<u>496,648</u>	<u>493,672</u>
Pro forma net earnings	<u>\$7,925,763</u>	<u>\$ 856,481</u>	<u>\$261,996</u>
Earnings per share:			
Basic - as reported	<u>\$0.85</u>	<u>\$0.13</u>	<u>\$0.07</u>
Basis - pro forma	<u>\$0.78</u>	<u>\$0.08</u>	<u>\$0.03</u>
Diluted - as reported	<u>\$0.78</u>	<u>\$0.13</u>	<u>\$0.07</u>
Diluted - pro forma	<u>\$0.71</u>	<u>\$0.08</u>	<u>\$0.03</u>

Net Earnings Per Common Share

Basic net earnings per share is computed by dividing net earnings by the weighted average number of outstanding common shares. Diluted net earnings per share is computed by dividing net earnings by the weighted average number of outstanding common shares and common share equivalents relating to stock options and warrants, when dilutive.

For the years ended December 31, 2003, 2002 and 2001, 966,890, 58,412 and 136,613 shares of common stock equivalents were included in the computation of diluted net earnings per share. Options and warrants to purchase 11,166,939 and 11,229,876 shares of common stock with a weighted average exercise price of \$20.10 and \$20.13 were outstanding at December 31, 2002 and 2001, but were excluded from the computation of common share equivalents because they were anti-dilutive. There were no anti-dilutive options or warrants outstanding at December 31, 2003.

Accounting Estimates

Preparing consolidated financial statements in conformity with accounting principles generally accepted in the United States of America requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, related revenues and expenses and disclosure of contingent assets and liabilities at the date of the financial statements. Actual results could differ from these estimates.

Reclassifications

Certain 2002 and 2001 amounts have been reclassified to conform to the 2003 presentation.

NOTE B - SHORT-TERM INVESTMENTS

Short-term investments consist primarily of a diversified portfolio of taxable governmental agency bonds, which will mature in 2003. The Company considers the investments as "available-for-sale." At December 31, 2003 and 2002, cost was equal to fair value and no amount was included as a separate component of shareholders' equity.

NOTE C - INVENTORIES

Inventories consist of the following:

	<u>December 31,</u>	
	<u>2003</u>	<u>2002</u>
Raw materials, service parts and work-in-process	\$16,589,121	\$16,502,994
Finished goods	7,385,768	10,779,010
Used equipment held for resale	<u>2,711,818</u>	<u>4,552,616</u>
	<u>\$26,686,707</u>	<u>\$31,834,620</u>

NOTE D - PROPERTY AND EQUIPMENT

Property and equipment consist of the following:

	<u>December 31,</u>	
	<u>2003</u>	<u>2002</u>
Land	\$ 353,134	\$ 132,635
Buildings and improvements	4,337,899	3,695,152
Tooling	1,730,110	1,182,839
Machinery and equipment	2,366,611	2,146,664
Vehicles	<u>310,400</u>	<u>409,739</u>
	9,098,154	7,567,029
Less accumulated depreciation	<u>2,968,232</u>	<u>2,486,493</u>
	<u>\$ 6,129,922</u>	<u>\$ 5,080,536</u>

NOTE E - LINE OF CREDIT

The Company has a \$10,000,000 line of credit agreement with a bank which is due on demand or July 1, 2004. The interest rate is variable at prime less one half percent (effective rates of 3.50% and 3.75% as of December 31, 2003 and 2002). As of December 31, 2003 and 2002, there were no advances on this line of credit. Any advances made under this line of credit are secured by accounts receivable and inventories. The agreement requires the Company to maintain certain financial requirements including a minimum tangible net worth level and a cash flow coverage ratio and restricts the Company from paying cash dividends. Management expects to renew the agreement at substantially the same terms and conditions.

Notes to Consolidated Financial Statements - continued

A.S.V., Inc. • Years ended December 31, 2003, 2002 and 2001

NOTE F - LONG-TERM LIABILITIES

Capital Lease Obligation

The Company leases its manufacturing and office building from the Grand Rapids Economic Development Authority. The agreement provides for monthly payments to 2018 and a balloon payment of approximately \$543,000 in December 2006.

Future minimum lease payments under this capital lease obligation at December 31, 2003 are as follows:

2004	\$ 228,134
2005	228,134
2006	766,132
2007	135,554
2008	135,554
Thereafter	<u>986,424</u>
Total payments	2,479,932
Amounts representing interest (weighted average 6.00%)	<u>574,070</u>
Present value of minimum capitalized lease payments	<u>\$1,905,862</u>

Asset cost related to the capital lease were \$2,250,773 at December 31, 2003 and 2002. Accumulated amortization was \$387,874 and \$331,603 at December 31, 2003 and 2002.

NOTE G - PROVISION FOR INCOME TAXES

The provision for income taxes consists of the following:

	Year ended December 31,		
	2003	2002	2001
Current			
Federal	\$5,143,000	\$301,000	\$138,000
State	<u>454,000</u>	<u>42,000</u>	<u>67,000</u>
	5,597,000	343,000	205,000
Deferred	<u>(747,000)</u>	<u>232,000</u>	<u>(25,000)</u>
	<u>\$4,850,000</u>	<u>\$575,000</u>	<u>\$180,000</u>

Net deferred income tax assets (liabilities) relate to the tax effect of temporary differences as follows:

	December 31,	
	2003	2002
Accruals and reserves	\$ 230,000	\$ 292,000
Net operating loss carryforwards	1,250,000	--
Other	<u>(405,000)</u>	<u>36,000</u>
	<u>\$1,075,000</u>	<u>\$ 328,000</u>

The net deferred tax asset is included in other current assets in the financial statements.

The following is a reconciliation of the Federal statutory income tax rate to the effective tax rate:

	2003	2002	2001
Statutory federal rate	34.0%	34.0%	34.0%
State income taxes, net of federal benefit	2.9	3.6	4.7
Research and development tax credit	(0.4)	(4.9)	(16.9)
Foreign tax credit	(0.3)	(2.8)	(4.2)
Other	<u>(0.5)</u>	<u>(0.1)</u>	<u>1.6</u>
	<u>35.7%</u>	<u>29.8%</u>	<u>19.2%</u>

The Company realizes an income tax benefit from the exercise or early disposition of certain stock options. This benefit results in a decrease in current income taxes payable and an increase in additional paid-in capital.

The Company generated and fully utilized research and development and foreign tax credits during 2003, 2002 and 2001.

At December 31, 2003, the Company has federal and state net operating loss carryforwards totaling approximately \$4,488,000, which will begin to expire in 2023.

NOTE H - TRANSACTIONS WITH CATERPILLAR

Prior to 2000, the Company entered into a Securities Purchase Agreement (the Agreement) with Caterpillar Inc. (Caterpillar). Under the terms of the Agreement, Caterpillar acquired, for an aggregate purchase price of \$18,000,000, one million newly issued shares of common stock and a warrant to purchase an additional 10,267,127 newly issued shares of common stock at a price of \$21.00 per share. The warrant is exercisable at any time through January 2009 subject to partial termination in the event the Company achieves certain financial goals.

As a result of the Agreement, the board of directors was increased with two members appointed by Caterpillar. In addition, the Agreement contains other provisions which allow Caterpillar to maintain its proportionate potential ownership and restricts acquisitions, loans and the payment of dividends, without approval of at least one of the Caterpillar designated members of the Board.

NOTE H - TRANSACTIONS WITH CATERPILLAR - Continued

The Company and Caterpillar also entered into a Commercial Alliance Agreement pursuant to which Caterpillar will provide the Company with access to its dealer network and will make various management, financial and engineering resources available to the Company. Included in the Commercial Alliance Agreement is a Marketing Agreement which provides, among other things, that the Company will pay Caterpillar a commission equal to 5% of the dealer net price for complete machines and 3% for replacement parts and Company-branded attachments for all sales made to Caterpillar dealers. In addition, if the Company's products are sold under the Caterpillar brand name, the Company will pay Caterpillar a trademark license fee equal to 3% of the net sales of these products to Caterpillar dealers. The Company and Caterpillar also entered into other ancillary agreements for the benefit of both companies. Total commission expense under the agreement was approximately \$88,000, \$215,000 and \$464,000 in 2003, 2002 and 2001.

In October 2000, the Company completed another Securities Purchase Agreement with Caterpillar in which Caterpillar purchased 500,000 newly issued shares of common stock at a price of \$18.00 per share.

The Company also amended its original warrant issued to Caterpillar reducing the number of shares of Company common stock available for purchase under the original warrant by 500,000 shares.

Also in October 2000, the Company and Caterpillar entered into an alliance agreement to jointly develop and manufacture a new product line of Caterpillar rubber track skid steer loaders called Multi-Terrain Loaders, or MTLs. The product line, which includes five models, will feature Caterpillar's patented skid steer loader technology and ASV's patented Maximum Traction Support System™ rubber track undercarriage. The MTLs are being sold through the Caterpillar dealer network. The Company is manufacturing the undercarriage for use on four of the MTLs, with the development of the undercarriage for the remaining model continuing.

In connection with this alliance agreement, the Company has agreed to reimburse Caterpillar for their research and development costs related to the MTLs as it pertains to the combination of the Caterpillar portion of the machines with the Company's undercarriages. Total research and development costs reimbursed to Caterpillar were approximately \$1,000,000 and \$1,904,000 in 2002 and 2001. There were no research and development costs reimbursed to Caterpillar in 2003.

At December 31, 2003, Caterpillar owned approximately 14% of the Company's outstanding common stock and had the right to own up to approximately 52% of the Company's common stock (assuming the exercise of all outstanding options and warrants) upon exercise of the amended warrant.

See Note N for January 2004 transactions relating to Caterpillar's ownership.

The Company purchases parts used in its products from Caterpillar. The Company also reimburses Caterpillar for the salary related costs of two Caterpillar employees that work on the Company's behalf. In addition, the Company utilizes Caterpillar's warranty processing system to handle warranty claims on its machines and reimburses Caterpillar for the warranty expense incurred by Caterpillar dealers. During 2003, 2002 and 2001, total parts purchases, salary and warranty reimbursements were approximately \$3,994,000, \$7,140,000 and \$6,877,000. Also, at December 31, 2003 and 2002, accounts payable to Caterpillar were approximately \$637,000 and \$1,213,000.

When the Company ships undercarriages to Caterpillar it recognizes as sales its cost for the undercarriage, as defined in the agreement, plus a portion of the anticipated gross profit that Caterpillar expects to recognize upon sale of the MTL to Caterpillar dealers.

During 2003, 2002 and 2001, 54%, 32% and 18% of net sales were made to Caterpillar. At December 31, 2003 and 2002, the accounts receivable balance due from Caterpillar was approximately \$3,800,000 and \$2,000,000.

NOTE I - SHAREHOLDERS' EQUITY**Stock Option Plans**

The Company has two stock option plans under which up to 3,375,000 shares of common stock are available for issuance. Stock options may be granted to any employee, including officers and directors of the Company, and certain non-employees, at a price not less than the fair market value of the Company's common stock on the date of grant. Options generally expire seven years from the date of grant. Options granted under the plans are generally exercisable in annual installments, beginning one year from the date of grant.

Notes to Consolidated Financial Statements - continued

A.S.V., Inc. • Years ended December 31, 2003, 2002 and 2001

NOTE I - SHAREHOLDERS' EQUITY - Continued

Director Stock Option Plan

The Company also has a stock option plan under which 450,000 shares of common stock are available for issuance. Stock options may be granted to directors who are not employees of the Company at a price not less than the fair market value of the Company's common stock on the date of grant. Options expire five years from date of grant and are exercisable in annual installments, beginning one year from the date of grant.

The plan, as amended, provides that each eligible director shall receive an option to purchase 3,000 shares on the first business day of each calendar year.

Option transactions under the plans during each of the three years in the period ended December 31, 2003 are summarized as follows:

	Shares	Weighted Average Exercise Price
Outstanding at		
December 31, 2000	1,388,364	\$14.21
Granted	143,500	11.71
Exercised	(21,863)	5.93
Canceled	<u>(63,250)</u>	13.46
Outstanding at		
December 31, 2001	1,446,751	14.12
Granted	159,500	10.95
Exercised	(18,000)	3.59
Canceled	<u>(165,189)</u>	16.11
Outstanding at		
December 31, 2002	1,423,062	13.67
Granted	534,750	8.83
Exercised	(892,692)	12.65
Canceled	<u>(7,000)</u>	9.86
Outstanding at		
December 31, 2003	<u>1,058,120</u>	<u>\$12.19</u>

At December 31, 2003, 2002 and 2001, 384,250, 1,145,937 and 1,205,501 options were exercisable with a weighted average exercise price of \$16.85, \$14.00 and \$14.20.

The following information applies to grants that are outstanding at December 31, 2003:

Range of exercise prices	Options outstanding		
	Number outstanding at period end	Weighted average remaining contractual life	Weighted- average exercise price
\$ 8.09-12.00	637,870	5.78	\$ 9.18
\$ 12.25-18.33	<u>420,250</u>	1.65	16.77
	<u>1,058,120</u>		<u>\$ 12.19</u>

Range of exercise prices	Options exercisable	
	Number exercisable at period end	Weighted- average exercise price
\$ 8.09-12.00	28,500	\$ 10.68
\$ 12.25-18.33	<u>355,750</u>	17.35
	<u>384,250</u>	<u>\$ 16.85</u>

The weighted average fair values of the options granted during 2003, 2002 and 2001 are \$4.52, \$5.47 and \$6.34. The fair value of each option grant is estimated on the date of grant using the Black-Scholes options-pricing model with the following weighted-average assumptions used for all grants in 2003, 2002 and 2001; zero dividend yield; expected volatility of 44.8%, 40.8% and 47.3%, risk-free interest rate of 3.55%, 4.71% and 4.33% and expected lives of 6.95, 6.85 and 6.79 years.

Shares Repurchased and Retired

In October 2003, the Company authorized a new stock buy-back program under which the Company may repurchase up to \$10,000,000 of its common stock on the open market. The Company is funding the repurchases with available funds. The repurchase program is not expected to last more than twelve months or until such amount of common stock is repurchased. No shares had been repurchased under this plan at December 31, 2003.

During 2003, 2002 and 2001, in connection with previous repurchase agreements, the Company repurchased 13,100, 159,405 and 26,554 shares of stock for total consideration of \$247,801, \$1,522,318 and \$270,960.

NOTE J - RELATED PARTY TRANSACTION

The Company uses a public relations firm that is affiliated with one of the Company's directors. Total fees paid to this firm in 2003, 2002 and 2001 were approximately \$157,000, \$188,000 and \$202,000.

NOTE K - CONSULTING AGREEMENT

The Company entered into a five year consulting agreement and issued a ten year warrant for the purchase of 337,500 shares of the Company's common stock at \$7.33 per share, expiring December 1, 2006. Subsequently, an individual who contracts with the consulting firm was appointed a member of the Board of Directors. The warrant was exercised in full in December 2003.

A fair value of \$2.24 per share for this warrant was calculated on the date of grant using the average of the Black-Scholes and Shelton options-pricing models. Compensation costs were amortized over the life of the consulting agreement of \$138,600 in 2001. The compensation cost was fully amortized in 2001.

NOTE L - COMMITMENTS AND CONTINGENCIESLease Residual Guarantee

The Company has guaranteed certain residual amounts of equipment financed by customers, generally 25% of the financed amount at the end of four years. Should the Company be required to make this payment, it will take title of the financed equipment. As of December 31, 2003, the total amount of future residual payments the Company may be required to make in the event of nonpayment by the customer was approximately \$100,000. The Company believes the value of the acquired equipment will equal or exceed the amount of residual payment. Accordingly, the Company does not anticipate any loss will be incurred should any residual payment need to be made.

Financing Guarantee

The Company has guaranteed the repayment of a \$589,000 note made by one of its customers to a non-affiliated finance company in payment of amounts owed to the Company by this customer. The Company has computed the value of the guarantee at \$35,000 and has recorded this amount as a reduction of net sales for the year ended December 31, 2003. A similar amount has been included in other accrued liabilities at December 31, 2003.

NOTE M - MAJOR CUSTOMERS AND SUPPLIERS

Other than sales to Caterpillar (see note H), the Company had sales to one unaffiliated customer in 2001, which accounted for 16% of sales. No other customers accounted for over 10% of sales in the years presented. At December 31, 2001, the accounts receivable balance from the unaffiliated customer was approximately \$706,000.

While current vendors are meeting the Company's quality and performance expectations, the Company believes alternative contract manufacturers are available should the necessity arise. However, shortages of parts or the need to change vendors could result in production delays or reductions in product shipments that could adversely affect the Company's business. The Company believes that a change in suppliers for the majority of component parts could occur without material disruption of the Company's business. However, certain parts, such as bogie wheels and rubber tracks, have a limited number of vendors and a disruption in supply could affect the Company's ability to deliver finished goods.

NOTE N - SUBSEQUENT EVENTS

In January 2004, the Company sold 1,040,069 shares of its common stock to Caterpillar at \$21.00 per share. These shares were subject to an acceleration notice issued to Caterpillar by the Company in October 2003 in connection with the warrant held by Caterpillar. (See Note H)

Also in January 2004, the Company repurchased the remaining warrant held by Caterpillar for a cash payment of \$7.2 million and the issuance of 500,000 shares of the Company's common stock. As a result of these transactions, Caterpillar owns 24.9% of the Company's outstanding common stock.

Notes to Consolidated Financial Statements - continued

A.S.V., Inc. • Years ended December 31, 2003, 2002 and 2001

NOTE 0 - SUPPLEMENTARY FINANCIAL INFORMATION

(unaudited)

The following table summarizes quarterly, unaudited financial data for 2003 and 2002.

Quarters	2003			
	1st	2nd	3rd	4th
<i>(Dollars in thousands, except per share data)</i>				
Net sales	\$ 14,612	\$ 26,414	\$ 29,189	\$ 26,171
Gross profit	2,804	5,332	6,512	5,843
Net earnings	768	2,285	3,079	2,585
Net earnings per common share				
Basic	.08	.23	.30	.24
Diluted	.08	.22	.29	.19

Quarters	2002			
	1st	2nd	3rd	4th
<i>(Dollars in thousands, except per share data)</i>				
Net sales	\$6,178	\$14,714	\$11,475	\$11,870
Gross profit	1,425	3,472	2,122	1,603
Net earnings (loss)	(366)	1,014	527	178
Net earnings (loss) per common share				
Basic	(.04)	.10	.05	.02
Diluted	(.04)	.10	.05	.02

Report of Independent Certified Public Accountants

A.S.V., Inc. -Years ended December 31, 2003, 2002 and 2001

Grant Thornton

Board of Directors
A.S.V., Inc.

We have audited the accompanying consolidated balance sheets of A.S.V., Inc. as of December 31, 2003 and 2002, and the related consolidated statements of earnings, changes in shareholders' equity, and cash flows for each of the three years in the period ended December 31, 2003. 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 of America. 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 consolidated financial statements referred to above, present fairly, in all material respects, the financial position of A.S.V., Inc. as of December 31, 2003 and 2002, and the results of its operations and its cash flows for each of the three years in the period ended December 31, 2003, in conformity with accounting principles generally accepted in the United States of America.

Grant Thornton LLP

Minneapolis, Minnesota
February 20, 2004

Directors and Officers

A.S.V., Inc.

Directors:

Gary D. Lemke

Chairman of the Board
President

Jerome T. Miner (1)(2)

Vice-Chairman of the Board
President
Jerry Miner Realty, Inc.
Grand Rapids, Minnesota

Edgar E. Hetteen

Vice President, Secretary

Leland T. Lynch

Chief Executive Officer
Carmichael Lynch, Inc.
Minneapolis, Minnesota

James H. Dahl (1)

President
James Dahl & Company
(Private Investments)
Jacksonville, Florida

R. E. "Teddy" Turner IV (1)(2)

Owner
Charleston Boatworks, Inc.
Charleston, South Carolina

Richard A. Benson

Vice President
Caterpillar Inc.
Peoria, Illinois

- (1) Audit Committee
- (2) Compensation and Stock
Option Committee

Executive Officers:

Gary D. Lemke

President

Edgar E. Hetteen

Vice President, Secretary

Thomas R. Karges

Chief Financial Officer

Corporate Headquarters:

A.S.V., Inc.

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South St. Paul, Minnesota 55075
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Corporate Counsel:

Dorsey & Whitney LLP

Minneapolis, Minnesota

Independent Auditor:

Grant Thornton LLP

Minneapolis, Minnesota

Investor Information

A.S.V., Inc.

Common Stock Information:

The Company's common stock is traded on the Nasdaq Stock Market® under the symbol "ASVI."

Common Stock High and Low Sale Price

Year Ended December 31, 2003

	High	Low
First Quarter	\$ 11.20	\$ 7.60
Second Quarter	15.55	10.41
Third Quarter	20.60	13.85
Fourth Quarter	37.99	19.02

Year Ended December 31, 2002

	High	Low
First Quarter	\$ 13.70	\$ 10.50
Second Quarter	12.70	10.80
Third Quarter	11.80	7.90
Fourth Quarter	10.20	6.55

The quotations above reflect the high and low inter-dealer bid prices, without retail markup, markdown or commissions.

As of April, 2004, there were approximately 210 shareholders of record holding shares of A.S.V., Inc. common stock. This number does not include shareholders who hold A.S.V., Inc. common stock in street name.

Dividend Policy

A.S.V., Inc. has never declared or paid a cash dividend on its common stock. The Company currently intends to retain earnings for use in the operation and expansion of its business.

Trademarks

Track Truck is a registered trademark and Posi-Track, RC-30, R-50, RC-50, RC-60, RC-85, RC-100, MTSS, RTSS, Posi-Turn, Posi-Tool and Snow Saver are trademarks of A.S.V., Inc.



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An Equal Opportunity Employer

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April, 2004
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