AEROCENTURY CORP
Form 10QSB
May 13, 2004

UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, DC 20549

FORM 10-QSB

(Mark One)
[X] Quarterly Report Under Section 13 or 15(d) of the Securities Exchange Act of 1934 For the quarterly period ended March 31, 2004

[ ] Transition Report Under Section 13 or 15(d) of the Securities Exchange Act of 1934 For the transition period from ____________ to ____________

Commission File Number: 001-13387

AeroCentury Corp.
(Exact name of small business issuer as specified in its charter)

Delaware	94-3263974
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

1440 Chapin Avenue, Suite 310 Burlingame, California	94010
(Address of principal executive offices)	(Zip Code)

Issuer's telephone number, including area code: (650) 340-1888

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

Title of Each Class	Name of Exchange on Which Registered
Common Stock, $0.001 par value	American Stock Exchange

Securities registered pursuant to Section 12(g) of the Act: None

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

As of May 13, 2004 the Issuer had 1,606,557 Shares of Common Stock outstanding, of which 63,300 are held as Treasury Stock.

Transitional Small Business Disclosure Format (check one): Yes No X

PART I
Financial Information

Forward-Looking Statements

This Quarterly Report on Form 10-QSB includes "forward-looking statements" within the meaning of Section 27A of the Securities Act and Section 21E of the Exchange Act. All statements in this Report other than statements of historical fact are "forward-looking statements" for purposes of these provisions, including any statements of plans and objectives for future operations and any statements of assumptions underlying any of the foregoing. Statements that include the use of terminology such as "may," "will," "expects," "plans," "anticipates," "estimates," "potential," or "continue," or the negative thereof, or other comparable terminology are forward-looking statements.

Forward-looking statements include: (i) in Item 1 "Financial Statements," statements concerning the Company's expectations with respect to the execution of a promissory note by a former lessee of the Company in the second quarter of 2004; (ii) in Item 2 "Management's Discussion and Analysis or Plan of Operation -- Liquidity and Capital Resources," statements concerning the Company's belief that it will continue to be in compliance with its credit facility covenants; the Company's belief that it will have adequate cash flow to meet its ongoing operational needs; the Company's belief that its assumptions used to forecast cash flow are reasonable; the Company's expectation regarding the long-term decline of lease rentals (iii) in Item 2 "Management's Discussion and Analysis or Plan of Operation -- Outlook," statements concerning the Company's anticipation with respect to the cost of maintenance on two DHC-7 aircraft; the Company's belief that the DHC-7 aircraft will be difficult to remarket and that a substantial amount of time will pass before the DHC-7 aircraft generate revenue; the Company's belief that it will have sufficient cash to fund any required repayments under its credit facility; and the Company's expectations with respect to the execution of a promissory note by a former lessee of the Company in the second quarter of 2004 and the adequacy of a $250,000 allowance against the estimated amount receivable under the Note; and (iv) in Item 2 "Management's Discussion and Analysis or Plan of Operation -- Factors that May Affect Future Results," statements regarding the Company's belief that it will have sufficient cash funds to make any payments that are required under the credit facility due to collateral pool limitations; the Company's intention to concentrate on future leases to regional air carriers; the Company's belief that overseas markets present opportunities; and the Company's belief that it is competitive because of JMC's experience and operational efficiency in identifying and obtaining financing for the transaction types desired by regional air carriers.

These forward-looking statements involve risks and uncertainties, and it is important to note that the Company's actual results could differ materially from those projected or assumed in such forward-looking statements. Among the factors that could cause actual results to differ materially are the factors detailed under the heading "Management's Discussion and Analysis or Plan of Operation -- Factors That May Affect Future Results," including general economic conditions, particularly those that affect the demand for regional aircraft and engines and the financial status of the Company's primary customers, foreign regional passenger airlines; lack of any further disruptions to the air travel industry similar due to terrorist attacks or wartime hostilities or catastrophic events; the success of the Company's efforts in remarketing or re-leasing aircraft that are currently or are about to come off-lease, particularly two DHC-7 aircraft; the Company's ability to renew and enlarge its credit facility on reasonable business terms at or prior to its expiration; the financial performance of the Company's lessees and their compliance with rental, maintenance and return conditions under their respective leases; the availability of suitable aircraft acquisition transactions in the regional aircraft market; and future trends and results which cannot be predicted with certainty. The cautionary statements made in this Quarterly Report should be read as being applicable to all related forward-looking statements wherever they appear herein. All forward-looking statements and risk factors included in this document are made as of the date hereof, based on information available to the Company as of the date hereof, and the Company assumes no obligation to update any forward-looking statement or risk factor. You should consult the risk factors listed from time to time in the Company's filings with the Securities and Exchange Commission.

Item 1. Financial Statements

AeroCentury Corp.
Condensed Consolidated Balance Sheet
Unaudited

ASSETS

	March 31, 2004
Assets:	
Cash and cash equivalents	$ 8,897,650
Accounts receivable, net of allowance for doubtful accounts of $250,000	1,687,280
Note receivable, net of allowance for doubtful accounts of $411,680	21,670
Aircraft and aircraft engines on operating leases, net of accumulated depreciation of $22,476,360	61,615,090
Prepaid expenses and other	539,360
Total assets	$ 72,761,050

LIABILITIES AND STOCKHOLDERS' EQUITY

Liabilities:	
Accounts payable and accrued expenses	$ 425,830
Notes payable and accrued interest	40,673,080
Maintenance reserves and accrued costs	8,650,060
Security deposits	1,475,320
Prepaid rent	192,000
Deferred taxes	2,783,830
Total liabilities	54,200,120
Stockholders' equity:	
Preferred stock, $.001 par value, 2,000,000 shares authorized, no shares issued and outstanding	-
Common stock, $.001 par value, 3,000,000 shares authorized, 1,606,557 shares issued and outstanding	1,610

Paid in capital	13,821,200
Retained earnings	5,242,190
	19,065,000
Treasury stock at cost, 63,300 shares	(504,070)
Total stockholders' equity	18,560,930
Total liabilities and stockholders' equity	$ 72,761,050

The accompanying notes are an integral part of these statements.

AeroCentury Corp.
Condensed Consolidated Statements of Operations
Unaudited

	For the Three Mont 2004
Revenues:	
Operating lease revenue	$ 2,059,800
Other income	70,230
	2,130,030
Expenses:	
Depreciation	845,080
Interest	551,140
Management fees	462,780
Professional fees and general and administrative	141,180
Insurance	74,020
Maintenance	24,780
Bad debt expense	-
	2,098,980
Income before taxes	31,050
Tax provision	930
Net income	$ 30,120

Weighted average common shares outstanding	1,543,257
Basic earnings per share	$ 0.02

The accompanying notes are an integral part of these statements.

AeroCentury Corp.
Condensed Consolidated Statements of Cash Flows
Unaudited

	For the Three Mont 2004
Net cash provided by operating activities	$ 579,330
Investing activities:	
Payments received on note receivable	-
Equipment additions to aircraft	(308,750)
Net cash (used)/provided by investing activities	(308,750)
Financing activity -	
Repayment of notes payable	(821,560)
Net cash used by financing activity	(821,560)
Net (decrease)/increase in cash and cash equivalents	(550,980)
Cash and cash equivalents, beginning of period	9,448,630
Cash and cash equivalents, end of period	$ 8,897,650

During the three months ended March 31, 2004 and 2003, the Company paid interest totaling $513,110 and $521,830, respectively, and no income taxes.

The accompanying notes are an integral part of these statements.

AeroCentury Corp.
Notes to Condensed Consolidated Financial Statements
March 31, 2004
Unaudited

1. Organization and Summary of Significant Accounting Policies

(a) Basis of Presentation

AeroCentury Corp. ("AeroCentury"), a Delaware corporation, uses leveraged financing to acquire leased aircraft assets. The Company purchases used regional aircraft on lease to foreign and domestic regional carriers. Financial information for AeroCentury and its wholly-owned subsidiary, AeroCentury Investments II LLC ("AeroCentury II LLC") (collectively, the "Company"), is presented on a consolidated basis. All intercompany balances and transactions have been eliminated in consolidation.

(b) Capitalization

In 1998, in connection with the adoption of a stockholder rights plan, the Company filed a Certificate of Designation, setting forth the rights, preferences and privileges of a new Series A Preferred Stock. Pursuant to the plan, the Company issued rights to its stockholders, giving each stockholder the right to purchase one one-hundredth of a share of Series A Preferred Stock for each share of Common Stock held by the stockholder. Such rights are exercisable only under certain circumstances concerning a proposed acquisition or merger of the Company.

As discussed above, AeroCentury is the sole member and manager of AeroCentury II LLC.

(c) Cash and Cash Equivalents/Deposits

The Company considers highly liquid investments readily convertible into known amounts of cash, with original maturities of 90 days or less, as cash equivalents. Because the Company's leases do not restrict the Company's use of such amounts, cash previously reported as deposits, representing cash balances held related to maintenance reserves and security deposits, has been reclassified to cash and cash equivalents.

(d) Aircraft and Aircraft Engines On Operating Leases

The Company's interests in aircraft and aircraft engines are recorded at cost, which includes acquisition costs. Depreciation is computed using the straight-line method over the aircraft's estimated economic life (generally assumed to be twelve years from the date of acquisition), to an estimated residual value based on appraisal.

(e) Impairment of Long-lived Assets

The Company periodically reviews its portfolio of assets for impairment in accordance with Statement of Financial Accounting Standards ("SFAS") No. 144, "Accounting for the Impairment or Disposal of Long-lived Assets." Such review necessitates estimates of current market values, residual values and component values. The estimates are based on currently available market data and are subject to fluctuation from time to time. The Company initiates its review periodically, whenever events or changes in circumstances indicate that the carrying amount of a long-lived asset may not be recoverable. Recoverability of an asset is measured by comparison of its carrying amount to the expected future undiscounted cash flows (without interest charges) that the asset is expected to generate. Any impairment to be recognized is measured by the amount by which the carrying amount of the asset exceeds its fair market value. Significant management judgment is required in the forecasting of future operating results which are used in the preparation of projected undiscounted cash flows and should different conditions prevail, material write downs may occur.

AeroCentury Corp.
Notes to Condensed Consolidated Financial Statements
March 31, 2004
Unaudited

1. Organization and Summary of Significant Accounting Policies (continued)

(f) Loan Commitment and Related Fees

To the extent that the Company is required to pay loan commitment fees and legal fees in order to secure debt, such fees are amortized over the life of the related loan.

(g) Maintenance Reserves and Accrued Costs and Security Deposits

Maintenance costs under the Company's triple net leases are generally the responsibility of the lessees. The accompanying balance sheet reflects maintenance reserves and accrued costs, which include refundable and non-refundable maintenance payments received from lessees, as well as security deposits received from lessees. The Company records a matching liability for all such amounts. At March 31, 2004, the Company had accrued liabilities for refundable maintenance reserves of $375,940, non-refundable maintenance reserves of $7,198,520 and security deposits of $1,475,320.

Maintenance reserves which are refundable to the lessee at the end of the lease may be retained by the Company if such amounts are necessary to meet the return conditions specified in the lease and, in some cases, to satisfy any other payments due under the lease.

Non-refundable maintenance reserves received by the Company are accounted for as a liability until the aircraft has been returned at the end of the lease, at which time the Company evaluates the adequacy of the remaining reserves in light of maintenance to be performed as a result of hours flown. At that time, any excess is recorded as income. When an aircraft is sold, any excess non-refundable maintenance reserves are recorded as income.

The Company periodically reviews maintenance reserves for adequacy in light of the number of hours flown, airworthiness directives issued by the manufacturer or government authority, and the return conditions specified in the lease, as well as the condition of the aircraft upon return or inspection. As a result of such review, when it is probable that the Company has incurred costs for maintenance in excess of amounts received from lessees, the Company accrues its share of costs for work to be performed as a result of hours flown. At March 31, 2004, the Company had accrued maintenance costs, in excess of reserve amounts received under the leases, of approximately $1,076,000 related to several of its aircraft.

The Company's leases are typically structured so that if any event of default occurs under a lease, the Company may apply all or a portion of the lessee's security deposit to cure such default. If such application of the security deposit is made, the lessee typically is required to replenish and maintain the full amount of the deposit during the remaining term of the lease. All of the security deposits received by the Company are refundable to the lessee at the end of the lease, upon satisfaction of all lease terms.

1. Organization and Summary of Significant Accounting Policies (continued)

(h) Income Taxes

The Company follows the liability method of accounting for income taxes. Under the liability method, deferred income taxes are recognized for the tax consequences of "temporary differences" by applying enacted statutory tax rates applicable to future years to differences between the financial statement carrying amounts and the tax bases of existing assets and liabilities. The effect on deferred taxes of a change in the tax rates is recognized in income in the period that includes the enactment date.

(i) Revenue Recognition

Revenue from leasing of aircraft assets is recognized as operating lease revenue on a straight-line basis over the terms of the applicable lease agreements. If the Company deems a portion of operating lease revenue as potentially uncollectible, the Company records an allowance for doubtful accounts.

(j) Use of Estimates

The preparation of financial statements in conformity with accounting principles generally accepted in the United States requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosures of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenues and expenses during the reporting period. Actual results could differ from those estimates.

The most significant estimates with regard to these financial statements are the residual values of the aircraft, the useful lives of the aircraft, the amount and timing of cash flow associated with each aircraft that are used to evaluate impairment, if any, accrued maintenance costs in excess of amounts received from lessees, and the amounts recorded as bad debt allowances.

(k) Comprehensive Income

The Company does not have any comprehensive income other than the revenue and expense items included in the consolidated statements of income. As a result, comprehensive income equals net income for the quarters ended March 31, 2004 and 2003.

(l) Recent Accounting Pronouncements

In November 2002, the Financial Accounting Standards Board ("FASB") issued SFAS Interpretation No. 45, "Guarantor's Accounting and Disclosure Requirements for Guarantees, Including Indirect Guarantees of Indebtedness of Others" ("FIN 45"). FIN 45 is effective for guarantees issued or modified after December 31, 2002. The Company had one guarantee, which was issued prior to December 31, 2002. During the second quarter of 2003, the Company recorded a liability for the maximum obligation it had assumed under this guarantee and wrote off the related receivable. During the fourth quarter of 2003, the vendor waived the amount due, and the Company reversed its accrual.

1. Organization and Summary of Significant Accounting Policies (continued)

(l) Recent Accounting Pronouncements (continued)

In January 2003, the FASB issued interpretation FIN No. 46, Consolidation of Variable Interest Entities ("FIN 46"), which was subsequently revised in December 2003 ("FIN 46R"). FIN 46R requires a variable interest entity to be consolidated by a company if that company is the primary beneficiary of the entity. A company is a primary beneficiary if it is subject to a majority of the risk of loss from the variable interest entity's activities or entitled to receive a majority of the entity's residual returns or both. FIN 46R also requires disclosures about variable interest entities that a company is not required to consolidate but in which it has a significant variable interest. FIN 46R was applicable immediately to variable interest entities created after January 31, 2003, and will be effective for all other existing entities in financial statements for periods ending after December 15, 2004. Certain of the disclosure requirements apply in all financial statements issued after December 31, 2003, regardless of when the variable interest entity was established. The Company has no interest in any variable interest entity and, therefore, the full adoption of FIN 46R had no effect on the Company's consolidated financial condition or results of operations.

SFAS 146, Accounting for Costs Associated with Exit or Disposal Activities, was effective for exit or disposal activities that were initiated after December 31, 2002. SFAS 146 addresses significant issues regarding the recognition, measurement and reporting of costs that are associated with exit and disposal activities, including restructuring activities that are currently accounted for under Emerging Issues Task Force ("EITF") No. 94-3, Liability Recognition for Certain Employee Termination Benefits and Other Costs to Exit an Activity (including Certain Costs Incurred in a Restructuring). The provisions of EITF No. 94-3 shall continue to apply for an exit activity initiated under an exit plan that meets the criteria of EITF No. 94-3 prior to the adoption of SFAS 146. The effect of adoption of SFAS 146 will change, on a prospective basis, the timing of when restructuring charges are recorded from a commitment date approach to when the liability is incurred. The adoption of this pronouncement had no effect on the Company's financial statements.

SFAS 150, Accounting for Certain Financial Instruments with Characteristics of Both Liabilities and Equities, addresses how to classify and measure certain financial instruments with characteristics of both liabilities (or an asset in some circumstances) and equity. SFAS 150 requirements apply to issuers' classification and measurement of freestanding financial instruments, including those that comprise more than one option or forward contract. It requires that all instruments with characteristics of both liabilities and equity be classified as a liability and remeasured at fair value on each reporting date. SFAS 150 was effective immediately for all financial instruments entered into or modified after May 31, 2003, and for the first interim period beginning after June 15, 2003 for all other instruments. The adoption of SFAS 150 had no impact on the Company's financial statements.

(m) Reclassifications

Certain amounts in the accompanying 2003 consolidated financial statements have been reclassified in order to conform to the presentation of the 2004 consolidated financial statements.

2. Aircraft and Aircraft Engines On Operating Leases

At March 31, 2004, the Company owned five deHavilland DHC-8s, two deHavilland DHC-7s, three deHavilland DHC-6s, one Fairchild Metro III, two Shorts SD 3-60s, six Fokker 50s, two Saab 340As and 26 turboprop engines. The Company did not acquire or sell any aircraft during the first quarter of 2004. As discussed in Note 7, the Company acquired four aircraft in April 2004.

AeroCentury Corp.
Notes to Condensed Consolidated Financial Statements
March 31, 2004
Unaudited

2. Aircraft and Aircraft Engines On Operating Leases (continued)

During the first quarter of 2004:

The lease for the Company's Fairchild Metro III aircraft was extended for one year, through April 3, 2005.

The lessee for one of the Company's deHavilland DHC-6 aircraft notified the Company that the lessee intends to extend the lease for two additional years, through April 30, 2006. As discussed in Note 7, the lease was extended in April 2004.

One of the Company's Shorts SD 3-60 aircraft was re-leased to a new customer for a term of 36 months.

The lessee for the Company's deHavilland DHC-8 financed in AeroCentury II LLC notified the Company that the lessee will not exercise its early termination option and, therefore, the lease will continue through April 15, 2006.

At March 31, 2004, two of the Company's aircraft and two of its turboprop engines were off-lease. The Company is seeking re-lease or sale opportunities for the two remaining off-lease aircraft.

The lease for one of the Company's Fokker 50 aircraft expired in September 2002, but the lessee was obligated by the lease to continue to pay rent until certain return conditions were met. The Company and the lessee have agreed to certain terms and conditions regarding the return of the aircraft and the amounts owed by the lessee. Although the Company held a security deposit from this lessee, the amount of the deposit was not sufficient to pay the rent accrued through the return date and reimburse the Company for maintenance work which has been performed to meet the return conditions of the lease. The lessee has agreed to deliver a note in 2004, with a principal amount equal to the rent and maintenance in excess of the security deposit. The required maintenance has been performed and the Company has determined that the amount of the note will be approximately $700,000. The Company has recorded a $250,000 allowance against the amount receivable and believes that such allowance is adequate to cover any shortfall in payment under the note. The Company expects that the note will be signed in the second quarter of 2004. The aircraft has been delivered to a new lessee.

3. Note Receivable

During the third quarter of 2003, the Company's two DHC-7 aircraft were returned to the Company by a defaulted lessee, and a settlement agreement was reached with the lessee in the amount of $500,000. The lessee paid $20,000 to the Company at the time of the settlement and signed a note in the amount of $480,000. The Company recorded an allowance for the full amount of the note and recorded income as note payments were received. The Company has entered into an agreement with a third party, who assisted the Company in the protection, management and recovery of the Company's assets from the lessee, which provides that the third party receives 40% of all amounts collected under the note. In the first quarter of 2004, the Company, based on the lessee's timely payment history on the note thus far, reversed 5% of the remaining allowance and recorded it as income. The Company also recorded the related expense for the amount payable to the third party. The Company will continue to monitor the lessee's payment history and may reverse additional portions of the allowance as the Company deems appropriate.

AeroCentury Corp.
Notes to Condensed Consolidated Financial Statements
March 31, 2004
Unaudited

4. Notes Payable and Accrued Interest

(a) Credit facility

In August 2003, the Company reached agreement with its lenders to extend the maturity date of its credit facility from August 28, 2003 to August 31, 2004. The facility bears interest, at the Company's option, at either (i) prime plus a margin of 50 to 150 basis points or (ii) LIBOR plus a margin of 275 to 375 basis points. Both the prime and LIBOR margins are determined by certain financial ratios.

In January 2004, a new bank was added to the Company's credit facility participant group. The new participant agreed to finance $10 million, bringing the Company's credit facility limit to $50 million.

In accordance with the agreement for the credit facility, the Company must maintain compliance with certain financial covenants, such as a requirement for positive quarterly earnings, bank approval of new leases and a net worth ratio. As of March 31, 2004, the Company was in compliance with all covenants, $38,405,000 was outstanding under the credit facility, and interest of $155,940 was accrued. As discussed in Note 7, in April 2004, the Company repaid $4,000,000 of the outstanding principal under the credit facility.

The Company's longer term viability will depend upon its ability to renew the credit facility at its expiration with the existing or replacement lenders, or to refinance the credit facility using equity or alternative debt financing. There is no assurance that the Company will be able to achieve either alternative prior to the currently scheduled expiration of the credit line on August 31, 2004.

If the Company is not able to renew the credit facility for the full outstanding amount, and cannot find suitable alternative financing, it may be required to make a principal repayment of the outstanding balance, or that portion of the balance for which replacement financing is not obtained. The Company does not have sufficient cash reserves to make a repayment of a significant portion of the outstanding credit facility indebtedness and would be forced to sell assets in order to raise funds to make such repayment. Such sales would likely not be on favorable terms to the Company as the full market value of the assets sold may not be realized by the Company in order to expedite the consummation of the sales.

Even if the Company is able to successfully sell a portion of its assets and use the proceeds to repay the credit line facility, if a renewed or replacement facility is not obtained, the Company's future ability to acquire assets would be significantly impaired, as the credit facility is the Company's primary means of financing acquisitions and no other sources of acquisition financing are immediately available. Thus the renewal or replacement of the Company's credit line facility in an amount equal or greater than the current $50 million limit will be critical to the Company's asset and revenue growth.

4. Notes Payable and Accrued Interest (continued)

(b) Special purpose financing

In September 2000, the Company acquired a deHavilland DHC-8 aircraft using cash and bank financing separate from its credit facility. The financing resulted in a note obligation, as amended, in the amount of $3,575,000, due April 15, 2006, which bears interest at the rate of one-month LIBOR plus 3%. The note is collateralized by this aircraft and is non-recourse to the Company. Payments due under the note consist of monthly principal and interest and a balloon principal payment due on the maturity date. The financing also provides for a six month remarketing period at the expiration or earlier termination of the lease. Payments due on the financing are reduced during this remarketing period and the balloon principal payment is due at the end of the six month period. The balance of the note payable at March 31, 2004 was $2,109,030 and interest of $3,110 was accrued. As of March 31, 2004, the Company was in compliance with all covenants of this note obligation.

5. Income Taxes

The items comprising income tax expense/(benefit) are as follows:

	For the Three Months 2004
Current tax provision:	
Federal	$ -
State	1,550
Current tax provision	1,550
Deferred tax provision/(benefit):	
Federal	10,030
State	(10,650)
Deferred tax provision/(benefit)	(620)
Total provision for income taxes	$ 930

Total income tax expense/(benefit) differs from the amount that would be provided by applying the statutory federal income tax rate to pretax earnings as illustrated below:

	For the Three Months 2004
Income tax expense/ at statutory federal income tax rate	$ 10,560
State tax expense, net of federal benefit	1,060
Tax rate differences	(10,690)
Total income tax expense	$ 930

AeroCentury Corp.
Notes to Condensed Consolidated Financial Statements

March 31, 2004
Unaudited

5. Income Taxes (continued)

Temporary differences and carryforwards that gave rise to a significant portion of deferred tax assets and liabilities as of March 31, 2004 are as follows:

Deferred tax assets:	
Bad debt allowance	$ 227,400
Deferred maintenance	465,430
Maintenance reserves	2,372,870
Net operating loss carryovers	135,730
Prepaid rent and other	66,250
Deferred tax assets	3,267,680
Deferred tax liabilities:	
Depreciation on aircraft and aircraft engines	(5,798,380)
Unearned income	(56,480)
Other	(196,650)
Net deferred tax liabilities	$ (2,783,830)

No valuation allowance is deemed necessary, as the Company anticipates generating adequate future taxable income to realize the benefits of all deferred tax assets on the balance sheet. Net operating loss carryovers may be carried forward twenty years and begin to expire in 2024.

6. Related Party Transactions

Since the Company has no employees, the Company's portfolio of leased aircraft assets is managed and administered under the terms of a management agreement with JetFleet Management Corp. ("JMC"), which is an integrated aircraft management, marketing and financing business and a subsidiary of JetFleet Holding Corp. ("JHC"). Certain officers of the Company are also officers of JHC and JMC and hold significant ownership positions in both JHC and the Company. Under the management agreement, JMC receives a monthly management fee based on the net asset value of the assets under management. JMC may also receive an acquisition fee for locating assets for the Company, provided that the aggregate purchase price, including chargeable acquisition costs and any acquisition fee, does not exceed the fair market value of the asset based on appraisal, and a remarketing fee in connection with the sale or re-lease of the Company's assets. The management fees, acquisition fees and remarketing fees may not exceed the customary and usual fees that would be paid to an unaffiliated party for such services. The Company recorded management fees of $462,780 and $487,060 during the three months ended March 31, 2004 and 2003, respectively. Because the Company did not acquire any aircraft during the first quarters of 2004 or 2003, no acquisition fees were paid to JMC. No remarketing fees were accrued to JMC during the first quarters of 2004 or 2003.

AeroCentury Corp.
Notes to Condensed Consolidated Financial Statements
March 31, 2004
Unaudited

7. Subsequent Events

In April 2004, the Company purchased four Fokker 50 aircraft. The aircraft are on lease to a lessee which also leases two of the Company's other Fokker 50 aircraft. In connection with the purchase, the leases for the two original aircraft were extended. The six aircraft have lease terms which vary from 18 to 30 months.

In April 2004, the lease for one of the Company's deHavilland DHC-6 aircraft was extended for two years, through April 30, 2006.

In April 2004, the lease for another of the Company's deHavilland DHC-6 aircraft was extended from its expiration date of April 25, 2004 to July 25, 2004. The Company and the lessee are negotiating a long-term extension of the lease.

In April 2004, the Company repaid $4,000,000 of the outstanding principal under its credit facility.

Item 2. Management's Discussion and Analysis or Plan of Operation.

Overview

The Company is a lessor of turboprop aircraft and engines which are used by customers pursuant to triple net operating leases. The acquisition of such equipment is generally made using debt financing. The Company's profitability and cash flow are dependent in large part upon its ability to acquire equipment, obtain and maintain favorable lease rates on such equipment, and re-lease owned equipment that comes off lease. The Company is subject to the credit risk of its lessees, both as to collection of rent and to performance by the lessees of obligations for maintaining the aircraft. Since lease rates for assets in the Company's portfolio generally decline as the assets age, the Company's ability to maintain revenue and earnings over the medium and long term is dependent upon the Company's ability to grow its asset portfolio.

The Company's principal expenditures are for interest costs on its financing, management fees, and maintenance of its aircraft assets. Maintenance expenditures are generally incurred only when aircraft are off lease, are being prepared for re-lease, or require maintenance in excess of lease return conditions.

The most significant non-cash expenses include accruals of maintenance costs to be borne by the Company and aircraft depreciation, both of which are the result of significant estimates. Maintenance expenses are estimated and accrued based upon utilization of the aircraft. Depreciation is recognized based upon the estimated residual value of the aircraft at the end of their estimated lives. Deviation from these estimates could have a substantial effect on the Company's cash flow and profitability.

Critical Accounting Policies

In response to the Securities and Exchange Commission's Release No. 33-8040, "Cautionary Advice Regarding Disclosure About Critical Accounting Policies," the Company has identified the most critical accounting policies upon which its financial status depends. It determined the critical policies by considering those that involve the most complex or subjective decisions or assessments. The Company identified these policies to be those related to valuation of aircraft, depreciation policies, maintenance reserves and accrued costs and lease rental revenue recognition.

a. Use of Estimates

In preparing its financial statements, as well as in evaluating future cash flow, the Company makes significant estimates, including the residual values of the aircraft, the useful lives of the aircraft, the amount and timing of cash flow associated with each aircraft that are used to evaluate impairment, if any, accrued maintenance costs in excess of amounts received from lessees, and amounts recorded as bad debt allowances. Actual results will likely vary from estimates.

Historically, the Company has realized at least its carrying value on the sale of any asset. However, in 2000, the Company recognized an impairment on two of its assets as a result of third party valuations.

The Company continually evaluates both short and long term maintenance expected to be required for each of its aircraft, including the estimated cost thereof, and compares it to the maintenance reserves established for each aircraft. With respect to estimated maintenance costs, the Company has found its accruals to be generally accurate, except in two occurrences in which the Company was required to recognize additional expense: (1) a circumstance in 2003 where a defaulted lessee failed to perform substantial maintenance required under the lease and (2) in 2001, the Company accrued an estimate related to compensation to be paid to the lessee of two aircraft, based on the maintenance-related return provisions of the leases. In the latter circumstance, the two aircraft were returned in 2002, at which time the final amount of compensation was determined and the Company reversed a portion of its accrual, which represented the amount of the Company's estimate in excess of the final amount, resulting in an increase in the Company's earnings.

b. Impairment of Long-lived Assets

The Company periodically reviews its portfolio of assets for impairment in accordance with Statement of Financial Accounting Standards ("SFAS") No. 144, "Accounting for the Impairment or Disposal of Long-lived Assets." Such review necessitates estimates of current market values, residual values and component values. The estimates are based on currently available market data and third-party appraisals and are subject to fluctuation from time to time. The Company initiates its review periodically, whenever events or changes in circumstances indicate that the carrying amount of a long-lived asset may not be recoverable. Recoverability of an asset is measured by comparison of its carrying amount to the expected future undiscounted cash flows (without interest charges) that the asset is expected to generate. Any impairment to be recognized is measured by the amount by which the carrying amount of the asset exceeds its fair market value. Significant management judgment is required in the forecasting of future operating results which are used in the preparation of projected undiscounted cash flows and should different conditions prevail, material write downs may occur.

c. Depreciation Policies

The Company's interests in aircraft and aircraft engines are recorded at cost, which includes acquisition costs. Depreciation is computed using the straight-line method over the aircraft's estimated economic life (generally assumed to be twelve years from the date of acquisition), to an estimated residual value based on appraisal.

d. Maintenance Reserves and Accrued Costs

Maintenance costs under the Company's triple net leases are generally the responsibility of the lessees. Maintenance reserves and accrued costs in the accompanying balance sheet include refundable and non-refundable maintenance payments received from lessees. The Company periodically reviews maintenance reserves for each of its aircraft for adequacy in light of the number of hours flown, airworthiness directives issued by the manufacturer or government authority, and the return conditions specified in the lease, as well as the condition of the aircraft upon return or inspection. As a result of such review, if it is probable that the Company has incurred costs for maintenance in excess of amounts received from lessees, the Company accrues its share of costs for work to be performed.

e. Revenue Recognition

Revenue from leasing of aircraft assets is recognized as operating lease revenue on a straight-line basis over the terms of the applicable lease agreements. If the Company deems a portion of operating lease revenue as potentially uncollectible, the Company records an allowance for doubtful accounts.

Results of Operations

a. Revenues

Operating lease revenue was approximately $392,000 lower in the three months ended March 31, 2004 versus the three months ended March 31, 2003, primarily because of lower lease rates for aircraft re-leased during 2003 and aircraft off lease during 2004. These decreases, totaling approximately $535,000, more than offset the increase of approximately $143,000 which resulted from several aircraft which had been off lease during the first three months of 2003 and which were re-leased beginning in April 2003. Other income was approximately $46,000 higher in the three months ended March 31, 2004 versus the same period in 2003 because of note payments received from a former lessee on a fully reserved note and because, based on the lessee's payment history to date, the Company reversed a portion of the allowance equal to 5% of the note balance. The Company continues to monitor the lessee's payment timeliness and evaluates further reversals of the allowance as the Company deems appropriate.

b. Expense items

Depreciation and management fees were approximately the same in the three month periods of both years.

Interest expense was approximately $40,000 higher in the three months ended March 31, 2004 versus the three months ended March 31, 2003 as a result of higher average interest rates arising from the renegotiation of the Company's credit facility in the third quarter of 2003, which was partially offset by a lower average outstanding balance on the facility.

Professional fees and general and administrative expenses and insurance expense were approximately the same in the three month periods of both years.

Maintenance expense was approximately $76,000 lower in the three months ended March 31, 2004 compared to the same period in 2003, as a result of accruals in 2003 to prepare aircraft for delivery to new lessees.

Bad debt expense was $100,000 in the three months ended March 31, 2003, versus no such expense in 2004, due to an allowance for doubtful accounts related to amounts due from a lessee for rent and maintenance necessary to meet the return conditions under its lease.

The Company's effective tax rates in the first quarter of 2004 and 2003 were approximately 3% and 20%, respectively. In both periods, the Company recognized approximately the same dollar reduction in tax expense arising from different state tax rates than had been accrued in earlier years. The reduction had a larger percentage effect in the 2004 period as a result of lower federal tax accruals in such period as compared to the 2003 period.

Liquidity and Capital Resources

The Company is currently financing its assets primarily through credit facility borrowings, special purpose financing and excess cash flow.

a. Credit facility

In August 2003, the Company reached agreement with its lenders to extend the maturity date of its credit facility from August 28, 2003 to August 31, 2004. The facility bears interest, at the Company's option, at either (i) prime plus a margin of 50 to 150 basis points or (ii) LIBOR plus a margin of 275 to 375 basis points. Both the prime and LIBOR margins are determined by certain financial ratios.

In January 2004, a new bank was added to the Company's credit facility participant group. The new participant agreed to finance $10 million, bringing the Company's credit facility limit to $50 million.

In accordance with the agreement for the credit facility, the Company must maintain compliance with certain financial covenants, such as a requirement for positive quarterly earnings, bank approval of new leases and a net worth ratio. As of March 31, 2004, the Company was in compliance with all covenants, $38,405,000 was outstanding under the credit facility, and interest of $155,940 was accrued. In April 2004, the Company repaid $4,000,000 of the outstanding principal under its credit facility. Based on its current projections, the Company believes it will continue to be in compliance with all covenants of its credit facility. See "Factors That May Affect Future Results - 'Credit Facility Obligations' and 'Risks of Debt Financing'," below.

The Company's interest expense in connection with the credit facility generally moves up or down with the prevailing interest rates, as the Company has not entered into any interest rate hedge transactions for the credit facility indebtedness. Because aircraft owners seeking financing generally can obtain financing through either leasing transactions or traditional secured debt financings, prevailing interest rates are a significant factor in determining market lease rates, and market lease rates generally move up or down with prevailing interest rates, assuming supply and demand of the desired equipment remain constant. However, because lease rates for the Company's assets typically are fixed under existing leases, the Company normally does not experience any positive or negative impact in revenue from changes in market lease rates due to interest rate changes until existing leases have terminated.

b. Special purpose financing

In September 2000, the Company acquired a deHavilland DHC-8 aircraft using cash and bank financing separate from its credit facility. The financing resulted in a note obligation, as amended, in the amount of $3,575,000, due April 15, 2006, which bears interest at the rate of one-month LIBOR plus 3%. The note is collateralized by this aircraft and is non-recourse to the Company. Payments due under the note consist of monthly principal and interest and a balloon principal payment due on the maturity date. The financing also provides for a six month remarketing period at the expiration or earlier termination of the lease. Payments due on the financing are reduced during this remarketing period and the balloon principal payment is due at the end of the six month period. The balance of the note payable at March 31, 2004 was $2,109,030 and interest of $3,110 was accrued. As of March 31, 2004, the Company was in compliance with all covenants of this note obligation.

The availability of special purpose financing in the future will depend on several factors including (1) the availability of funds to be used for the equity portion of the financing, (2) the type of asset being financed and (3) the creditworthiness of the underlying lessee. The availability of funds for the equity portion of the financing will be dependent on the Company's cash flow, as discussed in "Cash Flow," below.

c. Cash flow

The Company's primary source of revenue is lease rentals of its aircraft assets. It is the Company's policy to monitor each lessee's needs in periods before leases are due to expire. If it appears that a customer will not be renewing its lease, the Company immediately initiates marketing efforts to locate a potential new lessee or purchaser for the aircraft. The goal of this procedure is to reduce the time that an asset will be off lease. The Company's aircraft are subject to leases with varying expiration dates through October 2007.

Management believes that the Company will have adequate cash flow to meet its ongoing operational needs, including required repayments under its credit facility, based upon (i) its estimates of future revenues and expenditures and (ii) the expectation that the credit facility will be renewed on or before expiration. The Company's expectations concerning such cash flows are based on existing lease terms and rents, as well as numerous estimates, including (1) rents on assets to be re-leased, (2) sale proceeds of certain assets currently under lease, (3) the cost and anticipated timing of maintenance to be performed and (4) acquisition of additional aircraft and the lease thereof at favorable lease terms. While the Company believes that the assumptions it has made in forecasting its cash flow are reasonable in light of experience, actual results could deviate from such assumptions. Among the more significant external factors outside the Company's control that could have an impact on the accuracy of cash flow assumptions are (i) lessee non-performance or non-compliance with lease obligations (which may affect credit line collateral limitations as well as revenue and expenses) and (ii) an unexpected deterioration of demand for aircraft equipment beyond what the Company has assumed.

(i) Operating activities

The Company's cash flow from operations for the three months ended March 31, 2004 versus the three months ended March 31, 2003 decreased by approximately $643,000. The change in cash flow is a result of changes in several cash flow items during the period, including principally the following:

Lease rents, maintenance reserves and security deposits

Lease rental collections were approximately $210,000 lower in the three months ended March 31, 2004 than in the three months ended March 31, 2003, reflecting lower lease rates for aircraft re-leased during 2003 and aircraft off lease during 2004. These decreases more than offset the increase which resulted from several aircraft which had been off lease during the first three months of 2003 and which were re-leased beginning in April 2003. It is expected that rental rates on aircraft to be re-leased will continue to decline, so that, absent additional acquisitions by the Company, lease rentals for the current portfolio can be expected to decline over the long term.

Payments received from lessees for maintenance reserves increased by approximately $80,000 in the three months ended March 31, 2004 versus the same period in 2003, reflecting principally an increase in usage by lessees of the aircraft that are owned and on lease by the Company.

Expenditures for maintenance

Expenditures for maintenance were approximately $742,000 more in the three months ended March 31, 2004 than in the three months ended March 31, 2003 as a result of (1) the payment of a portion of maintenance accruals recorded in 2003 in connection with the return of three aircraft from a lessee declared in default of its obligations and (2) amounts paid by the Company for maintenance work which was performed to meet the return conditions of the lease for another aircraft which was returned at lease expiration in 2003. The lessee has entered into an agreement to reimburse the Company for the cost of the maintenance.

Professional fees and general and administrative

Expenditures for professional fees were approximately $60,000 higher during the three months ended March 31, 2004 as compared to the same period in 2003, principally as a result of higher legal expense related to aircraft re-leased in late 2003 and 2004.

(ii) Investing activities

The increase in cash flow used for investing activities from the three months ended March 31, 2003 to the same period in 2004 was primarily due to the addition of equipment to two of the Company's aircraft in 2004, versus no such expenditures in 2003.

(iii) Financing activities

Cash flow used by financing activities was approximately the same in the three months ended March 31, 2004 and 2003. The Company did not borrow on its credit facility during either period. Repayments of a portion of the Company's notes payable were approximately the same in both periods.

Outlook

The Company continually monitors the financial condition of its lessees in order to minimize the likelihood of significant defaults. In particular, the Company is currently monitoring both the financial position as well as the operations of a startup airline which leases two of its aircraft. In addition, any further weakening in the aircraft industry may affect the performance of lessees that currently appear creditworthy. See "Factors that May Affect Future Results - General Economic Conditions," below.

Although the Company purchased four aircraft in April 2004, in order to increase revenue, additional acquisitions of leased assets will be necessary to offset the anticipated decreased lease rates which will be obtained from the re-lease of the Company's current portfolio.

The Company continues to review its asset valuations in light of the worldwide economic downturn. Although the Company did not make any valuation adjustments during 2003, any future adjustments, if necessary, would negatively affect the Company's financial results and the collateral available for the Company's credit facility. In addition, the Company's periodic review of the adequacy of its maintenance reserves, as well as routine and manufacturer-required maintenance for any off-lease aircraft, may result in changes to estimated maintenance expense, further reducing earnings.

Maintenance on one of the three aircraft which were returned early by a defaulted lessee was completed and the aircraft was delivered to a new lessee in the first quarter of 2004. Maintenance on the other two assets, both of which are DHC-7 aircraft, has begun and is expected to be complete in the second quarter of 2004. The Company anticipates that the cost of the maintenance on these two aircraft will not exceed the accruals recorded in 2003. The Company believes that the aircraft, once ready, will be relatively difficult to remarket based on prior experience with this type of aircraft. Therefore, the Company anticipates that a substantial amount of time may pass before these DHC-7 aircraft return to revenue-generating status. See "Factors that May Affect Future Results - Remarketing of Repossessed Dash 7 Aircraft," below.

As a result of depreciation and collateral restrictions of aircraft leases set to expire in 2004, the Company may be required to make principal repayments under its credit facility. A focus of the Company, therefore, will be on re-leasing aircraft that come off lease to limit the amount of any required repayment. Management believes that the Company will have sufficient cash to fund any required repayments.

The former Brazilian lessee of a Fokker 50 aircraft has agreed to deliver a note, with a principal amount equal to the rent and maintenance in excess of the security deposit held by the Company. The required maintenance has been performed and the Company has determined that the amount of the note will be approximately $700,000. The Company has recorded a $250,000 allowance against the amount receivable and believes this allowance is adequate to cover any shortfall in payment under the note. The Company expects that the note will be signed in the second quarter of 2004.

Factors that May Affect Future Results

Term of Credit Facility. As discussed in "Outlook" above, the term of the credit facility was extended for one year, until August 31, 2004. The Company's longer term viability will depend upon its ability to renew the credit facility at its expiration with the existing or replacement lenders, or to refinance the credit facility using equity or alternative debt financing. There is no assurance that the Company will be able to achieve either alternative prior to the currently scheduled expiration of the credit line on August 31, 2004.

If the Company is not able to renew the credit facility for the full outstanding amount, and cannot find suitable alternative financing, it may be required to repay the outstanding balance, or that portion of the balance for which replacement financing is not obtained. The Company does not have sufficient cash reserves to make a repayment of a significant portion of the outstanding credit facility indebtedness and would be forced to sell assets in order to raise funds to make such repayment. Such sales would likely not be on favorable terms to the Company as the full market value of the assets sold may not be realized by the Company in order to expedite the consummation of the sales.

In any event, if a renewed or replacement facility is not obtained, the

Company's future ability to acquire assets will be significantly impaired, as the credit facility is the Company's primary means of financing acquisitions and no other sources of acquisition financing are immediately available. Thus the renewal or replacement of the Company's credit line facility in an amount equal or greater than the current $50 million limit will be critical to the Company's asset and revenue growth.

Credit Facility Obligations. The Company is obligated to make repayment of principal under the credit facility in order to maintain certain debt ratios with respect to its assets in the collateral pool. Assets that come off lease and remain off-lease for a period of time are removed from the collateral pool. The Company believes it will have sufficient cash funds to make any payment that arises due to collateral pool limitations caused by assets coming off lease in the near term. The Company's belief is based on certain assumptions regarding renewal of existing leases, a lack of extraordinary interest rate increases, no lessee defaults or bankruptcies, and certain other matters that the Company deems reasonable in light of its experience in the industry. There can be no assurance that the Company's assumptions will turn out to be correct. If the assumptions do not prove to be true (for example, if an asset in the collateral base unexpectedly goes off-lease for an extended period of time) and the Company has not obtained an applicable waiver or amendment of applicable covenants from its lenders to deal with the situation, the Company may have to sell a significant portion of its portfolio in order to maintain compliance with covenants or face default on its credit facility.

Concentration of Lessees and Aircraft Type. With the acquisition of four Fokker-50 aircraft on lease to an existing lessee of the Company, the Company's four biggest customers now comprise approximately 64% of the Company's current monthly lease revenue. The lessees, doing business in Taiwan, Sweden, Indonesia and the US, constitute approximately 23%, 19%, 12%, and 11% of the Company's monthly lease revenue, respectively. A lease default by or collection problems with one of these customers could have a disproportionate negative impact on the Company's financial results, and therefore, the Company's operating results will be especially sensitive to any negative developments with respect to these significant customers in terms of lease compliance or collection. Such concentration of lessee credit risk will diminish in the future only if the Company is able to lease additional assets to new lessees.

The acquisition of the four Fokker 50 aircraft also makes this aircraft type the dominant aircraft in the portfolio, constituting 10 of the 28 aircraft in the portfolio. As a result, a change in the desirability and availability of Fokker 50 aircraft, which would in turn affect valuations of such aircraft, would have a disproportionately large impact on the Company's portfolio value. Such aircraft type concentration will diminish if the Company acquires additional assets of other types. Conversely, acquisition of additional Fokker 50 aircraft will increase the Company's risks related to its concentration of aircraft type.

Remarketing of Repossessed Dash 7 Aircraft. In 2003, the Company repossessed two deHavilland DHC-7 aircraft from a Haitian lessee. These two aircraft are special purpose aircraft with short take-off and landing abilities, which make them attractive to specific niche operators. Because they have four engines, however, they are relatively more expensive to operate than two- engine 50-passenger turboprop aircraft and, therefore, unattractive to operators who do not require the aircraft's special characteristics. Thus, it has been the Company's experience that the remarketing period for DHC-7 aircraft may be significantly longer than for other similar turboprop aircraft. Consequently, a significant amount of time may pass before the DHC-7 aircraft begin to generate cash flow and contribute to earnings for the Company either through a re-lease or sale of the aircraft.

Risks of Debt Financing. The Company's use of acquisition financing under its credit facility and its special purpose financings subject the Company to increased risks of leveraging. If, due to a lessee default, the Company is unable to repay the debt secured by the aircraft acquired, then the Company could lose title to the acquired aircraft in a foreclosure proceeding. With respect to the credit facility, the loans are secured by the Company's existing assets as well as the assets acquired with each financing. In addition to payment obligations, the credit facility also requires the Company to comply with certain financial covenants, including a requirement of positive quarterly earnings, interest coverage and net worth ratios. Any default under the credit facility, if not waived by the lenders, could result in foreclosure upon not only the asset acquired using such financing, but also the existing assets of the Company securing the loan.

General Economic Conditions. The Company's business is dependent upon general economic conditions and the strength of the travel and transportation industry. The industry recently experienced a severe cyclical downturn which began in mid-2001. This downturn was exacerbated by the terrorist attacks of September 11, 2001 and a reduction in airline passenger loads caused by Severe Acute Respiratory Syndrome ("SARS"). As a result, there was an overall severe reduction in air travel and less demand for aircraft capacity by the major air carriers. There are signs that the industry is beginning to recover from the downturn, but it is unclear whether this recovery will be a sustained one. The recovery could be stalled or reversed by any number of events or circumstances, including the global economy slipping back into recession, or specific events related to the air travel industry, such as further weakening of the air carrier or travel industries as a result of terrorist attacks, or an increase in the price of jet fuel, operational or labor costs.

Since regional carriers are generally not as well-capitalized as major air carriers, any economic setback in the industry may result in the increased possibility of an economic failure of one or more of the Company's lessees, particularly since many carriers are undertaking expansion of capacity to accommodate the recovering air passenger traffic. If lessees experience financial difficulties, this could, in turn, affect the Company's financial performance.

During any periods of economic contraction, carriers generally reduce capacity, in response to lower passenger loads, and as a result there is a reduced demand for aircraft and a corresponding decrease in market lease rental rates and aircraft values. This reduced market value for aircraft could affect the Company's results if the market value of an asset or assets in the Company's aircraft portfolio falls below book value, and the Company determines that a write-down of the value on the Company's book is appropriate. Furthermore, as older leases expire and are replaced by lease renewals or re-leases at decreasing lease rates, the lease revenue of the Company on its existing portfolio is likely to decline, with the magnitude of the decline dependent on the length of the downturn and the depth of the decline in market rents.

Economic downturns can affect specific regions of the world exclusively. As the Company's portfolio is not entirely globally diversified, a localized downturn in one of the key regions in which the Company leases aircraft (e.g. Europe or Asia) could have a significant adverse impact on the Company.

Interest Rate Risk. All of the Company's current credit facility indebtedness carries a floating interest rate based upon either the lender's prime rate or a floating LIBOR rate. Lease rates, generally, but not always, move with interest rates. Because lease rates are fixed at the origination of leases, interest rate increases during the term of a lease have no effect on existing lease payments. Therefore, if interest rates rise significantly, and there is relatively little lease origination by the Company following such rate increases, the Company could experience lower net earnings. The Company has not hedged its interest rate obligations. Consequently, if an interest rate increase were great enough, the Company might not be able to generate sufficient lease revenue to meet its interest payment and other obligations and comply with the net earnings covenant of its credit facility.

Leasing Risks. The Company's successful negotiation of lease extensions, re-leases and sales may be critical to its ability to achieve its financial objectives, and involves a number of risks. Demand for lease or purchase of the assets depends on the economic condition of the airline industry which is, in turn, sensitive to general economic conditions. The ability to remarket equipment at acceptable rates may depend on the demand and market values at the time of remarketing. The Company anticipates that the bulk of the equipment it acquires will be used aircraft equipment. The market for used aircraft is cyclical, and generally reflects economic conditions and the strength of the travel and transportation industry. The demand for and value of many types of used aircraft in the recent past has been depressed by such factors as airline financial difficulties, increased fuel costs, the number of new aircraft on order and the number of aircraft coming off-lease. The Company's expected concentration in a limited number of airframe and aircraft engine types (generally, turboprop equipment) subjects the Company to economic risks if those airframe or engine types should decline in value. If "regional jets" were to be used on short routes previously served by turboprops, even though regional jets are more expensive to operate than turboprops, the demand for turboprops could lessen. This could result in lower lease rates and values for the Company's existing turboprop aircraft.

Lessee Credit Risk. If a customer defaults upon its lease obligations, the Company may be limited in its ability to enforce remedies. Most of the Company's lessees are small regional passenger airlines, which may be even more sensitive to airline industry market conditions than the major airlines. As a result, the Company's inability to collect rent under a lease or to repossess equipment in the event of a default by a lessee could have a material adverse effect on the Company's revenue. If a lessee that is a certified U.S. airline is in default under the lease and seeks protection under Chapter 11 of the United States Bankruptcy Code, Section 1110 of the Bankruptcy Code would automatically prevent the Company from exercising any remedies for a period of 60 days. After the 60-day period has passed, the lessee must agree to perform the obligations and cure any defaults, or the Company will have the right to repossess the equipment. This procedure under the Bankruptcy Code has been subject to significant recent litigation, however, and it is possible that the Company's enforcement rights may be further adversely affected by a declaration of bankruptcy by a defaulting lessee.

Risks Related to Regional Air Carriers. Because the Company has concentrated its existing leases and intends to concentrate on future leases to regional air carriers, it is subject to certain risks. Some of the lessees in the regional air carrier market are companies that are start-up, low capital, low margin operations. Often, the success of such carriers is dependent upon arrangements with major trunk carriers, which may be subject to termination or cancellation by such major carrier. These types of lessees result in a generally higher lease rate on aircraft, but may entail higher risk of default or lessee bankruptcy. The Company evaluates the credit risk of each lessee carefully, and attempts to obtain a third party guaranty, letters of credit or other credit enhancements, if it deems them necessary. There is no assurance, however, that such enhancements will be available or that if obtained they will fully protect the Company from losses resulting from a lessee default or bankruptcy. Also, a significant area of growth of this market is in areas outside of the United States, where collection and enforcement are often more difficult and complicated than in the United States.

Reliance on JMC. All management of the Company is performed by JMC under a management agreement which is in the seventh year of a 20-year term and provides for an asset-based management fee. JMC is not a fiduciary to the Company or its stockholders. The Company's Board of Directors has ultimate control and supervisory responsibility over all aspects of the Company and owes fiduciary duties to the Company and its stockholders. While JMC may not owe any fiduciary duties to the Company by virtue of the management agreement, the officers of JMC are also officers of the Company, and in that capacity owe fiduciary duties to the Company and the stockholders by virtue of holding such offices with the Company. In addition, certain officers of the Company hold significant ownership positions in JHC and the Company.

The JMC management agreement may be terminated if JMC defaults on its obligations to the Company. However, the agreement provides for liquidated damages in the event of its wrongful termination by the Company. All of the officers of JMC are also officers of the Company, and certain directors of the Company are also directors of JMC. Consequently, the directors and officers of JMC may have a conflict of interest in the event of a dispute between the Company and JMC. Although the Company has taken steps to prevent conflicts of interest arising from such dual roles, such conflicts may still occur.

JMC has acted as management company for two other aircraft portfolio owners, JetFleet III, which raised approximately $13,000,000 from investors, and AeroCentury IV, Inc. ("AeroCentury IV"), which raised approximately $5,000,000 from investors.

In the first quarter of 2002, AeroCentury IV defaulted on certain obligations to noteholders. In June 2002, the indenture trustee for AeroCentury IV's noteholders repossessed AeroCentury IV's assets and took over management of AeroCentury IV's remaining assets. JetFleet III anticipates that it will default on its Bond obligation of $11,076,350 on the April 30, 2004 maturity date. JetFleet III has disclosed that it is currently seeking purchasers for its aircraft, and anticipates that the indenture trustee for JetFleet III bondholders will repossess JetFleet III's unsold assets immediately after the maturity date.

Ownership Risks. Most of the Company's portfolio is leased under operating leases, where the terms of the leases are less than the entire anticipated useful life of an asset. The Company's ability to recover its purchase investment in an asset subject to an operating lease is dependent upon the Company's ability to profitably re-lease or sell the asset after the expiration of the initial lease term. Some of the factors that have an impact on the Company's ability to re-lease or sell include worldwide economic conditions, general aircraft market conditions, regulatory changes that may make an asset's use more expensive or preclude use unless the asset is modified, changes in the supply or cost of aircraft equipment and technological developments which cause the asset to become obsolete. In addition, a successful investment in an asset subject to an operating lease depends in part upon having the asset returned by the lessee in serviceable condition as required under the lease. If the Company is unable to remarket its aircraft equipment on favorable terms when the operating leases for such equipment expire, the Company's business, financial condition, cash flow, ability to service debt and results of operations could be adversely affected.

Furthermore, during the ownership of an asset, an asset impairment charge against the Company's earnings may result from the occurrence of unexpected adverse changes that impact the Company's estimates of expected cash flows generated from such asset. The Company periodically reviews long-term assets for impairments, in particular, when events or changes in circumstances indicate the carrying value of an asset may not be recoverable. An impairment loss is recognized when the carrying amount of an asset is not recoverable and exceeds its fair value. The Company may be required to recognize asset impairment charges in the future as a result of the continued weak economic environment, challenging market conditions in the airline industry or events related to particular lessees, assets or asset types.

International Risks. The Company has focused on leases in overseas markets, which the Company believes present opportunities. Leases with foreign lessees, however, may present somewhat different credit risks than those with domestic lessees.

Foreign laws, regulations and judicial procedures may be more or less protective of lessor rights than those which apply in the United States. The Company could experience collection or repossession problems related to the enforcement of its lease agreements under foreign local laws and the remedies in foreign jurisdictions. The protections potentially offered by Section 1110 of the Bankruptcy Code do not apply to non-U.S. carriers, and applicable local law may not offer similar protections. Certain countries do not have a central registration or recording system with which to locally establish the Company's interest in equipment and related leases. This could make it more difficult for the Company to recover an aircraft in the event of a default by a foreign lessee.

A lease with a foreign lessee is subject to risks related to the economy of the country or region in which such lessee is located, which may be weaker than the U.S. economy. On the other hand, a foreign economy may remain strong even though the U.S. economy does not. A foreign economic downturn may impact a foreign lessee's ability to make lease payments, even though the U.S. and other economies remain stable. Furthermore, foreign lessees are subject to risks related to currency conversion fluctuations. Although the Company's current leases are all payable in U.S. dollars, the Company may agree in the future to leases that permit payment in foreign currency, which would subject such lease revenue to monetary risk due to currency fluctuations. Even with U.S. dollar-denominated lease payment provisions, the Company could still be affected by a devaluation of the lessee's local currency that would make it more difficult for a lessee to meet its U.S. dollar-denominated lease payments, increasing the risk of default of that lessee, particularly if its revenue is primarily derived in the local currency.

Government Regulation. There are a number of areas in which government regulation may result in costs to the Company. These include aircraft registration, safety requirements, required equipment modifications, and aircraft noise requirements. Although it is contemplated that the burden and cost of complying with such requirements will fall primarily upon lessees of equipment, there can be no assurance that the cost will not fall on the Company. Furthermore, future government regulations could cause the value of any non-complying equipment owned by the Company to decline substantially.

Competition. The aircraft leasing industry is highly competitive. The Company competes with aircraft manufacturers, distributors, airlines and other operators, equipment managers, leasing companies, equipment leasing programs, financial institutions and other parties engaged in leasing, managing or remarketing aircraft, many of which have significantly greater financial resources and more experience than the Company. However, the Company believes that it is competitive because of JMC's experience and operational efficiency in identifying and obtaining financing for the transaction types desired by regional air carriers. This market segment, which is characterized by transaction sizes of less than $10 million and lessee credits that may be strong, but are generally unrated, is not well served by the Company's larger competitors in the aircraft industry. JMC has developed a reputation as a global participant in this segment of the market, and the Company believes that JMC's reputation will benefit the Company. There is, however, no assurance that the lack of significant competition from the larger aircraft leasing companies will continue or that the reputation of JMC will continue to be strong in this market segment.

Casualties, Insurance Coverage. The Company, as owner of transportation equipment, may be named in a suit claiming damages for injuries or damage to property caused by its assets. As a triple net lessor, the Company is generally protected against such claims, since the lessee would be responsible for, insure against and indemnify the Company for, such claims. Further, some protection may be provided by the United States Aviation Act with respect to the Company's aircraft assets. It is, however, not clear to what extent such statutory protection would be available to the Company, and the United States Aviation Act may not apply to aircraft operated in foreign countries. Also, although the Company's leases generally require a lessee to insure against likely risks, there may be certain cases where the loss is not entirely covered by the lessee or its insurance. Though this is a remote possibility, an uninsured loss with respect to the equipment, or an insured loss for which insurance proceeds are inadequate, would result in a possible loss of invested capital in and any profits anticipated from, such equipment, as well as a potential claim directly against the Company.

Possible Volatility of Stock Price. The market price of the Company's common stock could be subject to fluctuations in response to the Company's operating results, changes in general conditions in the economy, the financial markets, the airline industry, changes in accounting principles or tax laws applicable to the Company or its lessees, or other developments affecting the Company, its customers or its competitors, some of which may be unrelated to the Company's performance. Also, because the Company has a relatively small capitalization of approximately 1.5 million shares, there is a correspondingly limited amount of trading of the Company's shares. Consequently, a single or small number of trades could result in a market fluctuation not related to any business or financial development concerning the Company.

Item 3. Controls and Procedures

Quarterly evaluation of the Company's Disclosure Controls and Internal Controls. As of the end of the period covered by this report, the Company evaluated the effectiveness of the design and operation of its "disclosure controls and procedures" ("Disclosure Controls"), and its "internal controls over financial reporting" ("Internal Controls"). This evaluation (the "Controls Evaluation") was done under the supervision and with the participation of management, including the Company's Chief Executive Officer ("CEO") and Chief Financial Officer ("CFO"). Rules adopted by the SEC require that in this section of the Report the Company present the conclusions of the CEO and the CFO about the effectiveness of our Disclosure Controls and Internal Controls based on and as of the date of the Controls Evaluation.

CEO and CFO Certifications. Attached as exhibits to this report are two separate forms of "Certifications" of the CEO and the CFO. The first form of Certification is required in accordance with Section 302 of the Sarbanes-Oxley Act of 2002 (the "Section 302 Certification"). This section of the report which you are currently reading is the information concerning the Controls Evaluation referred to in the Section 302 Certifications and this information should be read in conjunction with the Section 302 Certifications for a more complete understanding of the topics presented.

Disclosure Controls and Internal Controls. Disclosure Controls are procedures that are designed with the objective of ensuring that information required to be disclosed in the Company's reports filed under the Securities Exchange Act of 1934 (the "Exchange Act"), such as this report, is recorded, processed, summarized and reported within the time periods specified in the Securities and Exchange Commission's ("SEC") rules and forms. Disclosure Controls are also designed with the objective of ensuring that such information is accumulated and communicated to the Company's management, including the CEO and CFO, as appropriate to allow timely decisions regarding required disclosure. Internal Controls are procedures which are designed with the objective of providing reasonable assurance that (1) the Company's transactions are properly authorized; (2) the Company's assets are safeguarded against unauthorized or improper use; and (3) the Company's transactions are properly recorded and reported, all to permit the preparation of the Company's consolidated financial statements in conformity with generally accepted accounting principles.

Limitations on the Effectiveness of Controls. The Company's management, including the CEO and CFO, does not expect that its Disclosure Controls or its Internal Controls will prevent all errors and all fraud. A control system, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control system are met. Further, the design of a control system must reflect the fact that there are resource constraints, and the benefits of controls must be considered relative to their costs. Because of the inherent limitations in all control systems, no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, within the Company have been detected. These inherent limitations include the realities that judgments in decision-making can be faulty, and that breakdowns can occur because of simple error or mistake. Additionally, controls can be circumvented by the individual acts of some persons, by collusion of two or more people, or by management override of the control. The design of any system of controls also is based in part upon certain assumptions about the likelihood of future events, and there can be no assurance that any design will succeed in achieving its stated goals under all potential future conditions; over time, control may become inadequate because of changes in conditions, or the degree of compliance with the policies or procedures may deteriorate. Because of the inherent limitations in a cost-effective control system, misstatements due to error or fraud may occur and not be detected.

Scope of the Controls Evaluation. The CEO/CFO evaluation of the Company's Disclosure Controls and the Company's Internal Controls included a review of the controls objectives and design, the controls implementation by the company and the effect of the controls on the information generated for use in this report. In the course of the Controls Evaluation, we sought to identify data errors, controls problems or acts of fraud and to confirm that appropriate corrective action, including process improvements, were being undertaken. This type of evaluation will be done on a quarterly basis so that the conclusions concerning controls effectiveness can be reported in the Company's quarterly reports on Form 10-QSB and annual report on Form 10-KSB. The Company's Internal Controls are also evaluated on an ongoing basis by other personnel in the Company's finance organization and by the Company's independent auditors in connection with their audit and review activities. The overall goals of these various evaluation activities are to monitor the Company's Disclosure Controls and the Company's Internal Controls and to make modifications as necessary; the Company's intent in this regard is that the Disclosure Controls and the Internal Controls will be maintained as dynamic systems that change (including with improvements and corrections) as conditions warrant.

Among other matters, the Company sought in its evaluation to determine whether there were any "significant deficiencies" or "material weaknesses" in the Company's Internal Controls, or whether the Company had identified any acts of fraud involving personnel who have a significant role in the Company's Internal Controls. This information was important both for the Controls Evaluation generally and because item 5 in the Section 302 Certifications of the CEO and CFO require that the CEO and CFO disclose that information to the Audit Committee of the Company's Board and to the Company's independent auditors and to report on related matters in this section of the report. In the professional auditing literature, "significant deficiencies" are referred to as "reportable conditions"; these are control issues that could have a significant adverse effect on the ability to record, process, summarize and report financial data in the financial statements. A "material weakness" is defined in the auditing literature as a particularly serious reportable condition where the internal control does not reduce to a relatively low level the risk that misstatements caused by error or fraud may occur in amounts that would be material in relation to the financial statements and not be detected within a timely period by employees in the normal course of performing their assigned functions. The Company also sought to deal with other controls matters in the Controls Evaluation, and in each case if a problem was identified, the Company considered what revision, improvement and/or correction to make in accordance with our ongoing procedures.

In accordance with SEC requirements, the CEO and CFO note that, there has been no significant change in Internal Controls that occurred during our most recent fiscal quarter that has materially affected or is reasonably likely to materially affect our Internal Controls.

Conclusions. Based upon the Controls Evaluation, the Company's CEO and CFO have concluded that, subject to the limitations noted above, the Company's Disclosure Controls are effective to ensure that material information relating to the Company and its consolidated subsidiaries is made known to management, including the CEO and CFO, particularly during the period when periodic reports are being prepared, and that the Company's Internal Controls are effective to provide reasonable assurance that the Company's consolidated financial statements are fairly presented in conformity with generally accepted accounting principles.

PART II
OTHER Information

Item 6. Exhibits and Reports on Form 8-K.

(a) Exhibits

Exhibit Number	Description
31.1	Certification of Neal D. Crispin, Chief Executive Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
31.2	Certification of Toni M. Perazzo, Chief Financial Officer, pursuant to Section 302 of the Sarbanes-Oxley Act of 2002.
32.1*	Certification of Neal D. Crispin, Chief Executive Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.
32.2*	Certification of Toni M. Perazzo, Chief Financial Officer, pursuant to Section 906 of the Sarbanes-Oxley Act of 2002.

* These certificates are furnished to, but shall not be deemed to be filed with, the Securities and Exchange Commission ("SEC").

(b) Reports on Form 8-K

The Company filed a Report on Form 8-K disclosing the Sixth Amendment to Credit Agreement on January 5, 2004.

SIGNATURES

In accordance with the requirements of the Exchange Act, the registrant caused this report to be signed on its behalf by the undersigned, thereunto duly authorized.

AEROCENTURY CORP.

Date: May 13, 2004

By: /s/ Toni M. Perazzo

Toni M. Perazzo

Title: Senior Vice President-Finance and Chief Financial Officer