SECURITIES AND EXCHANGE COMMISSION
WASHINGTON, D.C. 20549

FORM 10-Q

|X| QUARTERLY REPORT PURSUANT TO SECTION 13 OR 15(d) OF THE SECURITIES EXCHANGE ACT OF 1934 FOR THE QUARTERLY PERIOD ENDED September 30, 2004.

Commission file number: 0-23336

AROTECH CORPORATION

(Exact name of registrant as specified in its charter)

Delaware	95-4302784
(State or other jurisdiction of incorporation or organization)	(I.R.S. Employer Identification No.)

250 West 57th Street, Suite 310, New York, New York	10107
(Address of principal executive offices)	(Zip Code)

(212) 258-3222

(Registrant's telephone number, including area code)

(Former address, if changed since last report)

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

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

APPLICABLE ONLY TO CORPORATE ISSUERS:

The number of shares outstanding of the issuer's common stock as of November 10, 2004 was 79,096,283.

AROTECH CORPORATION

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AROTECH CORPORATION

Item 1. INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

CONSOLIDATED BALANCE SHEETS
(U.S. Dollars)

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ASSETS	September 30, 2004 (Unaudited)	December 31, 2003 (Note 1.c.)
CURRENT ASSETS:		
Cash and cash equivalents	$ 4,573,875	$13,685,125
Restricted securities and deposits due within one year	13,236,461	706,180
Available-for-sale marketable securities	128,826	--
Trade receivables (net of allowance for doubtful accounts in the amounts of $56,394 and $61,282 as of September 30, 2004 and December 31, 2003, respectively)	7,800,632	4,706,423
Current portion of note receivable	329,550	--
Unbilled revenues	2,560,108	--
Other accounts receivable and prepaid expenses	1,623,183	1,187,371
Inventories	7,631,193	1,914,748
Assets of discontinued operations	--	66,068
Total current assets	37,883,828	22,265,915
SEVERANCE PAY FUND	1,837,616	1,023,342
RESTRICTED SECURITIES AND DEPOSITS	1,000,000	--
LONG TERM NOTE RECEIVABLES	667,245	--
PROPERTY AND EQUIPMENT, NET	4,463,675	2,292,741
GOODWILL	24,978,764	5,064,555
OTHER INTANGIBLE Assets, NET	15,300,743	2,375,195
	$86,131,871	$33,021,748

</TABLE>

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

AROTECH CORPORATION
CONSOLIDATED BALANCE SHEETS
(U.S. Dollars, except share data)

<TABLE>
<CAPTION>

LIABILITIES AND SHAREHOLDERS' EQUITY	September 30, 2004 (Unaudited)	December 31, 2003* (Note 1.c.)
CURRENT LIABILITIES:		
Trade payables	$ 4,190,155	$ 1,967,448
Other accounts payable and accrued expenses	5,947,310	4,030,411**
Current portion of promissory notes due to purchase of subsidiaries	1,149,509	150,000
Short-term bank loans and current portion of long-term loans	106,691	40,849
Deferred revenues	2,884,295	140,936**
Liability related to warrants	9,011,995	--
Liabilities of discontinued operations	--	380,108
Total current liabilities	23,289,955	6,709,752
LONG TERM LIABILITIES		
Accrued severance pay	3,241,581	2,814,492
Convertible debentures, net	1,792,370	1,450,194
Deferred warranty revenue, less current portion	181,722	220,143
Promissory notes due to purchase of subsidiaries	977,861	150,000
Total long-term liabilities	6,193,534	4,634,829
MINORITY INTEREST	85,885	51,290

SHAREHOLDERS' EQUITY:		
Share capital -		
Common stock - $0.01 par value each; Authorized: 250,000,000 shares as of September 30, 2004 and December 31, 2003; Issued: 79,100,166 shares as of September 30, 2004 and 47,972,407 shares as of December 31, 2003; Outstanding - 78,544,833 shares as of September 30, 2004 and 47,417,074 shares as of December 31, 2003	791,002	479,726
Preferred shares - $0.01 par value each; Authorized: 1,000,000 shares as of September 30, 2004 and December 31, 2003; No shares issued and outstanding as of September 30, 2004 and December 31, 2003	--	--
Additional paid-in capital	177,348,358	135,702,413
Deferred stock compensation	(1,027,653)	(8,464)
Accumulated deficit	(115,698,412)	(109,911,240)
Treasury stock, at cost (common stock - 555,333 shares as of September 30, 2004 and December 31, 2003)	(3,537,106)	(3,537,106)
Notes receivable on account of shares	(1,222,902)	(1,203,881)
Accumulated other comprehensive income (loss)	(90,790)	104,429
Total shareholders' equity	56,562,497	21,625,877
	$ 86,131,871	$ 33,021,748

</TABLE>

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* Restated.
** Reclassified.

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

AROTECH CORPORATION
CONSOLIDATED STATEMENTS OF OPERATIONS (Unaudited)
(U.S. Dollars, except share data)

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<TABLE>
<CAPTION>

	Nine months ended September 30,		Three months ended September 30,	
	2004	2003*	2004	2003*
<S>	<C>	<C>	<C>	<C>
Revenues	$ 33,383,023	$ 13,232,486	$ 16,272,521	$ 5,705,898
Cost of revenues	22,680,921	8,365,212	11,548,948	3,252,323
Gross profit	10,702,102	4,867,274	4,723,573	2,453,575
Operating expenses:				
Research and development	1,302,774	762,629	431,147	252,085
Selling and marketing	3,435,183	2,395,190	1,294,487	757,614
General and administrative	7,571,923	3,456,286	2,111,853	982,779
Amortization of intangible assets	1,731,425	727,127	739,400	103,584
Total operating costs and expenses	14,041,305	7,341,232	4,576,887	2,096,062
Operating income (loss)	(3,339,203)	(2,473,958)	146,686	357,513
Financial income (expenses), net	(2,126,079)	(1,213,582)	1,105,276	(82,333)
Income (loss) before income taxes	(5,465,282)	(3,687,540)	1,251,962	275,180
Income tax expenses, net	(286,525)	(308,137)	(116,460)	(31,089)
Income (loss) before minority interest in loss (earnings) of a subsidiary and income tax expenses	(5,751,807)	(3,995,677)	1,135,502	244,091
Minority interest in loss (earnings) of a subsidiary	(35,365)	134,813	(8,657)	(25,485)
Income (loss) from continuing operations	(5,787,172)	(3,860,864)	1,126,845	218,606
Income (loss) from discontinued operations	--	80,883	--	(2,285)
Net income (loss)	(5,787,172)	(3,779,981)	1,126,845	216,321
Deemed dividend to certain stockholders of common stock	(3,328,952)	(267,026)	(2,165,952)	(94,676)
Net income (loss) attributable to common stockholders	$ (9,116,124)	$ (4,047,007)	$ (1,039,107)	$ 121,645

Basic and diluted net earnings (loss) per share from continuing operations	$ (0.14)	$ (0.11)	$ (0.01)	$ 0.00
	============	============	============	============
Basic and diluted net earnings (loss) per share from discontinued operations	$ 0.00	$ 0.00	$ 0.00	$ 0.00
	============	============	============	============
Basic and diluted net earnings (loss) per share .	$ (0.14)	$ (0.11)	$ (0.01)	$ 0.00
	============	============	============	============
Weighted average number of shares used in computing basic net loss per share	67,072,069	37,276,260	76,744,251	40,371,940

</TABLE>

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* Restated.

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

AROTECH CORPORATION
CONSOLIDATED STATEMENT OF CHANGES IN STOCKHOLDERS' EQUITY
(U.S. Dollars, except share data)

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<TABLE>
<CAPTION>

	Common Stock		Additional paid-in capital	Deferred stock compensation	Accumulated deficit
	Shares	Amount			
<S>	<C>	<C>	<C>	<C>	<C>
BALANCE AT JANUARY 1, 2004 - NOTE 1	47,972,407	$ 479,726	$ 135,702,413*	$ (8,464)	$(109,911,240)*
CHANGES DURING THE NINE-MONTH PERIOD ENDED SEPTEMBER 30, 2004					
Issuance of shares, net	14,548,491	145,485	24,944,639	--	--
Issuance of shares in respect of FAAC acquisition	1,003,856	10,039	1,993,639	--	--
Conversion of convertible debentures	3,213,292	32,132	3,035,583	--	--
Exercise of warrants by investors	11,363,342	113,633	19,119,008	--	--
Issuance of shares to consultants	74,215	742	170,489	--	--
Compensation related to warrants issued in settlement of litigation ...	--	--	483,828	--	--
Compensation related to non-recourse loan granted to shareholder	--	--	(13,500)	--	--
Exercise of options by employees	856,948	8,569	1,053,012	--	--
Exercise of options by consultants	27,615	276	38,399	--	--
Shares issued to employee	40,000	400	92,800	--	--
Deferred stock compensation ..	--	--	1,556,147	(1,556,147)	--
Amortization of deferred stock compensation	--	--	--	536,958	--
Reclassification to liability in connection with warrants granted	--	--	(10,841,020)	--	--
Interest accrued on notes receivable from shareholders	--	--	12,921	--	--
Other comprehensive loss - foreign currency translation adjustment	--	--	--	--	--
Other comprehensive loss - unrealized gain on available for sale marketable securities	--	--	--	--	--
Net loss	--	--	--	--	(5,787,172)
	----------	-------------	-------------	-------------	-------------
Total comprehensive loss	--	--	--	--	--
BALANCE AT SEPTEMBER 30, 2004 - UNAUDITED	79,100,166	$ 791,002	$ 177,348,358	$ (1,027,653)	$(115,698,412)

<CAPTION>

	Treasury stock	Notes receivable from shareholders	Accumulated other comprehensive income (loss)	Total comprehensive loss	Total
<S>	<C>	<C>	<C>	<C>	<C>
BALANCE AT JANUARY 1, 2004 - NOTE 1	$ (3,537,106)	$ (1,203,881)	$ 104,429	$ --	$ 21,625,877*
CHANGES DURING THE NINE-MONTH					

PERIOD ENDED SEPTEMBER 30, 2004					
Issuance of shares, net	--	--	--	--	25,090,124
Issuance of shares in respect of FAAC acquisition	--	--	--	--	2,003,678
Conversion of convertible debentures	--	--	--	--	3,067,715
Exercise of warrants by investors	--	--	--	--	19,232,641
Issuance of shares to consultants	--	--	--	--	171,231
Compensation related to warrants issued in settlement of litigation ...	--	--	--	--	483,828
Compensation related to non-recourse loan granted to shareholder	--	--	--	--	(13,500)
Exercise of options by employees	--	(6,100)	--	--	1,055,481
Exercise of options by consultants	--	--	--	--	38,675
Shares issued to employee	--	--	--	--	93,200
Deferred stock compensation ..	--	--	--	--	--
Amortization of deferred stock compensation	--	--	--	--	536,958
Reclassification to liability in connection with warrants granted	--	--	--	--	(10,841,020)
Interest accrued on notes receivable from shareholders	--	(12,921)	--	--	--
Other comprehensive loss - foreign currency translation adjustment	--	--	(198,067)	(198,067)	(198,067)
Other comprehensive loss - unrealized gain on available for sale marketable securities	--	--	2,848	2,848	2,848
Net loss	--	--	--	(5,787,172)	(5,787,172)
Total comprehensive loss	--	--	--	$ (5,982,391)	--
BALANCE AT SEPTEMBER 30, 2004 - UNAUDITED	$ (3,537,106)	$ (1,222,902)	$ (90,790)		$ 56,562,497

</TABLE>

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* Restated.

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

AROTECH CORPORATION

CONSOLIDATED STATEMENT OF CASH FLOWS (Unaudited) (U.S. Dollars)

- --

<TABLE>
<CAPTION>

	Nine months ended September 30, 2004	2003*
CASH FLOWS FROM OPERATING ACTIVITIES:		
Net loss for the period	$ (5,787,172)	$ (3,779,981)
Net income for the period from discontinued operations	--	(80,883)
Adjustments required to reconcile net loss to net cash used in operating activities:		
Depreciation	834,637	529,155
Amortization of intangible assets	1,703,936	732,364
Amortization of subsidiary purchase price allocated to inventory	586,325	--
Amortization of prepaid financial expenses	--	236,250
Amortization of compensation related to warrants issued to the holders of convertible debentures and beneficial conversion feature	3,454,676	1,134,001
Amortization of deferred expenses related to convertible debenture issuance	176,771	156,802
Amortization of capitalized research and development projects	27,489	--
Adjustment of liability in connection to warrants granted	(1,829,025)	--
Stock-based compensation due to options and shares granted to employees	576,648	--
Stock-based compensation due to options granted to consultants	--	29,759
Stock-based compensation due to shares granted to consultants	--	154,331
Write-off of inventory	67,951	23,830
Earnings (loss) to minority	35,363	(134,813)
Impairment of fixed assets	--	62,332
Mark-up of loans to shareholders	(32,397)	(12,519)
Interest expenses (income) accrued on promissory notes due to purchase of subsidiary	36,385	(35,853)
Capital gain from sale of marketable securities	(4,114)	--
Interest accrued on certificates of deposit due within one year	(184,374)	--
Amortization of premium related to restricted securities	146,105	--
Capital gain from sale of property and equipment	(5,744)	(3,163)
Accrued severance pay, net	(474,575)	24,984
Increase in deferred tax assets	(16,499)	--

Changes in operating asset and liability items:		
Decrease (increase) in trade receivables	725,593	(1,495,380)
Increase in unbilled revenues	(1,259,720)	--
Decrease in notes receivable	283,078	--
Increase in other accounts receivable and prepaid expenses	(447,270)	(232,303)**
Decrease (increase) in inventories	(2,895,083)	130,404
Increase (decrease) in trade payables	955,347	(320,782)
Increase in deferred revenues	2,092,736	--
Decrease in accounts payable and accruals	202,891	444,651
Net cash used in operating activities from continuing operations (reconciled from .... continuing operations)	(1,030,042)	(2,436,814)
Net cash used in operating activities from discontinued operations (reconciled from discontinued operations)	(211,628)	(360,502)
Net cash used in operating activities	(1,241,670)	(2,797,316)
CASH FLOWS FROM INVESTING ACTIVITIES:		

</TABLE>

<TABLE>
<CAPTION>

	Nine months ended September 30,	
	2004	2003*
<S>	<C>	<C>
Repayment of promissory note related to purchase of subsidiary	(1,150,000)	(750,000)
Investment in subsidiary(1)	(7,190,777)	--
Investment in subsidiary(2)	(12,129,103)	--
Investment in subsidiary(3)	(17,302,167)	--
Proceeds from sale of marketable securities, net	812	--
Repayment of loan granted to shareholder	32,397	9,280**
Purchase of intangible assets and inventory	--	(196,331)
Purchase of property and equipment	(1,121,991)	(417,530)
Loans granted to stockholders, net	--	(13,737)**
Increase in capitalized research and development projects	(304,108)	(169,548)**
Proceeds from sale of property and equipment	93,786	7,585
Decrease (increase) in demo inventories, net	(26,970)	8,733
Decrease (increase) in restricted securities and deposits, net	(13,111,519)	585,807
Net cash used in investing activities	(52,209,640)	(935,741)
FORWARD	$(53,451,310)	$ (3,733,057)

</TABLE>

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* Restated.
** Reclassified.

<TABLE>
<CAPTION>

	Nine months ended September 30,	
	2004	2003*
<S>	<C>	<C>
FORWARD	$(53,451,310)	$ (3,733,057)
CASH FLOWS FROM FINANCING ACTIVITIES:		
Decrease in short-term credit from banks	(419,085)	(93,799)
Proceeds from issuance of share capital, net	24,319,890	--
Proceeds from exercise of options	1,094,156	57,285
Proceeds from exercise of warrants	19,387,651	1,730,732
Payment on capital lease obligation	(2,888)	(343)
Repayment of long-term loans	(42,529)	--
Issuance of convertible debenture	--	3,238,662**

Net cash provided by financing activities	44,337,195	4,932,537
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	(9,114,115)	1,199,480
CASH EROSION DUE TO EXCHANGE RATE DIFFERENCES	2,865	(4,063)
BALANCE OF CASH AND CASH EQUIVALENTS AT THE BEGINNING OF THE PERIOD	13,685,125	1,457,526
BALANCE OF CASH AND CASH EQUIVALENTS AT THE END OF THE PERIOD	$ 4,573,875	$ 2,652,943
SUPPLEMENTARY INFORMATION ON NON-CASH TRANSACTIONS:		
Issuance of shares and warrants against accrued expenses	$ 1,310,394	$ --
Exercise of options and warrants against notes receivable	$ 6,100	$ --
Issuance expenses against account payable	$ 155,002	$ --
Purchase of property and equipment against accounts payable	$ 32,841	$ --
Purchase of intangible assets against notes receivable	$ --	$ 300,000
Increase of investment in subsidiary against shares of common stock	$ --	$ 123,480
Investment in subsidiary against promissory note	$ 2,940,985	$ --
Conversion of promissory note to shares of common stock	$ --	$ 450,000
Exercise of convertible debentures against shares	$ 3,112,500	$ 1,500,000
Liability in connection to warrants granted	$ 10,841,020	$ --
Compensation related to issuance of warrants in connection with convertible debenture and beneficial conversion feature of convertible debentures	$ --	$ 1,890,000
SUPPLEMENTAL DISCLOSURE OF CASH FLOWS INFORMATION - CASH PAID DURING THE PERIOD FOR:		
Interest	$ (404,503)	$ (24,384)

</TABLE>

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* Restated.

** Reclassified.

- --

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

- --

(1) In January 2004, the Company acquired substantially all of the outstanding ordinary shares of Epsilor Electronic Industries, Ltd. ("Epsilor"). The net fair value of the assets acquired and the liabilities assumed, at the date of acquisition, was as follows:

Working capital, excluding cash and cash equivalents (unaudited)	$ (688,592)
Property and equipment (unaudited)	709,847
Intangible assets and goodwill (unaudited)	10,110,507
	10,131,762
Issuance of promissory note (unaudited)	(2,940,985)
	$ 7,190,777

(2) In January 2004, the Company acquired all of the outstanding common stock of FAAC Incorporated ("FAAC"). The net fair value of the assets acquired was as follows:

Working capital, excluding cash and cash equivalents (unaudited)	$ 2,647,822
Property and equipment (unaudited)	263,669
Intangible assets and goodwill (unaudited)	11,221,290
	14,132,781
Issuance of shares, net (unaudited)	(2,003,678)
	$ 12,129,103

(3) In August 2004, the Company acquired all of the outstanding common stock

of Armour of America, Incorporated ("AoA"). The net fair value of the assets acquired was as follows:

Working capital, excluding cash and cash equivalents (unaudited)	$ 3,219,728
Property and equipment (unaudited)	997,148
Intangible assets and goodwill (unaudited)	13,085,291
	$ 17,302,167

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

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS (UNAUDITED)

NOTE 1: BASIS OF PRESENTATION

a. Company:

Arotech Corporation, formerly known as Electric Fuel Corporation ("Arotech" or the "Company"), and its subsidiaries provide defense and security products for the military, law enforcement and homeland security markets, including advanced zinc-air and lithium batteries and chargers, multimedia interactive simulators/trainers and lightweight vehicle armoring. The Company is primarily operating through IES Interactive Training Systems, Inc., a wholly-owned subsidiary based in Littleton, Colorado; FAAC Corporation, a wholly-owned subsidiary based in Ann Arbor, Michigan; Electric Fuel Battery Corporation, a wholly-owned subsidiary based in Auburn, Alabama; Electric Fuel Ltd. ("EFL") a wholly-owned subsidiary based in Beit Shemesh, Israel; Epsilor Electronic Industries, Ltd., a wholly-owned subsidiary located in Dimona, Israel; M.D.T. Protective Industries, Ltd., a majority-owned subsidiary based in Lod, Israel; MDT Armor Corporation, a majority-owned subsidiary based in Auburn, Alabama; and Armour of America, Incorporated, a wholly-owned subsidiary based in Los Angeles, California.

In June 2004, the Company established a European subsidiary in Germany, Arotech Europa, in order to market Arotech's simulation and armoring products.

b. Restatement of previously-issued financial statements:

During management's review of the Company's interim financial statements for the period ended September 30, 2004 the Company, after discussion with and based on a new and revised review of accounting treatment by its independent auditors, conducted a comprehensive review on the re-pricing of warrants and grant of new warrants to certain of its investors and others during 2003 and 2004. As a result of that review, the Company, upon recommendation of management and with the approval of the Audit Committee of the Board of Directors after discussion with the Company's independent auditors, reconsidered the accounting related to these transactions and is now reclassifying certain expenses as a deemed dividend, a non-cash item, instead of as general and administrative expenses due to the recognition of these transactions as capital transactions that should not be expensed. The consolidated financial statements for the nine and three months ended September 30, 2003 and for the year ended December 31, 2003 will be restated to record deemed dividends and to decrease general and administrative expenses accordingly. These restatements do not affect the balance sheet, the shareholders' equity or the cash flow statements. In addition and as a result of the remeasurement described above, the Company has reviewed assumptions used in the calculation of fair value of all warrants granted during the year 2003. As a result of this comprehensive review, the Company has decreased its general and administrative expenses in the amount of $150,000, related to errors found in valuation underlying assumptions of warrants granted as a result of a litigation settlement, in the financial statements for the year ended December 31, 2003.

In addition, during management's review of the Company's interim financial statements for the period ended September 30, 2004, the Company also reviewed its calculation of amortization of debt discount attributable to the beneficial conversion feature of convertible debentures. As a result of this review, the Company found errors which increased (decreased) its financial expenses for the nine and three months ended September 30, 2003 and for the year ended December 31, 2003. The errors were related to the debt discount attributable to the warrants and their related convertible debentures, whereby the Company understated the amount of amortization in the year ended December 31, 2003 attributable to the conversion of certain of the convertible debentures, and overstated the amount of amortization in the six months ended June 30, 2004 attributable to the exercise of certain of the warrants.

The impacts of certain of these restatements are summarized below:

Statement of Operations Data:

<TABLE>
<CAPTION>

	For the Three Months ended September 30, 2003		
	Previously Reported	Adjustment	As Restated
General and administrative expenses	$ 1,105,864	$ (123,085)	$ 982,779
Operating income	234,428	123,085	357,513
Financial expenses, net	100,761	(18,428)	82,333
Net income from continuing operations	77,093	141,513	218,606
Net income	74,808	141,513	216,321
Deemed dividend to certain stockholders of common stock	--	(94,676)	(94,676)
Net income attributable to common stockholders	$ 74,808	$ 46,837	$ 121,645
Basic and diluted net earnings per share from continuing operations	$ 0.00	$ 0.00	$ 0.00
Basic and diluted net earnings per share	$ 0.00	$ 0.00	$ 0.00

</TABLE>

<TABLE>
<CAPTION>

	For the Nine Months ended September 30, 2003		
	Previously Reported	Adjustment	As Restated
General and administrative expenses	$ 3,579,371	$ (123,085)	$ 3,456,286
Operating loss	2,597,043	(123,085)	2,473,958
Financial expenses, net	1,084,582	129,000	1,213,582
Net income from continuing operations	3,854,949	5,915	3,860,864
Net loss	3,774,066	5,915	3,779,981
Deemed dividend to certain stockholders of common stock	--	267,026	267,026
Net loss attributable to common stockholders	$ 3,774,066	$ 272,941	$ 4,047,007
Basic and diluted net loss per share from continuing operations	$ 0.10	$ 0.01	$ 0.11
Basic and diluted net loss per share	$ 0.10	$ 0.01	$ 0.11

</TABLE>

Balance sheet data:

<TABLE>
<CAPTION>

	As of December 31, 2003		
	Previously Reported	Adjustment	As Restated
Other accounts payable and accrued expenses	$ 4,180,411	$ (150,000)	$ 4,030,411
Convertible debenture	881,944	568,250	1,450,194
Total long term liabilities	4,066,579	568,250	4,634,829
Additional paid in capital	135,891,316	(188,903)	135,702,413
Accumulated deficit	(109,681,893)	(229,347)	(109,911,240)
Total shareholders' equity	22,044,127	(418,250)	21,625,877

Cash flow data:
</TABLE>

<TABLE>
<CAPTION>

	For the Nine Months ended September 30, 2003		
	Previously Reported	Adjustment	As Restated
Net loss	$ 3,774,066	$ (5,915)	$ 3,779,981

Stock based compensation related to repricing of warrants granted to investors and the grant of new warrants	152,844	(123,085)	29,759
Amortization of compensation related to beneficial conversion feature and warrants issued to holders of convertible debentures ..	1,005,001	129,000	1,134,001

</TABLE>

c. Basis of presentation:

The accompanying interim consolidated financial statements have been prepared by Arotech Corporation in accordance with generally accepted accounting principles in the United States and the rules and regulations of the Securities and Exchange Commission, and include the accounts of Arotech Corporation and its subsidiaries. Certain information and footnote disclosures, normally included in financial statements prepared in accordance with generally accepted accounting principles in the United States, have been condensed or omitted pursuant to such rules and regulations. In the opinion of the Company, the unaudited financial statements reflect all adjustments (consisting only of normal recurring adjustments) necessary for a fair presentation of its financial position at September 30, 2004 and its operating results and cash flows for the nine month periods ended September 30, 2004 and 2003.

The results of operations for the nine months ended September 30, 2004 are not necessarily indicative of results that may be expected for any other interim period or for the full fiscal year ending December 31, 2004.

The balance sheet at December 31, 2003 has been derived from the audited financial statements at that date but does not include all the information and footnotes required by generally accepted accounting principles for complete financial statements. These consolidated financial statements should be read in conjunction with the audited financial statements included in the Company's Annual Report on Form 10-K for the year ended December 31, 2003.

d. Revenue recognition according to Statement of Position 81-1, "Accounting for Performance of Construction-Type and Certain Production-Type Contracts"

Revenues from contracts that involve customization of FAAC's simulation system to customer specific specifications are recognized in accordance with Statement Of Position 81-1, "Accounting for Performance of Construction-Type and Certain Production-Type Contracts," using contract accounting on a percentage of completion method, in accordance with the "Input Method." The amount of revenue recognized is based on the percentage to completion achieved. The percentage to completion is measured by monitoring progress using records of actual time incurred to date in the project compared to the total estimated project requirement, which corresponds to the costs related to earned revenues. Estimates of total project requirements are based on prior experience of customization, delivery and acceptance of the same or similar technology and are reviewed and updated regularly by management. Provisions for estimated losses on uncompleted contracts are made in the period in which such losses are first determined, in the amount of the estimated loss on the entire contract. As of September 30, 2004 no such estimated losses were identified.

e. Right of return:

When a right of return exists, the Company defers its revenues until the expiration of the period in which returns are permitted.

f. Available-for-sale marketable securities

The Company and its subsidiaries account for investments in debt and equity securities in accordance with Statement of Financial Accounting Standard No. 115, "Accounting for Certain Investments in Debt and Equity Securities" ("SFAS No. 115"). Management determines the appropriate classification of its investments in debt and equity securities at the time of purchase and reevaluates such determinations at each balance sheet date.

Securities classified as available for sale are stated at fair value, with unrealized gains and losses reported in accumulated other comprehensive income (loss), a separate component of shareholders' equity, net of taxes. Realized gains and losses on sales of investments, as determined on a specific identification basis, are included in the consolidated statement of operations.

g. Accounting for stock-based compensation:

The Company has elected to follow Accounting Principles Board Opinion No. 25, "Accounting for Stock Issued to Employees" ("APB No. 25") and FASB No. Interpretation No. 44, "Accounting for Certain Transactions Involving Stock Compensation" ("FIN No. 44") in accounting for its employee stock option plans. Under APB No. 25, when the exercise price of the Company's stock options is less than the market price of the underlying shares on the date of grant, compensation expense is recognized.

The Company adopted the disclosure provisions of Statement of Financial Accounting Standard No. 148, "Accounting for Stock-Based Compensation -

Transition and Disclosure" ("SFAS No. 148"), which amended certain provisions of Statement of Financial Accounting Standard No. 123 "Accounting for Stock-Based Compensation" ("SFAS No. 123"), to provide alternative methods of transition for

an entity that voluntarily changes to the fair value based method of accounting for stock-based employee compensation. The Company continues to apply the provisions of APB No. 25 in accounting for stock-based compensation.

Under Statement of Financial Accounting Standard No. 123 "Accounting for Stock-Based Compensation ("SFAS No. 123"), pro forma information regarding net income and net earnings per share is required, and has been determined as if the Company had accounted for its employee stock options under the fair value method of SFAS No. 123. The fair value for these options is amortized over their vesting period and estimated at the date of grant using a Black-Scholes Option Valuation Model with the following weighted-average assumptions for the nine and three month periods ended September 30, 2004 and 2003:

<TABLE>
<CAPTION>

	Nine months ended September 30,		Three months ended September 30,	
	2004	2003	2004	2003
		(Unaudited)		
<S>	<C>	<C>	<C>	<C>
Risk free interest	3.38	1.0%	3.38	1.0%
Dividend yields	0.0%	0.0%	0.0%	0.0%
Volatility	0.817	0.69	0.817	0.69
Expected life	5 years	4 years	5 years	4 years

</TABLE>

Pro forma information under SFAS No. 123:

<TABLE>
<CAPTION>

	Nine months ended September 30,		Three months ended September 30,	
	2004	2003*	2004	2003*
		Unaudited (U.S. Dollars, except per share data)		
<S>	<C>	<C>	<C>	<C>
Net income (loss) as reported	$ (9,116,124)	$ (4,047,007)	$ (1,039,107)	$ 121,645
Add - stock-based compensation expense determined under APB 25	536,958	--	174,787	--
Deduct - stock based compensation expense determined under fair value method for all awards	(1,605,146)	(2,073,362	(745,546)	(660,205)
Pro forma net loss	$ (10,184,312)	$ (6,120,369)	$ (1,609,866)	$ (538,560)
Loss per share:				
Basic and diluted, as reported	$ (0.14)	$ (0.11)	$ (0.01)	$ 0.00
Pro forma basic and diluted	$ (0.15)	$ (0.16)	$ (0.02)	$ (0.01)

- ------------------------------------
* Restated. See also Note 1.b.
</TABLE>

NOTE 2: ACQUISITION OF EPSILOR

In January 2004, the Company entered into a stock purchase agreement between itself and all of the shareholders of Epsilor Electronic Industries, Ltd. ("Epsilor"), pursuant to the terms of which the Company purchased all of the outstanding shares of Epsilor from Epsilor's existing shareholders. Epsilor develops and sells rechargeable and primary lithium batteries and smart chargers to the military, and to private industry in the Middle East, Europe and Asia.

The Acquisition was accounted under the purchase method accounting. Accordingly, all assets and liabilities acquired were recorded at their estimated market values as of the date of acquisition, and results of Epsilor's operations have been included in the consolidated financial statements commencing the date of

acquisition. The total consideration of $10,131,762 (including transaction costs) for the shares purchased consisted of (i) cash in the amount of $7,000,000, and (ii) a series of three $1,000,000 promissory notes, due on the first, second and third anniversaries of the agreement, which were recorded at their fair value of $2,940,985.

Based upon a valuation of tangible and intangible assets acquired, Arotech has allocated the total cost of the acquisition to Epsilor's net assets as follows (unaudited):

Tangible assets acquired	$ 2,313,277
Intangible assets	
Technology	159,364
Customer list	4,889,671
Goodwill	5,061,472
Liabilities assumed	(2,292,022)
Total consideration	$10,131,762

Intangible assets in the amount of $5,049,035 have a weighted-average useful life of approximately ten years.

In accordance with SFAS No. 142, "Goodwill and Other Intangible Assets," goodwill arising from acquisitions will not be amortized. In lieu of amortization, Arotech is required to perform an annual impairment test. If Arotech determines, through the impairment review process, that goodwill has been impaired, it will record the impairment charge in its statement of operations. Arotech will also assess the impairment of goodwill whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

The value assigned to tangible, intangible assets and liabilities was determined as follows:

1. To determine the estimated market value of Epsilor's net current assets, property and equipment, and net liabilities, the "Cost Approach" was used. According to the valuation made, the book values for the current assets and liabilities were reasonable proxies for their market values.

2. The amount of the excess cost attributable to technology of developing a system with battery and charger was determined using the Cost Approach, and was valued at $159,364.

3. The customer list is the asset that generates most of the Company's sales. Hence, the "Income Approach" was used to estimate its value, resulting in a value of $4,889,671.

See Note 5 for pro forma financial information.

NOTE 3: ACQUISITION OF FAAC

In January of 2004, the Company entered into a stock purchase agreement with the shareholders of FAAC Incorporated ("FAAC"), pursuant to the terms of which it acquired all of the issued and outstanding common stock of FAAC, a leading provider of driving simulators, systems engineering and software products to the United States military, government and private industry.

The Acquisition was accounted under the purchase method accounting. Accordingly, all assets and liabilities were recorded at their estimated market values as of the date acquired, and results of FAAC's operations have been included in the consolidated financial statements commencing the date of acquisition. The consideration for the purchase consisted of (i) cash in the amount of $12.0 million, and (ii) the issuance of a total of 1,003,856 shares of our common stock, $0.01 par value per share, having a value of approximately $2.0 million. Additionally, there is an earn-out based on 2004 net pretax profit, with an additional earn-out on the 2005 net profit from certain specific and limited programs. When the contingency on the earn-out provision is resolved, the additional consideration will be recorded as additional purchase price. The total consideration of $14.1 million (including $135,131 of transaction costs) was determined based upon arm's-length negotiations between the Company and FAAC's shareholders.

Based upon a valuation of tangible and intangible assets acquired, Arotech has allocated the total cost of the acquisition to FAAC's assets as follows (unaudited):

Tangible assets acquired	$ 5,684,584
Intangible assets	
Technology	4,610,000
Existing contracts	636,000
Customer list	1,125,000
Trademarks	374,000
Goodwill	4,476,290
Liabilities assumed	(2,770,843)
Total consideration	$14,135,031

Intangible assets in the amount of $6,385,000 have a weighted-average useful life of approximately eight years.

In accordance with SFAS No. 142, "Goodwill and Other Intangible Assets," goodwill arising from acquisitions will not be amortized. In lieu of amortization, Arotech is required to perform an annual impairment test. If Arotech determines, through the impairment review process, that goodwill has been impaired, it will record the impairment charge in its statement of operations. Arotech will also assess the impairment of goodwill whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

The value assigned to tangible, intangibles assets and liabilities was determined as follows:

1. To determine the estimated fair value of FAAC's net current assets, property and equipment, and net liabilities, the "Cost Approach" was used. According to the valuation made, the book values for the current assets and liabilities were reasonable proxies for their market values.

2. The amount of the cost attributable to technology of the software, documentation and know-how that drives the vehicle simulators and the high-speed missile fly-out simulators is $4,610,000 and was determined using the "Income Approach."

3. FAAC's sales are all made on a contractual basis, most of which are over a relatively long period of time. At the date of the purchase FAAC had

several signed contracts at various stages of completion. The value of the existing contracts was determined using the Income approach and resulting in a value of $636,000.

4. FAAC's customer list includes various branches of the U.S. military, major defense contractors, various city and country governments and others. Since customer relationship represent one of the most important revenue generating assets for FAAC, its value was estimated using the Income Approach, resulting in a value of $1,125,000.

5. FAAC's trade name value represents the name recognition value of the FAAC brand name as a result of advertising spending by the company. The Cost Approach was used to determine the value of FAAC's trade name in the amount of $360,000.

See Note 5 for pro forma financial information.

NOTE 4: ACQUISITION OF AOA

In August 2004, the Company purchased all of the outstanding stock of Armour of America, Incorporated, a California corporation ("AoA"), from AoA's existing shareholder. The assets acquired through the purchase of all of AoA's outstanding stock consisted of all of AoA's assets, including AoA's current assets, property and equipment, and other assets (including intangible assets such as intellectual property and contractual rights).

The total purchase price consisted of $19,000,000 in cash, with additional possible earn-outs if AoA is awarded certain material contracts. An additional $3,000,000 was to be paid into an escrow account pursuant to the terms of an escrow agreement, to secure a portion of the Earnout Consideration. Pursuant to the purchase agreement, the total consideration, sale price plus Earnout Consideration, will not be in excess of $40,000,000. When the contingency on the earn-out provision is resolved, the additional consideration will be recorded as additional purchase price. The purchase price also included $83,837 of transaction costs. The transaction has been accounted for using the purchase method of accounting, and accordingly, the purchase price has been allocated to the assets acquired and liabilities assumed based upon their fair values at the date the acquisition was completed.

Based upon a preliminary valuation of tangible and intangible assets acquired, Arotech has allocated the total cost of the acquisition to AoA's assets as follows (unaudited):

Tangible assets acquired	$ 6,346,316
Intangible assets	
Patent	1,969
Certifications	245,000
Backlog	1,583,000
Customer relationships	490,000
Tradename /Trademark	70,000
Covenants not to compete	260,000
Goodwill and workforce in place	10,435,322
Liabilities assumed	(347,770)
Total consideration	$19,083,837

Intangible assets in the amount of $2,648,000 have a weighted-average useful life of approximately two years.

In accordance with SFAS No. 142, "Goodwill and Other Intangible Assets," goodwill arising from acquisitions will not be amortized. In lieu of amortization, Arotech is required to perform an annual impairment test. If Arotech determines, through the impairment review process, that goodwill has been impaired, it will record the impairment charge in its statement of operations. Arotech will also assess the impairment of goodwill whenever events or changes in circumstances indicate that the carrying value may not be recoverable.

See Note 5 for pro forma financial information.

NOTE 5: PRO FORMA FINANCIAL INFORMATION

In January 2004, the Company acquired FAAC and Epsilor, as more fully described in "Note 2 - Acquisition of Epsilor" and "Note 3 - Acquisition of FAAC," above, and in August 2004, the Company acquired AoA, as more fully described in "Note 4 - - Acquisition of AoA," above (the "Acquisitions"). The following summary pro forma information includes the effects of the Acquisitions on the operating results of the Company. The pro forma data for the nine months ended September 30, 2004 and 2003 are presented as if the Acquisitions had been completed on January 1, 2004 and 2003, respectively. This pro forma financial information does not purport to be indicative of the results of operations that would have occurred had the Acquisitions taken place at the beginning of the period, nor do they purport to be indicative of the results of operations that will be obtained in the future.

<TABLE>
<CAPTION>

	Nine Months Ended September 30,	
	2004	2003*
	(in thousands, except per share data) (Unaudited)	
<S>	<C>	<C>
Total revenues	$ 44,515,874	$ 27,869,907
Gross profit	15,783,252	12,798,206
Net loss	(2,932,378)	(3,381,393)
Deemed dividend of common stock attributable to certain shareholders	(3,328,952)	(267,026)
Net loss attributable to stockholders of common stock	$ (6,261,330)	$ (3,648,419)
Basic and diluted net loss per share	$ (0.09)	$ (0.07)
Weighted average number of shares used in computing basic net loss per share	67,072,069	51,352,416

\- ------------------------

* Restated.
</TABLE>

NOTE 6: INVENTORIES

Inventories are stated at the lower of cost or market value. Cost is determined using the average cost method. The Company periodically evaluates the quantities on hand relative to current and historical selling prices and historical and projected sales volume. Based on these evaluations, provisions are made in each period to write down inventory to its net realizable value. Inventories write-offs are provided to cover risks arising from slow-moving items, technological obsolescence, excess inventories, and for market prices lower than cost. In the nine months ended September 30, 2004 the Company wrote off inventory in the amount of $67,951, which has been included in cost of revenues. Inventories are composed of the following:

	September 30, 2004	December 31, 2003
	(Unaudited)	(Note 1.b.)
Raw materials	$ 2,553,612	$ 657,677
Work-in-progress	4,221,470	634,221
Finished goods	856,111	622,850
	$ 7,631,193	$ 1,914,748

NOTE 7: IMPACT OF RECENTLY ISSUED ACCOUNTING STANDARDS

In January 2003, the FASB issued Interpretation No. 46, "Consolidation of Variable Interest Entities" ("FIN No. 46") which clarifies the application of Accounting Research Bulletin (ARB) No. 51, "Consolidated Financial Statements," relating to consolidation of certain entities. First, FIN No. 46 requires identification of the Company's participation in variable interest entities (VIEs), which are defined as entities with a level of invested equity that is not sufficient to fund future activities to permit them to operate on a stand-alone basis, or whose equity holders lack certain characteristics of a controlling financial interest. Then, for entities identified as VIEs, FIN No. 46 sets forth a model to evaluate potential consolidation based on an assessment of which party to the VIE, if any, bears a majority of the exposure to its expected losses, or stands to gain from a majority of its expected returns. FIN No. 46 is effective for all new VIEs created or acquired after January 31, 2003. For VIEs created or acquired prior to February 1, 2003, the provisions of FIN No. 46 must be applied for the first interim or annual period beginning after December 15, 2003. FIN No. 46 also sets forth certain disclosures regarding interests in VIEs that are deemed significant, even if consolidation is not required. The adoption of FIN No. 46 has not had a material impact on the Company's results of operations or financial position.

NOTE 8: SEGMENT INFORMATION

a. General:

The Company and its subsidiaries operate primarily in three business segments and follow the requirements of SFAS No. 131.

Prior to its purchase of FAAC, Epsilor and AoA, the Company had managed its business in two reportable segments organized on the basis of differences in its related products and services. With the acquisition of FAAC and Epsilor early in 2004, the Company reorganized into three segments: Simulation, Training and Consulting; Battery and Power Systems; and Armored Vehicles. As a result the Company restated information previously reported in order to comply with new segment reporting.

The Company's reportable operating segments have been determined in accordance with the Company's internal management structure, which is organized based on operating activities. The accounting policies of the operating segments are the same as those of the Company. The Company evaluates performance based upon two primary factors, one is the segment's operating income and the other is based on the segment's contribution to the Company's future strategic growth.

b. The following is information about reported segment revenues, income (losses) and assets for the nine and three months ended September 30, 2004 and 2003:

<TABLE>
<CAPTION>

<S>	Simulation, Training and Consulting <C>	Battery and Power Systems <C>	Armored Vehicles <C>	All Others <C>	Total <C>
Nine months ended September 30, 2004					
Revenues from outside customers	$ 13,258,943	$ 8,046,095	$ 12,077,985	$ --	$ 33,383,023
Depreciation expenses and amortization (1)	(1,225,248)	(855,797)	(941,342)	(130,000)	(3,152,387)
Direct expenses (2)	(11,947,426)	(7,476,476)	(10,650,363)	(3,818,306)	(33,892,571)
Segment gross profit (loss)	$ 86,269	$ (286,178)	$ 486,280	$ (3,948,306)	(3,661,935)
Financial expenses (after deduction of minority interest)					(2,125,237)
Net loss from continuing operations					$ (5,787,172)
Segment assets (3)	$ 18,393,997	$ 12,914,008	$ 20,367,854	$ 698,516	$ 52,374,375
Nine months ended September 30, 2003					
Revenues from outside customers	$ 5,760,231	$ 4,697,143	$ 2,775,112	$ --	$ 13,232,486
Depreciation expenses and amortization	(634,188)	(339,572)	(139,522)	(143,000)	(1,256,282)
Direct expenses (2)	(5,139,480)	(4,339,425)	(2,834,817)	(2,317,071)*	(14,630,793)
Segment gross profit (loss)	$ (13,436)	$ 18,146	$ (199,227)	$ (2,460,071)	(2,654,589)
Financial expenses (after deduction of minority interest)					(1,206,275)*
Net loss from continuing operations					$ (3,860,864)
Segment assets (3)	$ 7,098,090	$ 1,404,092	$ 1,930,079	$ 394,755	$ 10,827,016
Three months ended September 30, 2004					
Revenues from outside customers	$ 6,034,299	$ 2,913,705	$ 7,324,517	$ --	$ 16,272,521

Depreciation expenses and amortization (1)	(417,005)	(291,806)	(882,219)	(51,000)	(1,642,030)
Direct expenses (1)	(5,010,108)	(2,398,561)	(6,245,370)	(957,319)	(14,611,358)
Segment gross profit (loss)	$ 607,186	$ 223,338	$ 196,928	$ (1,008,319)	19,133
Financial income (after deduction of minority interest)					1,107,712
Net income from continuing operations					$ 1,126,845
Three months ended September 30, 2003					
Revenues from outside customers	$ 2,918,866	$ 1,844,061	$ 942,971	$ --	$ 5,705,898
Depreciation expenses and amortization	(90,545)	(113,524)	(32,269)	(48,000)	(284,338)
Direct expenses (2)	(2,083,404)	(1,580,982)	(780,071)	(676,194)*	(5,120,651)*
Segment gross profit (loss)	$ 744,917	$ 149,555	$ 130,631	$ (724,194)	300,909
Financial expenses (after deduction of minority interest)					(82,303)*
Net income from continuing operations					$ 218,606*

</TABLE>

- ------------------------------------
* Restated

(1) Includes depreciation of property and equipment, amortization expenses of intangible assets and other amortization expenses.
(2) Including sales and marketing, general and administrative and tax expenses.
(3) Consisting of property and equipment, inventory and intangible assets.

NOTE 9: CONVERTIBLE DEBENTURES AND DETACHABLE WARRANTS

a. 9% Secured Convertible Debentures due June 30, 2005

Pursuant to the terms of a Securities Purchase Agreement dated December 31, 2002, the Company issued and sold to a group of institutional investors an aggregate principal amount of 9% secured convertible debentures in the amount of $3.5 million due June 30, 2005. These debentures are convertible at any time prior to June 30, 2005 at a conversion price of $0.75 per share. The conversion price of these debentures was adjusted to $0.64 per share in April 2003. In accordance with EITF 96-19, "Debtor's Accounting for a Modification or Exchange of Debt Instruments," the terms of convertible debentures are not treated as changed or modified when the cash flow effect on a present value basis is less than 10%, and therefore the Company did not record any compensation related to the change in the conversion price of the convertible debentures.

As part of the Securities Purchase Agreement dated December 31, 2002, the Company issued to the purchasers of its 9% secured convertible debentures due June 30, 2005, warrants, as follows: (i) Series A Warrants to purchase an aggregate of 1,166,700 shares of common stock at any time prior to December 31, 2007 at a price of $0.84 per share; (ii) Series B Warrants to purchase an aggregate of 1,166,700 shares of common stock at any time prior to December 31, 2007 at a price of $0.89 per share; and (iii) Series C Warrants to purchase an aggregate of 1,166,700 shares of common stock at any time prior to December 31, 2007 at a price of $0.93 per share. The exercise price of these warrants was adjusted to $0.64 per share in April 2003.

During the nine months ended September 30, 2004, the remaining principal amount of $1,150,000 of 9% secured convertible debentures outstanding was converted into an aggregate of 1,796,875 shares of common stock.

This transaction was accounted according to APB No. 14 "Accounting for Convertible Debt and Debt Issued with Stock Purchase Warrants" and Emerging Issue Task Force No. 00-27 "Application of Issue No. 98-5 to Certain Convertible Instruments" ("EITF 00-27"). The fair value of these warrants was determined using Black-Scholes pricing model, assuming a risk-free interest rate of 3.5%, a volatility factor 64%, dividend yields of 0% and a contractual life of five years.

In connection with these convertible debentures, the Company recognized $1,890,000 with respect to the beneficial conversion feature, which was amortized from the date of issuance to the actual conversion dates as financial expenses.

During the nine months ended September 30, 2004, the Company recorded an expense of $372,600, all which was attributable to the accelerated amortization of debt discount and beneficial conversion feature due to conversion of the convertible debenture into shares. This expense was included in financial expenses.

b. 8% Secured Convertible Debentures due September 30, 2006 and issued in September 2003

Pursuant to the terms of a Securities Purchase Agreement dated September 30,

2003, the Company, in September 2003, issued and sold to a group of institutional investors an aggregate principal amount of 8% secured convertible

debentures in the amount of $5.0 million due September 30, 2006. These debentures are convertible at any time prior to September 30, 2006 at a conversion price of $1.15 per share (see also Note 10.b).

As part of the Securities Purchase Agreement dated September 30, 2003, the Company issued to the purchasers of its 8% secured convertible debentures due September 30, 2006, warrants to purchase an aggregate of 1,250,000 shares of common stock at any time prior to September 30, 2006 at a price of $1.4375 per share. During the nine months ended September 30, 2004, an aggregate of 687,500 shares were issued pursuant to exercises of these warrants.

During the nine months ended September 30, 2004, a total of $350,000 principal amount of debentures was converted, at a conversion price of $1.15 per share. As of September 30, 2004, $875,000 remained outstanding under these debentures.

This transaction was accounted according to APB No. 14 "Accounting for Convertible Debt and Debt Issued with Stock Purchase Warrants" and Emerging Issue Task Force No. 00-27 "Application of Issue No. 98-5 to Certain Convertible Instruments" ("EITF 00-27"). The fair value of these warrants was determined using Black-Scholes pricing model, assuming a risk-free interest rate of 1.95%, a volatility factor 98%, dividend yields of 0% and a contractual life of three years.

In connection with these convertible debentures, the Company recognized financial expenses of $2,963,043 with respect to the beneficial conversion feature, which is being amortized from the date of issuance to the stated redemption date - September 30, 2006 - as financial expenses.

During the nine months ended September 30, 2004 the Company recorded an expense of $319,636, of which $148,369 was attributable to amortization of debt discount and beneficial conversion features related to the convertible debenture over its term, and $171,267 of which was attributable to amortization due to conversion of the convertible debentures into shares during the nine months ended September 30, 2004. These expenses were included in the financial expenses.

c. 8% Secured Convertible Debentures due September 30, 2006 and issued in December 2003

Pursuant to the terms of a Securities Purchase Agreement dated September 30, 2003, the Company, in December 2003, issued and sold to a group of institutional investors an aggregate principal amount of 8% secured convertible debentures in the amount of $6.0 million due September 30, 2006. These debentures are convertible at any time prior to September 30, 2006 at a conversion price of $1.45 per share (see also Note 10.c.).

During the nine months ended September 30, 2004, a total of $1,612,500 principal amount of debentures was converted, at a conversion price of $1.45 per share. As of September 30, 2004, $4,387,500 remained outstanding under these debentures.

As a further part of the Securities Purchase Agreement dated September 30, 2003, the Company issued to the purchasers of its 8% secured convertible debentures due December 31, 2006, warrants to purchase an aggregate of 1,500,000 shares of common stock at any time prior to December 31, 2006 at a price of $1.8125 per share. Additionally, the Company issued to the investors supplemental warrants to purchase an aggregate of 1,038,000 shares of common stock at any time prior to June 18, 2009 at a price of $2.20 per share.

During the nine months ended September 30, 2004 an aggregate of 1,500,000 shares were issued pursuant to exercise of these warrants. Out of these warrants, the holders of 1,125,000 warrants exercised their warrants on July 14, 2004 were granted an additional warrants to purchase 1,125,000 shares of common stock of the Company at an exercise price per share of $1.38. The fair value of the new warrants was determined using Black-Scholes pricing model, assuming a risk-free interest rate of 3.5%, a volatility factor 79%, dividend yields of 0% and a contractual life of five years (see also Note 11.b.).

This transaction was accounted according to APB No. 14, "Accounting for Convertible Debt and Debt Issued with Stock Purchase Warrants" and Emerging Issue Task Force No. 00-27, "Application of Issue No. 98-5 to Certain Convertible Instruments" ("EITF 00-27"). The fair value of the warrants granted in respect of convertible debentures was determined using Black-Scholes pricing model, assuming a risk-free interest rate of 2.45%, a volatility factor 98%, dividend yields of 0% and a contractual life of three years.

In connection with these convertible debentures, the Company recognized financial expenses of $6,000,000 with respect to the beneficial conversion feature, which is being amortized from the date of issuance to the stated redemption date - September 30, 2006 - as financial expenses.

During the nine months ended September 30, 2004 the Company recorded an expense of $2,762,440, of which $1,398,879 was attributable to amortization of the beneficial conversion feature of the convertible debenture over its term, and $1,363,561 of which was attributable to amortization due to conversion of the convertible debentures into shares. These expenses were included in the financial expenses.

NOTE 10: WARRANTS

a. Warrants issued to an investor

In November 2000 and May 2001, the Company issued a total of 916,667 warrants to an investor, which warrants contained certain antidilution provisions: a Series A warrant to purchase 666,667 shares of the Company's common stock at a price of $3.50 per share, and a Series C warrant to purchase 250,000 shares at a price of $3.08 per share. Operation of the antidilution provisions provided that the Series A warrant should be adjusted to be a warrant to purchase 888,764 shares at a price of $2.67 per share, and the Series C warrant should be adjusted to be a warrant to purchase 333,286 shares at a price of $2.35 per share. After negotiations, the investor agreed to exercise its warrants immediately, in exchange for an exercise price reduction to $1.45 per share, and the issuance of a new six-month Series D warrant to purchase 1,222,050 shares at an exercise price of $2.10 per share. The new Series D warrant does not have similar antidilution provisions. As a result of this repricing and the issuance of new warrants, the Company recorded a deemed dividend in the amount of approximately $1,163,000 in the nine months ended September 30, 2004.

b. Warrants issued in January 2004

In connection with the Securities Purchase Agreement referred to in Note 11.a below, the Company granted three-year warrants to purchase up to an aggregate of 9,840,426 shares of the Company's common stock at any time beginning six months after closing at an exercise price per share of $1.88.

During the nine months ended September 30, 2004 an aggregate of 7,446,811 shares were issued pursuant to exercise of these warrants. In connection with the exercise of the warrants, the Company granted to the same investors five-year warrants to purchase up to an aggregate of 7,446,811 shares of the Company's common stock at an exercise price per share of $1.38. The fair value of these warrants was determined using Black-Scholes pricing model, assuming a risk-free interest rate of 3.5%, a volatility factor 79%, dividend yields of 0% and a contractual life of five years. See also Note 11.b.

c. Warrants issued in May 2001

As part of the investment agreement in May 2001, the Company issued to one of its investors warrants to purchase shares of common stock at a price of $3.22 per share; these warrants are exercisable by the holder at any time after November 8, 2001 and will expire on May 8, 2006. On July 14, 2004, the Company repriced the warrants exercise price to $1.88 in order to induce their holders to exercise immediately. In connection with the exercise of the warrants, the Company additionally granted five-year warrants to purchase up to an aggregate of 145,454 shares of the Company's common stock at an exercise price per share of $1.38. The fair value of these warrants was determined using Black-Scholes pricing model, assuming a risk-free interest rate of 3.5%, a volatility factor 79%, dividend yields of 0% and a contractual life of five years. See also Note 11.b.

NOTE 11: ISSUANCE OF SHARES

a. Shares issued in January 2004:

Pursuant to the terms of a Securities Purchase Agreement dated January 7, 2004 by and between the Company and several institutional investors, the Company issued and sold an aggregate of 9,840,426 shares of the Company's common stock at a purchase price of $1.88 per share. Gross proceeds of this offering were approximately $18.5 million.

b. Shares and warrants issued in July 2004:

In July 2004, pursuant to a Securities Purchase Agreement dated July 15, 2004, the Company issued to a group of investors an aggregate of 4,258,065 shares of common stock at a price of $1.55 per share, or a total purchase price of $6,600,000.

On July 14, 2004, warrants to purchase 8,814,235 shares of common stock, having an aggregate exercise price of $16,494,194, net of issuance expenses, were exercised (see also Note 9.c and Note 10.b). Out of the shares issued in conjunction with the exercise of these warrants, 1,125,000 shares were issued upon exercise of warrants issued in the transaction referred to in Note 9.c above and 7,446,811 shares were issued upon exercise of warrants issued in the transaction referred to in the Note 10.b above; the remaining 242,424 shares were issued upon exercise of a warrant that the Company issued to an investor in May 2001 referred to in Note 10.c. In connection with this transaction, the Company issued to the holders of those exercising warrants an aggregate of 8,717,265 new five-year warrants to purchase shares of common stock at an exercise price of $1.38 per share. (See also Notes 9 c., 10.b. and 10.c.)

As a result of the aforesaid transactions, including the repricing of the warrants to the investors and the issuance of additional warrants to the investors, the Company recorded a deemed dividend in the amount of $2,165,952, to reflect the additional benefit created for these investors. The deemed

dividend increased the loss applicable to common stockholders in the calculation of basic and diluted net loss per share for the nine months ended September 30, 2004, without any effect on total shareholder's equity.

In addition, the Company recorded a liability related to the grant of these warrants, which are subject to the shareholders approval, which the Company intend to seek in its special shareholders meeting on December 14, 2004. This transaction was accounted according to Emerging Issue Task Force No.00-19, "Accounting for Derivative Financial Instruments Indexed to, and Potentially Settled in, a Company's Own Stock." Accordingly the fair value of these warrants was determined using Black-Scholes pricing model, assuming a risk-free interest rate of 3.5%, a volatility factor 79%, dividend yields of 0% and a contractual life of five years. The change in the fair value of the warrants between the date of grant and September 30, 2004 has been recorded as finance income during the nine months ended September 30, 2004 in the amount of $1,829,025.

NOTE 12: LITIGATION SETTLEMENT

On February 4, 2004, the Company entered into an agreement settling the litigation brought against it in the Tel-Aviv, Israel district court by I.E.S. Electronics Industries, Ltd. ("IES Electronics") and certain of its affiliates in connection with the Company's purchase of the assets of its IES Interactive Training, Inc. from IES Electronics in August 2002. The litigation had sought monetary damages in the amount of approximately $3.0 million.

Pursuant to the terms of the settlement agreement, in addition to agreeing to dismiss their lawsuit with prejudice, IES Electronics agreed (i) to cancel the Company's $450,000 debt to IES Electronics that had been due on December 31, 2003, and (ii) to transfer to the Company title to certain certificates of deposit in the approximate principal amount of $112,000.

In consideration of the foregoing, the Company issued to IES Electronics (i) 450,000 shares of its common stock, and (ii) five-year warrants to purchase up to an additional 450,000 shares of its common stock at a purchase price of $1.91 per share.

The fair value of the warrants was determined using Black-Scholes pricing model, assuming a risk-free interest rate of 3.5%, a volatility factor 79%, dividend yields of 0% and a contractual life of five years.

NOTE 13: RESTRICTED SECURITIES AND DEPOSITS

The restricted collateral deposit is invested in a $14,236,461 certificate of deposit that is used primarily to secure earn-out provisions in respect of the acquisition of FAAC and AoA and to secure that part of the Epsilor acquisition price that is paid in three installments.

FAAC	$ 5,942,970
Epsilor	2,000,000
AoA	5,996,850
Other	296,641
Total	14,236,461
Less current portion	13,236,461
Long-term portion ..	$ 1,000,000

ITEM 2. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

This report contains forward-looking statements made pursuant to the safe harbor provisions of the Private Securities Litigation Reform Act of 1995. These statements involve inherent risks and uncertainties. When used in this discussion, the words "believes," "anticipated," "expects," "estimates" and similar expressions are intended to identify such forward-looking statements. Such statements are subject to certain risks and uncertainties that could cause actual results to differ materially from those projected. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date hereof. We undertake no obligation to publicly release the result of any revisions to these forward-looking statements that may be made to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events. Our actual results could differ materially from those anticipated in these forward-looking statements as a result of certain factors including, but not limited to, those set forth elsewhere in this report. Please see "Risk Factors," below, and in our other filings with the

Securities and Exchange Commission.

Arotech(TM) is a trademark and Electric Fuel(R) is a registered trademark of Arotech Corporation. All company and product names mentioned may be trademarks or registered trademarks of their respective holders. Unless the context requires otherwise, all references to us refer collectively to Arotech Corporation and its subsidiaries.

We make available through our internet website free of charge our annual report on Form 10-K, quarterly reports on Form 10-Q, current reports on Form 8-K, amendments to such reports and other filings made by us with the SEC, as soon as practicable after we electronically files such reports and filings with the SEC. Our website address is www.arotech.com. The information contained in this website is not incorporated by reference in this report.

The following discussion and analysis should be read in conjunction with the interim financial statements and notes thereto appearing elsewhere in this Quarterly Report. We have rounded amounts reported here to the nearest thousand, unless such amounts are more than 1.0 million, in which event we have rounded such amounts to the nearest hundred thousand.

Executive Summary

Divisions and Subsidiaries

We operate primarily as a holding company, through our various subsidiaries, which we have organized into three divisions. Our divisions and subsidiaries (all 100% owned by us, unless otherwise noted) are as follows:

> Our Simulation, Training and Consulting Division, which develops, manufactures and markets advanced hi-tech multimedia and interactive digital solutions for use-of-force and driving training of military, law enforcement and security personnel, as well as offering security consulting and other services, consisting of:

o IES Interactive Training, Inc., located in Littleton, Colorado, which provides specialized "use of force" training for police, security personnel and the military ("IES");

o FAAC Incorporated, located in Ann Arbor, Michigan, which provides simulators, systems engineering and software products to the United States military, government and private industry ("FAAC"); and

o Arocon Security Corporation, located in New York, New York, which provides security consulting and other services, focusing on protecting life, assets and operations with minimum hindrance to personal freedom and daily activities ("Arocon").

> Our Battery and Power Systems Division, which manufactures and sells Zinc-Air and lithium batteries for defense and security products and other military applications and pioneers advancements in Zinc-Air battery technology for electric vehicles, consisting of:

o Electric Fuel Battery Corporation, located in Auburn, Alabama, which manufactures and sells Zinc-Air fuel sells, batteries and chargers for the military, focusing on applications that demand high energy and light weight ("EFB");

o Epsilor Electronic Industries, Ltd., located in Dimona, Israel (in Israel's Negev desert area), which develops and sells rechargeable and primary lithium batteries and smart chargers to the military and to private industry in the Middle East, Europe and Asia ("Epsilor"); and

o Electric Fuel (E.F.L.) Ltd., located in Beit Shemesh, Israel, which produces water-activated lifejacket lights for commercial aviation and marine applications, and which conducts our Electric Vehicle effort, focusing on obtaining and implementing demonstration projects in the U.S. and Europe, and on building broad industry partnerships that can lead to eventual commercialization of our Zinc-Air energy system for electric vehicles ("EFL").

> Our Armored Vehicle Division, which utilizes sophisticated lightweight materials and advanced engineering processes to armor vehicles, consisting of:

o MDT Protective Industries, Ltd., located in Lod, Israel, which specializes in using state-of-the-art lightweight ceramic materials, special ballistic glass and advanced engineering processes to fully armor vans and cars, and is a leading supplier to the Israeli military, Israeli special forces and special services ("MDT") (75.5% owned by us);

o MDT Armor Corporation, located in Auburn, Alabama, which conducts MDT's United States activities ("MDT Armor") (88% owned by us); and

o Armour of America, located in Los Angeles, California, which manufacturers aviation armor both for helicopters and for fixed wing

aircraft, marine armor, personnel armor, armoring kits for military vehicles, fragmentation

blankest and a unique ballistic/flotation vest (ArmourFloat) that is U.S. Coast Guard-certified ("AoA").

Restatement of Previously-Issued Financial Statements

During our management's review of our interim financial statements for the period ended September 30, 2004 we, after discussion with and based on a new and revised review of accounting treatment by our independent auditors, conducted a comprehensive review on the re-pricing of warrants and grant of new warrants to certain of our investors and others during the years 2004 and 2003. As a result of that review, we, upon recommendation of our management and with the approval of the Audit Committee of our Board of Directors after discussion with our independent auditors, reconsidered the accounting related to these transactions and are now reclassifying certain expenses as a deemed dividend, a non-cash item, instead of as general and administrative expenses due to the recognition of this transaction as a capital transaction that should not be expensed. The consolidated financial statements for the nine months ended September 30, 2003, for the six months ended June 2003 and 2004, for the three months ended March 31, 2004 and the year ended December 31, 2003 will be restated to record deemed dividends and to decrease general and administrative expenses accordingly. These restatements do not affect our balance sheet, shareholders' equity or cash flow statements. In addition and as a result of the remeasurement described above, we have reviewed assumptions used in the calculation of fair value of all warrants granted during the year 2003. As a result of this comprehensive review, we have decreased general and administrative expenses in the amount of $150,000, related to errors found in valuation underlying assumptions of warrants granted as a result of a litigation settlement, in the financial statements for the year ended December 31, 2003.

In addition, during our management's review of our interim financial statements for the period ended September 30, 2004, we also reviewed our calculation of amortization of debt discount attributable to the beneficial conversion feature of convertible debentures. As a result of this review, we found errors which increased (decreased) our financial expenses for the nine months ended September 30, 2003, for the six months ended June 2003 and 2004, for the three months ended March 31, 2004 and the year ended December 31, 2003. The errors were related to the debt discount attributable to the warrants and their related convertible debentures, whereby we understated the amount of amortization in the year ended December 31, 2003 attributable to the conversion of certain of the convertible debentures, and we overstated the amount of amortization in the six months ended June 30, 2004 attributable to the exercise of certain of the warrants.

The impacts of certain of these restatements are summarized below:

Statement of Operations Data:

<TABLE>
<CAPTION>

	For the Three Months ended September 30, 2003		
	Previously Reported	Adjustment	As Restated
<S>	<C>	<C>	<C>
General and administrative expenses	$ 1,105,864	$ (123,085)	$ 982,779
Operating income	234,428	123,085	357,513
Financial expenses, net	100,761	(18,428)	82,333
Net income from continuing operations	77,093	141,513	218,606
Net income	74,808	141,513	216,321
Deemed dividend to certain stockholders of common stock	--	(94,676)	(94,676)
Net income attributable to common stockholders	$ 74,808	$ 46,837	$ 121,645
Basic and diluted net earnings per share from continuing operations	$ 0.00	$ 0.00	$ 0.00
Basic and diluted net earnings per share	$ 0.00	$ 0.00	$ 0.00

<CAPTION>

	For the Nine Months ended September 30, 2003
	Previously

	Reported	Adjustment	As Restated
<S>	<C>	<C>	<C>
General and administrative expenses	$ 3,579,371	$ (123,085)	$ 3,456,286
Operating loss	2,597,043	(123,085)	2,473,958
Financial expenses, net	1,084,582	129,000	1,213,582
Net income from continuing operations	3,854,949	5,915	3,860,864
Net loss	3,774,066	5,915	3,779,981
Deemed dividend to certain stockholders of common stock	--	267,026	267,026
Net loss attributable to common stockholders .	$ 3,774,066	$ 272,941	$ 4,047,007
Basic and diluted net loss per share from continuing operations	$ 0.10	$ 0.01	$ 0.11
Basic and diluted net loss per share	$ 0.10	$ 0.01	$ 0.11

</TABLE>

Balance sheet data:

<TABLE>
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	As of December 31, 2003		
	Previously Reported	Adjustment	As Restated
<S>	<C>	<C>	<C>
Other accounts payable and accrued expenses	$ 4,180,411	$ (150,000)	$ 4,030,411
Convertible debenture	881,944	568,250	1,450,194
Total long term liabilities	4,066,579	568,250	4,634,829
Additional paid in capital	135,891,316	(188,903)	135,702,413
Accumulated deficit	(109,681,893)	(229,347)	(109,911,240)
Total shareholders' equity	22,044,127	(418,250)	21,625,877

</TABLE>

Cash flow data:

<TABLE>
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	For the Nine Months ended September 30, 2003		
	Previously Reported	Adjustment	As Restated
<S>	<C>	<C>	<C>
Net loss	$ 3,774,066	$ (5,915)	$ 3,779,981
Stock based compensation related to repricing of warrants granted to investors and the grant of new warrants	152,844	(123,085)	29,759
Amortization of compensation related to beneficial conversion feature and warrants issued to holders of convertible debentures	1,005,001	129,000	1,134,001

</TABLE>

Overview of Results of Operations

We incurred significant operating losses for the years ended December 31, 2001, 2002 and 2003 and for the first nine months of 2004. While we expect to continue to derive revenues from the sale of products that our subsidiaries manufacture and the services that they provide, there can be no assurance that we will be able to achieve or maintain profitability on a consistent basis.

During 2003, we substantially increased our revenues and reduced our operating loss from $18.5 million in 2002 to $9.7 million in 2003. This was achieved through a combination of cost-cutting measures and increased revenues, particularly from the sale of Zinc-Air batteries to the military and from sales of interactive training systems by IES. We believe that our acquisitions of FAAC, Epsilor and AoA will contribute to our goal of achieving profitability.

We regard moving the company to a positive cash flow situation on a consistent basis to be an important goal, and we are focused on achieving that goal for the second half of 2004 and beyond. In this connection, we note that most of our business lines historically have had weaker first halves than second halves, and weaker first quarters than second quarters. This has proved to be the case thus far for 2004 as well.

A portion of our operating loss during the first nine months of 2004 arose as a result of non-cash charges. These charges were primarily related to our acquisitions and to our raising capital. Because we anticipate continuing these

activities, we expect to continue to incur such non-cash charges in the future.

Non-cash charges related to acquisitions arise when the purchase price for an acquired company exceeds the company's book value. In such a circumstance, a portion of the excess of the purchase price is recorded as goodwill and a portion as intangible assets. In the case of goodwill, the assets recorded as goodwill are not amortized; instead, we are required to perform an annual impairment review. If we determine, through the impairment review process, that goodwill has been impaired, we must record the impairment charge in our statement of operations. Intangible assets are amortized in accordance with their useful life. Accordingly, for a period of time following an acquisition, we incur a non-cash charge in the amount of a fraction (based on the useful life of the intangible assets) of the amount recorded as intangible assets. Our acquisitions of FAAC, Epsilor and AoA resulted in our incurring similar non-cash charges during the first nine months of 2004.

As a result of the application of the above accounting rule, we incurred non-cash charges related to our acquisitions in the amount of $2,332,900 during the first nine months of 2004.

The non-cash charges that relate to our financings arise when we sell convertible debentures and warrants. When we issue convertible debentures, we record an expense for a beneficial conversion feature that is amortized ratably over the life of the debenture. When a debenture is converted, however, the entire remaining unamortized beneficial conversion feature expense is immediately recognized in the quarter in which the debenture is converted. Similarly, when we issue warrants in connection with convertible debentures, we record an expense for financial expenses that is amortized ratably over the term of the convertible debentures; when the convertible debentures are converted, the entire remaining unamortized financial expense is immediately recognized in the quarter in which the conversion occurs. As and to the extent that our remaining convertible debentures are converted, we would incur similar non-cash charges going forward.

As a result of the application of the above accounting rule, we incurred non-cash charges related to our financings in the amount of $3,454,676 during the first nine months of 2004.

Additionally, in an effort to improve our cash situation and our shareholders' equity, we have periodically induced holders of certain of our warrants to exercise their warrants by lowering the exercise price of the warrants in exchange for immediate exercise of such warrants, and by issuing to such investors new warrants. Under such circumstances, we record a deemed dividend in an amount determined based upon the fair value of the new warrants (using a Black-Scholes pricing model). As and to the extent that we engage in similar warrant repricings and issuances in the future, we would incur similar non-cash charges.

As a result of the application of the above accounting rule we recorded a deemed dividend related to warrants repricing in amount of $3,328,952 during the first nine months of 2004.

In addition, we incurred non-cash charges in the amount of $576,648 during the first nine months of 2004 in connection with options and shares granted to employees.

Overview of Operating Performance and Backlog

We shut down our money-losing consumer battery operations and began acquiring new businesses in the defense and security field in 2002. Since then, we have concentrated on eliminating our operating deficit and moving Arotech to cash-flow positive operations. In order to do this, we have focused on acquiring businesses with strong revenues and profitable operations.

In the first nine months of 2004, IES experienced a substantial slowdown of new sales. As of September 30, 2004, our backlog for our Simulation, Training and Consulting Division totaled $12.2 million, most of which was attributable to FAAC.

In our Battery and Power Systems Division, EFB and Epsilor had revenues roughly in line with expectations. As of September 30, 2004, our backlog for our Battery and Power Systems Division totaled $3.6 million.

In our Armored Vehicle Division, MDT Armor experienced an increase in revenues during the first nine months of 2004 as a result of new orders in connection with the War in Iraq. As of September 30, 2004, our backlog for our Armored Vehicle Division totaled $7.1 million.

Functional Currency

We consider the United States dollar to be the currency of the primary economic environment in which we and our Israeli subsidiary EFL operate and, therefore, both we and EFL have adopted and are using the United States dollar as our functional currency. Transactions and balances originally denominated in U.S. dollars are presented at the original amounts. Gains and losses arising from non-dollar transactions and balances are included in net income.

The majority of financial transactions of our Israeli subsidiaries MDT and Epsilor, is in New Israel Shekels ("NIS") and a substantial portion of MDT's and Epsilor's costs is incurred in NIS. Management believes that the NIS is the functional currency of MDT and Epsilor. Accordingly, the financial statements of MDT and Epsilor have been translated into U.S. dollars. All balance sheet accounts have been translated using the exchange rates in effect at the balance sheet date. Statement of operations amounts have been translated using the average exchange rate for the period. The resulting translation adjustments are reported as a component of accumulated other comprehensive loss in shareholders' equity.

Critical Accounting Policies

The changes to our critical accounting policies as a result of our purchases of Epsilor, FAAC and AoA include the following:

- Revenue Recognition
- Accounting for Income Taxes

Revenue Recognition

Significant management judgments and estimates must be made and used in connection with the recognition of revenue in any accounting period. Material differences in the amount of revenue in any given period may result if these judgments or estimates prove to be incorrect or if management's estimates change on the basis of development of the business or market conditions. Management judgments and estimates have been applied consistently and have been reliable historically.

A portion of our revenue is generated by our subsidiary FAAC from arrangements involving significant customization of simulation system. Revenues from such arrangements are recognized based on the percentage of completion method. The percentage of completion is measured by monitoring progress using records of actual time incurred to date in the project compared with the total estimated project requirement, which corresponds to the costs related to earned revenues. Estimates of total project requirements are based on prior experience of customization, delivery and acceptance of the same or similar technology and are reviewed and updated regularly by management. We believe that the use of the percentage of completion method is appropriate as we have the ability to make reasonably dependable estimates of the extent of progress towards completion, contract revenues and contract costs. In addition, contracts executed include provisions that clearly specify the enforceable rights regarding services to be provided and received by the parties to the contracts, the consideration to be exchanged and the manner and terms of settlement. In all cases we expect to perform our contractual obligations and our licensees are expected to satisfy their obligations under the contract. The complexity of the estimation process and the issues related to the assumptions, risks and uncertainties inherent with the application of the percentage of completion method of accounting affect the amounts of revenue and related expenses reported in our consolidated financial statements. A number of internal and external factors can affect our estimates, including labor rates, utilization and specification and testing requirement changes.

Accounting for Income Taxes

Significant judgment is required in determining our worldwide income tax expense provision. In the ordinary course of a global business, there are many transactions and calculations where the ultimate tax outcome is uncertain. Some of these uncertainties arise as a consequence of cost reimbursement arrangements among related entities, the process of identifying items of revenue and expense that qualify for preferential tax treatment and segregation of foreign and domestic income and expense to avoid double taxation. Although we believe that our estimates are reasonable, the final tax outcome of these matters may be different from that which is reflected in our historical income tax provisions and accruals. Such differences could have a material effect on our income tax provision and net income (loss) in the period in which such determination is made.

Results of Operations

Preliminary Note

Results for the three and nine months ended September 30, 2004 include the results of FAAC, Epsilor and AoA for such period as a result of our acquisitions of these companies during 2004. The results of FAAC, Epsilor and AoA were not included in our operating results for the three and nine months ended September 30, 2003. Accordingly, the following period-to-period comparisons should not necessarily be relied upon as indications of future performance.

Three months ended September 30, 2004 compared to the three months ended September 30, 2003.

Revenues. During the three months ended September 30, 2004, we (through our subsidiaries) recognized revenues as follows:

> IES and FAAC recognized revenues from the sale of interactive use-of-force training systems and from the provision of maintenance services in connection with such systems;

> MDT, MDT Armor and AoA recognized revenues from payments under vehicle armoring contracts, for service and repair of armored vehicles, and on sale of armoring products;

> EFB and Epsilor recognized revenues from the sale of batteries, chargers and adapters to the military, and under certain development contracts with the U.S. Army; and

> EFL recognized revenues from the sale of lifejacket lights and from subcontracting fees received in connection with Phase IV of the United States Department of Transportation (DOT) electric bus program.

Revenues for the three months ended September 30, 2004 totaled $16.3 million, compared to $5.7 million in the comparable period in 2003, an increase of $10.6 million, or 185%. This increase was primarily attributable to the following factors:

> Increased revenues from our Armored Vehicle Division, particularly MDT Armor; and

> Revenues generated by FAAC ($4.6 million), Epsilor ($1.9 million) and AoA ($1.3 million) in the third quarter of 2004 that were not present in the corresponding period of 2003.

These revenues were offset to some extent by

> Decreased U.S. Army Communications Electronics Command (CECOM) revenues from our EFB subsidiary.

In the third quarter of 2004, revenues were $6.0 million for the Simulation, Training and Consulting Division (compared to $2.9 million in the third quarter of 2003, an increase of $3.1 million, or 107%, due primarily to the added revenues of FAAC); $2.9 million for the Battery and Power Systems Division (compared to $1.8 million in the third quarter of 2003, an increase of $1.1 million, or 58%, due primarily to the added revenues of Epsilor, offset to some extent by decreased revenues from EFB); and $7.3 million for the Armored Vehicle Division (compared to $943,000 in the third quarter of 2003, an increase of $6.4 million, or 677%, due primarily to increased revenues from MDT Armor and to the added revenues of AoA).

Cost of revenues and gross profit. Cost of revenues totaled $11.5 million during the third quarter of 2004, compared to $3.3 million in the third quarter of 2003, an increase of $8.3 million, or 255%, due primarily to increased sales in all divisions.

Direct expenses for our three divisions during the third quarter of 2004 were $5.0 million for the Simulation, Training and Consulting Division (compared to $2.1 million in the third quarter of 2003, an increase of $2.9 million, or 140%, due primarily the added expenses of FAAC); $2.4 million for the Battery and Power Systems Division (compared to $1.6 million in the third quarter of 2003, an increase of $818,000, or 52%, due primarily to the added revenues of Epsilor ($1.9 million), offset by decreased revenues of our Zinc-Air military batteries); and $6.2 million for the Armored Vehicle Division (compared to $780,000 in the third quarter of 2003, an increase of $5.5 million, or 701%, due primarily to increased revenues from MDT Armor and to the added revenues of AoA).

Gross profit was $4.7 million during the third quarter of 2004, compared to $2.5 million during the third quarter of 2003, an increase of $2.3 million, or 93%. This increase was the direct result of all factors presented above, most notably the presence of FAAC, Epsilor and AoA in our results and the increase in vehicle armoring revenues.

Research and development expenses. Research and development expenses for the third quarter of 2004 were $431,000, compared to $252,000 during the third quarter of 2003, an increase of $179,000, or 71%. This increase was primarily the result of the inclusion of the research and development expenses of FAAC and Epsilor in our results this quarter.

Sales and marketing expenses. Sales and marketing expenses for the third quarter of 2004 were $1.3 million, compared to $758,000 the third quarter of 2003, an increase of $537,000, or 71%. This increase was primarily attributable to the inclusion of the sales and marketing expenses of FAAC, Epsilor and AoA in our results for 2004.

General and administrative expenses. General and administrative expenses for the third quarter of 2004 were $2.1 million compared to $1.0 million in the third quarter of 2003, an increase of $1.1 million, or 115%. This increase was primarily attributable to the following factors:

> The inclusion of the general and administrative expenses of FAAC, Epsilor and AoA in our results for 2004;

> Expenses in 2004 in connection with grants of options and shares to employees that did not exist in 2003;

> Increases in other general and administrative expenses in comparison to 2003, such as employees salaries, travel expenses and audit fees.

Financial income (expenses), net. Financial income , net of financial expenses and exchange differentials, totaled approximately $1.1 million in the third quarter of 2004 compared to $(82,000) in the third quarter of 2003. The difference was due primarily to amortization of debt discount related to the issuance of convertible debentures, as well as interest expenses related to those debentures. Those expenses were offset by $1.8 million financial income due to the change in the fair market value of the warrants that were issued in July 2004 (see Note 11.b. to the financial statements) .

Income taxes. We and certain of our subsidiaries incurred accumulated net operating losses during previous years and, accordingly, we were not required to make any provision for income taxes. With respect to some of our subsidiaries that operated at a net profit during 2004, we were able to offset federal taxes against our accumulated loss carry forward. We recorded a total of $116,000 in tax expenses in the third quarter of 2004, with respect to certain of our subsidiaries that operated at a net profit during 2004 and we are not able to offset their taxes against our loss carry forward. In the third quarter of 2003, tax expenses written were with respect to MDT's taxable income.

Amortization of intangible assets. Amortization of intangible assets totaled $739,000 in the third quarter of 2004, compared to $104,000 the third quarter of 2003, an increase of

$636,000, or 614%. Of this increase, $226,000 of this amortization was attributable to FAAC, $142,000 was attributable to Epsilor, and $213,000 was attributable to AoA.

Net income before deemed dividend of common stock to certain stockholders. Due to the factors cited above, we reported a net income of $1.1 million in the third quarter of 2004, compared to a net income of $216,000 in the third quarter of 2003, an increase in income of $911,000.

Net income (loss) after deemed dividend of common stock to certain stockholders was a net loss of $(1.0) million in the third quarter of 2004 due to a deemed dividend of $2.2 million in the third quarter of 2004 (see Note 11.b. to the financial statements) compared to a net income of $122,000 in the third quarter of 2003 due to a deemed dividend of $95,000 in the third quarter of 2003.

Nine months ended September 30, 2004 compared to the nine months ended September 30, 2003.

Revenues. During the nine months ended September 30, 2004, we (through our subsidiaries) recognized revenues as follows:

> IES and FAAC recognized revenues from the sale of interactive use-of-force training systems and from the provision of warranty services in connection with such systems;

> MDT, MDT Armor and AoA recognized revenues from payments under vehicle armoring contracts, for service and repair of armored vehicles, and on sale of armoring products;

> EFB and Epsilor recognized revenues from the sale of batteries, chargers and adapters to the military, and under certain development contracts with the U.S. Army;

> Arocon recognized revenues under consulting agreements; and

> EFL recognized revenues from the sale of lifejacket lights and from subcontracting fees received in connection with Phase IV of the United States Department of Transportation (DOT) electric bus program.

Revenues for the nine months ended September 30, 2004 totaled $33.4 million, compared to $13.2 million in the comparable period in 2003, an increase of $20.2 million, or 152%. This increase was primarily attributable to the

following factors:

> Increased revenues from our Armored Vehicle Division, particularly MDT Armor;

> Increased revenues from our Battery and Power Systems Division, particularly CECOM revenues from EFB; and

> Revenues generated by FAAC ($9.4 million), Epsilor ($3.9 million) and AoA ($1.3 million) in the first nine months of 2004 that were not present in the corresponding period of 2003.

These revenues were offset to some extent by

> Decreased revenues from our IES subsidiary.

In the first nine months of 2004, revenues were $13.3 million for the Simulation, Training and Consulting Division (compared to $5.8 million in the first nine months of 2003, an increase of $7.5 million, or 130%, due primarily to the added revenues of FAAC, offset to some extent by decreased revenues from IES); $8.0 million for the Battery and Power Systems Division (compared to $4.7 million in the first nine months of 2003, an increase of $3.3 million, or 71%, due primarily to the added revenues of Epsilor ($3.9 million), offset to some extent by decreased revenues from our Zinc-Air military batteries); and $12.1 million for the Armored Vehicle Division (compared to $2.8 million in the first nine months of 2003, an increase of $9.3 million, or 335%, due primarily to increased revenues from MDT Armor and to the added revenues of AoA).

Cost of revenues and gross profit. Cost of revenues totaled $22.7 million during the first nine months of 2004, compared to $8.4 million in the first nine months of 2003, an increase of $14.3 million, or 171%, due primarily to increased sales in all divisions.

Direct expenses for our three divisions during the first nine months of 2004 were $11.9 million for the Simulation, Training and Consulting Division (compared to $5.1 million in the first nine months of 2003, an increase of $6.8 million, or 132%, due primarily to the added expenses of FAAC, offset to some extent by decreased expenses by IES); $7.5 million for the Battery and Power Systems Division (compared to $4.3 million in the first nine months of 2003, an increase of $3.1 million, or 72%, due primarily to the added expenses of Epsilor; and $10.7 million for the Armored Vehicle Division (compared to $2.8 million in the first nine months of 2003, an increase of $7.8 million, or 276%, due primarily to increased revenues from MDT Armor and to the added expenses of AoA ($759,000).

Gross profit was $10.7 million during the first nine months of 2004, compared to $4.9 million during the first nine months of 2003, an increase of $5.8 million, or 120%. This increase was the direct result of all factors presented above, most notably the presence of FAAC, Epsilor and AoA in our results and the increase in vehicle armoring revenues from MDT Armor.

Research and development expenses. Research and development expenses for the first nine months of 2004 were $1.3 million, compared to $763,000 during the first nine months of 2003, an increase of $540,000, or 71%. This increase was the result of the inclusion of the research and development expenses of FAAC and Epsilor in our results this nine months.

Sales and marketing expenses. Sales and marketing expenses for the first nine months of 2004 were $3.4 million, compared to $2.4 million the first nine months of 2003, an increase of $1.0 million, or 43%. This increase was primarily attributable to the inclusion of the sales and marketing expenses of FAAC, Epsilor and AoA in our results for 2004.

Those expenses were offset to some extent by a decrease in expenses related to our security consulting business in the U.S., a decrease in expenses related to our military batteries field and a decrease in IES sales and marketing expenses.

General and administrative expenses. General and administrative expenses for the first nine months of 2004 were $7.6 million compared to $3.5 million in the first nine months of 2003, an increase of $4.1 million, or 119%. This increase was primarily attributable to the following factors:

> The inclusion of the general and administrative expenses of FAAC, Epsilor and AoA in our results for 2004;

> Expenses in 2004 in connection with grant of options and shares to employees that were not present in 2003; and

> Increases in other general and administrative expenses in comparison to 2003, such as employee accruals, travel expenses, audit fees and expenses related to due diligence performed in connection to certain

potential acquisitions; and

> We incurred expenses in connection with new activities by our Arocon and MDT Armor subsidiaries.

Financial expenses, net. Financial expenses, net of interest income and exchange differentials, totaled approximately $2.1 million in the first nine months of 2004 compared to $1.2 million in the first nine months of 2003, a difference of $912,000 or 75%. This difference was due primarily to amortization of debt discount related to the issuance of convertible debentures, as well as interest expenses related to those debentures.

Income taxes. We and certain of our subsidiaries incurred net operating losses during 2004 and, accordingly, we were not required to make any provision for income taxes. With respect to some of our subsidiaries that operated at a net profit during 2004, we were able to offset federal taxes against our losses carry forward. We recorded a total of $287,000 in tax expenses in the first nine months of 2004, with respect to certain of our subsidiaries that operated at a net profit during 2004 and we are not able to offset their taxes against our loss carry forward and with respect to state taxes. In the first nine months of 2003, tax expenses were written with respect to MDT's taxable income.

Amortization of intangible assets. Amortization of intangible assets totaled $1.7 million in the first nine months of 2004, compared to $727,000 in the first nine months of 2003, an increase of $1.0 million, or 138%. Of this increase, $678,000 of this amortization was attributable to FAAC, $426,000 was attributable to Epsilor and $213,000 was attributable to AoA. The expenses were offset to some extent by a decrease in IES's and MDT's amortization expenses in 2004.

Net loss before deemed dividend of common stock to certain stockholders. Due to the factors cited above, we reported a net loss of $5.8 million in the first nine months of 2004, compared to a net loss of $3.8 million the first nine months of 2003, an increase of $2.0 million.

Net loss after deemed dividend of common stock to certain stockholders was $9.1 million due to a deemed dividend of $3.3 million (see Notes 10.a. and 11.b. to the financial statements) compared to $4.0 million in the first nine months of 2003 due to a deemed dividend of $267,000 in the first nine months of 2003.

Liquidity and Capital Resources

As of September 30, 2004, we had $4.6 million in cash, $13.2 million in restricted collateral securities and cash deposits due within one year, $1.0 million in long-term restricted securities and deposits, and $129,000 in marketable securities, as compared to at December 31, 2003, when we had $13.7 million in cash and $706,000 in restricted cash deposits due within one year. The decrease in cash was primarily the result of the costs of the acquisitions of FAAC, Epsilor and AoA, and working capital needed in our other segments.

We used available funds in the third quarter of 2004 primarily for acquisitions, sales and marketing, continued research and development expenditures, and other working capital needs. We increased our investment in fixed assets during the nine months ended September 30, 2004 by $1.1 million over the investment as at December 31, 2003, primarily in the Battery and Power Systems Division and in the Simulation, Training and Consulting Division. Our net fixed assets amounted to $4.5 million at quarter end.

Net cash used in operating activities from continuing operations for the nine months ended September 30, 2004 and 2003 was $1.0 million and $2.4 million, respectively, a decrease of $1.4 million. This decrease was primarily the result of an increase in our adjusted profits in 2004 (profit in statement of operations less non-cash charges such as depreciation, amortization, non-cash financial expenses and non-cash expenses related to options and warrants).

Net cash used in investing activities for the nine months ended September 30, 2004 and 2003 was $52.2 million and $936,000, an increase of $51.3 million. This increase was primarily the result of our investment in the acquisition of FAAC, Epsilor and AoA in 2004.

Net cash provided by financing activities for the nine months ended September 30, 2004 and 2003 was $44.3 million and $4.9 million, respectively, an increase of $39.4 million. This increase was primarily the result of higher amounts of funds raised through sales of our securities in 2004 compared to 2003.

During the nine months ended September 30, 2004, certain of our employees exercised options under our registered employee stock option plan. The proceeds to us from the exercised options were approximately $1.1 million.

As of September 30, 2004, we had (based on the contractual amount of the debt and not on the accounting valuation of the debt) approximately $7.5 million in long term bank and certificated debt outstanding, of which $5.3 million was convertible debt, and approximately $1.25 million in short-term debt.

Our current debt agreements grant to our investors a right of first refusal on any future financings, except for underwritten public offerings in

excess of $30 million, and contain certain other affirmative and negative covenants. We do not believe that these covenants will materially limit our ability to undertake future financings.

Based on our internal forecasts, we believe that our present cash position and anticipated cash flows from operations should be sufficient to satisfy our current estimated cash requirements through the next year. This belief is based on certain assumptions that our management believes to be reasonable, some of which are subject to the risk factors detailed below. Over the long term, we will need to become profitable, at least on a cash-flow basis, and maintain that profitability in order to avoid future capital requirements. Additionally, we would need to raise additional capital in order to fund any future acquisitions.

RISK FACTORS

The following factors, among others, could cause actual results to differ materially from those contained in forward-looking statements made in this Report and presented elsewhere by management from time to time.

Business-Related Risks

We have had a history of losses and may incur future losses.

We were incorporated in 1990 and began our operations in 1991. We have funded our operations principally from funds raised in each of the initial public offering of our common stock in February 1994; through subsequent public and private offerings of our common stock and equity and debt securities convertible or exercisable into shares of our common stock; research contracts and supply contracts; funds received under research and development grants from the Government of Israel; and sales of products that we and our subsidiaries manufacture. We have incurred significant operating losses since our inception. Additionally, as of September 30, 2004, we had an accumulated deficit of approximately $115.8 million. There can be no assurance that we will ever be able to maintain profitability consistently or that our business will continue to exist.

Our existing indebtedness may adversely affect our ability to obtain additional funds and may increase our vulnerability to economic or business downturns.

Our bank and certificated indebtedness aggregated approximately $7.5 million as of September 30, 2004. Accordingly, we are subject to the risks associated with indebtedness, including:

- we must dedicate a portion of our cash flows from operations to pay debt service costs and, as a result, we have less funds available for operations, future acquisitions of consumer receivable portfolios, and other purposes;

- it may be more difficult and expensive to obtain additional funds through financings, if available at all;

- we are more vulnerable to economic downturns and fluctuations in interest rates, less able to withstand competitive pressures and less flexible in reacting to changes in our industry and general economic conditions; and

- if we default under any of our existing debt instruments or if our creditors demand payment of a portion or all of our indebtedness, we may not have sufficient funds to make such payments.

The occurrence of any of these events could materially adversely affect our results of operations and financial condition and adversely affect our stock price.

The agreements governing the terms of our debentures contain numerous affirmative and negative covenants that limit the discretion of our management with respect to certain business matters and place restrictions on us, including obligations on our part to preserve and maintain our assets and restrictions on our ability to incur or guarantee debt, to merge with or sell our assets to another company, and to make significant capital expenditures without the consent of the debenture holders. Our ability to comply with these and other provisions of such agreements may be affected by changes in economic or business conditions or other events beyond our control.

Failure to comply with the terms of our debentures could result in a default that could have material adverse consequences for us.

A failure to comply with the obligations contained in our debenture agreements could result in an event of default under such agreements which could result in an acceleration of the debentures and the acceleration of debt under other instruments evidencing indebtedness that may contain cross-acceleration or

cross-default provisions. If the indebtedness under the debentures or other indebtedness were to be accelerated, there can be no assurance that our assets would be sufficient to repay in full such indebtedness.

We have pledged a substantial portion of our assets to secure our borrowings.

Our debentures are secured by a substantial portion of our assets. If we default under the indebtedness secured by our assets, those assets would be available to the secured creditors to satisfy our obligations to the secured creditors, which could materially adversely affect our results of operations and financial condition and adversely affect our stock price.

We need significant amounts of capital to operate and grow our business.

We require substantial funds to market our products and develop and market new products. To the extent that we are unable to fully fund our operations through profitable sales of our products and services, we may continue to seek additional funding, including through the issuance of equity or debt securities. However, there can be no assurance that we will obtain any such additional financing in a timely manner or on acceptable terms. If additional funds are raised by issuing equity securities, stockholders may incur further dilution. If additional funding is not secured, we will have to modify, reduce, defer or eliminate parts of our anticipated future commitments and/or programs.

We may not be successful in operating a new business.

Prior to the acquisitions of IES and MDT in 2002 and the acquisitions of FAAC and Epsilor in January 2004 and AoA in August 2004, our primary business was the marketing and sale of products based on primary and refuelable Zinc-Air fuel cell technology and advancements in battery technology for defense and security products and other military applications, electric vehicles and consumer electronics. As a result of our acquisitions, a substantial component of our business is the marketing and sale of hi-tech multimedia and interactive training solutions and sophisticated lightweight materials and advanced engineering processes used to armor vehicles. These are new businesses for us and our management group has limited experience operating these types of businesses. Although we have retained our acquired companies' management personnel, we cannot assure that such personnel will continue to work for us or that we will be successful in managing this new business. If we are unable to successfully operate these new businesses, our business, financial condition and results of operations could be materially impaired.

Our acquisition strategy involves various risks.

Part of our strategy is to grow through the acquisition of companies that will complement our existing operations or provide us with an entry into markets we do not currently serve. Growth through acquisitions involves substantial risks, including the risk of improper valuation of the acquired business and the risk of inadequate integration. There can be no assurance that suitable acquisition candidates will be available, that we will be able to acquire or manage profitably such additional companies or that future acquisitions will produce returns that justify our investments therein. In addition, we may compete for acquisition and expansion opportunities with companies that have significantly greater resources than we do. Furthermore, acquisitions could disrupt our ongoing business, distract the attention of our senior managers, make it difficult to maintain our operational standards, controls and procedures and subject us to contingent and latent risks that are different, in nature and magnitude, than the risks we currently face.

We may finance future acquisitions with cash from operations or additional debt or equity financings. There can be no assurance that we will be able to generate internal cash or obtain financing from external sources or that, if available, such financing will be on terms acceptable to us. The issuance of additional common stock to finance acquisitions may result in substantial dilution to our stockholders. Any debt financing may significantly increase our leverage and may involve restrictive covenants which limit our operations.

We may not successfully integrate our new acquisitions.

In light of our recent acquisitions of IES, MDT, FAAC, Epsilor and AoA, our success will depend in part on our ability to manage the combined operations of these companies and to integrate the operations and personnel of these companies along with our other subsidiaries and divisions into a single organizational structure. There can be no assurance that we will be able to effectively integrate the operations of our subsidiaries and divisions and our newly-acquired businesses into a single organizational structure. Integration of these operations could also place additional pressures on our management as well as on our key technical resources. The failure to successfully manage this integration could have an adverse material effect on us.

If we are successful in acquiring additional businesses, we may experience a period of rapid growth that could place significant additional demands on, and require us to expand, our management, resources and management information systems. Our failure to manage any such rapid growth effectively could have a material adverse effect on our financial condition, results of operations and cash flows.

If we are unable to manage our growth, our operating results will be impaired.

As a result of our acquisitions, we are currently experiencing a period of significant growth and development activity which could place a significant strain on our personnel and resources. Our activity has resulted in increased levels of responsibility for both existing and new management personnel. Many of our management personnel have had limited or no experience in managing growing companies. We have sought to manage our current and anticipated growth through the recruitment of additional management and technical personnel and the implementation of internal systems and controls. However, our failure to manage growth effectively could adversely affect our results of operations.

A significant portion of our business is dependent on government contracts.

Many of the customers of IES, FAAC and AoA to date have been in the public sector of the U.S., including the federal, state and local governments, and in the public sectors of a number of other countries, and most of MDT's customers have been in the public sector in Israel, in particular the Ministry of Defense. Additionally, all of EFB's sales to date of battery products for the military and defense sectors have been in the public sector in the United States. A significant decrease in the overall level or allocation of defense spending or law enforcement in the U.S. or other countries could have a material adverse effect on our future results of operations and financial condition. MDT has already experienced a slowdown in orders from the Ministry of Defense due to budget constraints and a requirement of U.S. aid to Israel that a substantial proportion of such aid be spent in the U.S., where MDT has only recently opened a factory in operation.

Sales to public sector customers are subject to a multiplicity of detailed regulatory requirements and public policies as well as to changes in training and purchasing priorities. Contracts with public sector customers may be conditioned upon the continuing availability of public funds, which in turn depends upon lengthy and complex budgetary procedures, and may be subject to certain pricing constraints. Moreover, U.S. government contracts and those of many international government customers may generally be terminated for a variety of factors when it is in the best interests of the government and contractors may be suspended or debarred for misconduct at the discretion of the government. There can be no assurance that these factors or others unique to government contracts or the loss or suspension of necessary regulatory licenses will not have a material adverse effect on our future results of operations and financial condition.

Our U.S. government contracts may be terminated at any time and may contain other unfavorable provisions.

The U.S. government typically can terminate or modify any of its contracts with us either for its convenience or if we default by failing to perform under the terms of the applicable contract. A termination arising out of our default could expose us to liability and have a material adverse effect on our ability to re-compete for future contracts and orders. Our U.S. government contracts contain provisions that allow the U.S. government to unilaterally suspend us from receiving new contracts pending resolution of alleged violations of procurement laws or regulations, reduce the value of existing contracts, issue modifications to a contract and control and potentially prohibit the export of our products, services and associated materials.

A negative audit by the U.S. government could adversely affect our business, and we might not be reimbursed by the government for costs that we have expended on our contracts.

Government agencies routinely audit government contracts. These agencies review a contractor's performance on its contract, pricing practices, cost structure and compliance with applicable laws, regulations and standards. If we are audited, we will not be reimbursed for any costs found to be improperly allocated to a specific contract, while we would be required to refund any improper costs for which we had already been reimbursed. Therefore, an audit could result in a substantial adjustment to our revenues. If a government audit uncovers improper or illegal activities, we may be subject to civil and criminal penalties and administrative sanctions, including termination of contracts, forfeitures of profits, suspension of payments, fines and suspension or debarment from doing business with United States government agencies. We could suffer serious reputational harm if allegations of impropriety were made against us. A governmental determination of impropriety or illegality, or an allegation of impropriety, could have a material adverse effect on our business, financial condition or results of operations.

We may be liable for penalties under a variety of procurement rules and regulations, and changes in government regulations could adversely impact our revenues, operating expenses and profitability.

Our defense and commercial businesses must comply with and are affected by various government regulations that impact our operating costs, profit margins and our internal organization and operation of our businesses. Among the most significant regulations are the following:

- the U.S. Federal Acquisition Regulations, which regulate the formation, administration and performance of government contracts;

- the U.S. Truth in Negotiations Act, which requires certification and disclosure of all cost and pricing data in connection with contract negotiations; and

- the U.S. Cost Accounting Standards, which impose accounting requirements that govern our right to reimbursement under certain cost-based government contracts.

These regulations affect how we and our customers do business and, in some instances, impose added costs on our businesses. Any changes in applicable laws could adversely affect the financial performance of the business affected by the changed regulations. With respect to U.S. government contracts, any failure to comply with applicable laws could result in contract termination, price or fee reductions or suspension or debarment from contracting with the U.S. government.

Our operating margins may decline under our fixed-price contracts if we fail to estimate accurately the time and resources necessary to satisfy our obligations.

Some of our contracts are fixed-price contracts under which we bear the risk of any cost overruns. Our profits are adversely affected if our costs under these contracts exceed the assumptions that we used in bidding for the contract. Often, we are required to fix the price for a contract before we finalize the project specifications, which increases the risk that we will mis-price these contracts. The complexity of many of our engagements makes accurately estimating our time and resources more difficult.

If we are unable to retain our contracts with the U.S. government and subcontracts under U.S. government prime contracts in the competitive rebidding process, our revenues may suffer.

Upon expiration of a U.S. government contract or subcontract under a U.S. government prime contract, if the government customer requires further services of the type provided in the contract, there is frequently a competitive rebidding process. We cannot guarantee that we, or if we are a subcontractor that the prime contractor, will win any particular bid, or that we will be able to replace business lost upon expiration or completion of a contract. Further, all U.S. government contracts are subject to protest by competitors. The termination of several of our significant contracts or nonrenewal of several of our significant contracts could result in significant revenue shortfalls.

Some of the components of our products pose potential safety risks which could create potential liability exposure for us.

Some of the components of our products contain elements that are known to pose potential safety risks. In addition to these risks, and there can be no assurance that accidents in our facilities will not occur. Any accident, whether occasioned by the use of all or any part of our products or technology or by our manufacturing operations, could adversely affect commercial acceptance of our products and could result in significant production delays or claims for damages resulting from injuries. Any of these occurrences would materially adversely affect our operations and financial condition.

We may face product liability claims.

In the event that our products, including the products manufactured by MDT and AoA, fail to perform as specified, users of these products may assert claims for substantial amounts. These claims could have a materially adverse effect on our financial condition and results of operations. There is no assurance that the amount of the general product liability insurance that we maintain will be sufficient to cover potential claims or that the present amount of insurance can be maintained at the present level of cost, or at all.

Our fields of business are highly competitive.

The competition to develop defense and security products and electric vehicle battery systems, and to obtain funding for the development of these products, is, and is expected to remain, intense.

Our defense and security products compete with other manufacturers of specialized training systems, including Firearms Training Systems, Inc., a producer of interactive simulation systems designed to provide training in the handling and use of small and supporting arms. In addition, we compete with manufacturers and developers of armor for cars and vans, including O'Gara-Hess & Eisenhardt, a division of Armor Holdings, Inc.

Our battery technology competes with other battery technologies, as well as other Zinc-Air technologies. The competition in this area of our business

consists of development stage companies, major international companies and consortia of such companies, including battery manufacturers, automobile manufacturers, energy production and transportation companies, consumer goods companies and defense contractors. Many of our competitors have financial, technical, marketing, sales, manufacturing, distribution and other resources significantly greater than ours.

Various battery technologies are being considered for use in electric vehicles and defense and safety products by other manufacturers and developers, including the following: lead-acid, nickel-cadmium, nickel-iron, nickel-zinc, nickel-metal hydride, sodium-sulfur, sodium-nickel chloride, zinc-bromine, lithium-ion, lithium-polymer, lithium-iron sulfide, primary lithium, rechargeable alkaline and Zinc-Air.

If we are unable to compete successfully in each of our operating areas, especially in the defense and security products area of our business, our business and results of operations could be materially adversely affected.

Our business is dependent on proprietary rights that may be difficult to protect and could affect our ability to compete effectively.

Our ability to compete effectively will depend on our ability to maintain the proprietary nature of our technology and manufacturing processes through a combination of patent and trade secret protection, non-disclosure agreements and licensing arrangements.

Litigation, or participation in administrative proceedings, may be necessary to protect our proprietary rights. This type of litigation can be costly and time consuming and could divert company resources and management attention to defend our rights, and this could harm us even if we were to be successful in the litigation. In the absence of patent protection, and despite our reliance upon our proprietary confidential information, our competitors may be able to use innovations similar to those used by us to design and manufacture products directly competitive with our products. In addition, no assurance can be given that others will not obtain patents that we will need to license or design around. To the extent any of our products are covered by third-party patents, we could need to acquire a license under such patents to develop and market our products.

Despite our efforts to safeguard and maintain our proprietary rights, we may not be successful in doing so. In addition, competition is intense, and there can be no assurance that our competitors will not independently develop or patent technologies that are substantially equivalent or superior to our technology. Moreover, in the event of patent litigation, we cannot assure you that a court would determine that we were the first creator of inventions covered by our issued patents or pending patent applications or that we were the first to file patent applications for those inventions. If existing or future third-party patents containing broad claims were upheld by the courts or if we were found to infringe third party patents, we may not be able to obtain the required licenses from the holders of such patents on acceptable terms, if at all. Failure to obtain these licenses could cause delays in the introduction of our products or necessitate costly attempts to design around such patents, or could foreclose the development, manufacture or sale of our products. We could also incur substantial costs in defending ourselves in patent infringement suits brought by others and in prosecuting patent infringement suits against infringers.

We also rely on trade secrets and proprietary know-how that we seek to protect, in part, through non-disclosure and confidentiality agreements with our customers, employees, consultants, and entities with which we maintain strategic relationships. We cannot assure you that these agreements will not be breached, that we would have adequate remedies for any breach or that our trade secrets will not otherwise become known or be independently developed by competitors.

We are dependent on key personnel and our business would suffer if we fail to retain them.

We are highly dependent on the presidents of our IES, FAAC and AoA subsidiaries and the general managers of our MDT and Epsilor subsidiaries, and the loss of the services of one or more of these persons could adversely affect us. We are especially dependent on the services of our Chairman, President and Chief Executive Officer, Robert S. Ehrlich. The loss of Mr. Ehrlich could have a material adverse effect on us. We are party to an employment agreement with Mr. Ehrlich, which agreement expires at the end of 2005. We do not have key-man life insurance on Mr. Ehrlich.

There are risks involved with the international nature of our business.

A significant portion of our sales are made to customers located outside the U.S., primarily in Europe and Asia. In 2003, 2002 and 2001, without taking account of revenues derived from discontinued operations, 42%, 56% and 49%, respectively, of our revenues, were derived from sales to customers located

outside the U.S. We expect that our international customers will continue to account for a substantial portion of our revenues in the near future. Sales to international customers may be subject to political and economic risks, including political instability, currency controls, exchange rate fluctuations, foreign taxes, longer payment cycles and changes in import/export regulations and tariff rates. In addition, various forms of protectionist trade legislation have been and in the future may be proposed in the U.S. and certain other countries. Any resulting changes in current tariff structures or other trade and monetary policies could adversely affect our sales to international customers.

Investors should not purchase our common stock with the expectation of receiving cash dividends.

We currently intend to retain any future earnings for funding growth and, as a result, do not expect to pay any cash dividends in the foreseeable future.

Market-Related Risks

The price of our common stock is volatile.

The market price of our common stock has been volatile in the past and may change rapidly in the future. The following factors, among others, may cause significant volatility in our stock price:

- Announcements by us, our competitors or our customers;
- The introduction of new or enhanced products and services by us or our competitors;

- Changes in the perceived ability to commercialize our technology compared to that of our competitors;
- Rumors relating to our competitors or us;
- Actual or anticipated fluctuations in our operating results; and
- General market or economic conditions.

If our shares were to be delisted, our stock price might decline further and we might be unable to raise additional capital.

One of the continued listing standards for our stock on the Nasdaq National Market is the maintenance of a $1.00 bid price. Our stock price has periodically traded below $1.00 in the recent past. If our bid price were to go and remain below $1.00 for 30 consecutive business days, Nasdaq could notify us of our failure to meet the continued listing standards, after which we would have 180 calendar days to correct such failure or be delisted from the Nasdaq National Market.

Although we would have the opportunity to appeal any potential delisting, there can be no assurances that this appeal would be resolved favorably. As a result, there can be no assurance that our common stock will remain listed on the Nasdaq National Market. If our common stock were to be delisted from the Nasdaq National Market, we might apply to be listed on the Nasdaq SmallCap market; however, there can be no assurance that we would be approved for listing on the Nasdaq SmallCap market, which has the same $1.00 minimum bid and other similar requirements as the Nasdaq National Market. If we were to move to the Nasdaq SmallCap market, current Nasdaq regulations would give us the opportunity to obtain an additional 180-day grace period and an additional 90-day grace period after that if we meet certain net income, stockholders' equity or market capitalization criteria. While our stock would continue to trade on the over-the-counter bulletin board following any delisting from the Nasdaq, any such delisting of our common stock could have an adverse effect on the market price of, and the efficiency of the trading market for, our common stock. Also, if in the future we were to determine that we need to seek additional equity capital, it could have an adverse effect on our ability to raise capital in the public equity markets.

In addition, if we fail to maintain Nasdaq listing for our securities, and no other exclusion from the definition of a "penny stock" under the Securities Exchange Act of 1934, as amended, is available, then any broker engaging in a transaction in our securities would be required to provide any customer with a risk disclosure document, disclosure of market quotations, if any, disclosure of the compensation of the broker-dealer and its salesperson in the transaction and monthly account statements showing the market values of our securities held in the customer's account. The bid and offer quotation and compensation information must be provided prior to effecting the transaction and must be contained on the customer's confirmation. If brokers become subject to the "penny stock" rules when engaging in transactions in our securities, they would become less willing to engage in transactions, thereby making it more difficult for our stockholders to dispose of their shares.

A substantial number of our shares are available for sale in the public market and sales of those shares could adversely affect our stock price.

Sales of a substantial number of shares of common stock into the public market, or the perception that those sales could occur, could adversely affect our stock price or could impair our ability to obtain capital through an offering of equity securities. As of November 10, 2004, we had 79,096,283 shares of common stock issued and outstanding. Of these shares, most are freely transferable without restriction under the Securities Act of 1933, and a substantial portion of the remaining shares may be sold subject to the volume restrictions, manner-of-sale provisions and other conditions of Rule 144 under the Securities Act of 1933.

Exercise of our warrants, options and convertible debt could adversely affect our stock price and will be dilutive.

As of November 10, 2004, there were outstanding warrants to purchase a total of 17,251,020 shares of our common stock at a weighted average exercise price of $1.55 per share, options to purchase a total of 8,994,130 shares of our common stock at a weighted average exercise price of $1.32 per share, of which 5,905,336 were vested, at a weighted average exercise price of $1.46 per share, and outstanding debentures convertible into a total of 3,786,732 shares of our common stock at a weighted average conversion price of $1.39 per share. Holders of our options, warrants and convertible debt will probably exercise or convert them only at a time when the price of our common stock is higher than their respective exercise or conversion prices. Accordingly, we may be required to issue shares of our common stock at a price substantially lower than the market price of our stock. This could adversely affect our stock price. In addition, if and when these shares are issued, the percentage of our common stock that existing stockholders own will be diluted.

Our certificate of incorporation and bylaws and Delaware law contain provisions that could discourage a takeover.

Provisions of our amended and restated certificate of incorporation may have the effect of making it more difficult for a third party to acquire, or of discouraging a third party from attempting to acquire, control of us. These provisions could limit the price that certain investors might be willing to pay in the future for shares of our common stock. These provisions:

- divide our board of directors into three classes serving staggered three-year terms;

- only permit removal of directors by stockholders "for cause," and require the affirmative vote of at least 85% of the outstanding common stock to so remove; and

- allow us to issue preferred stock without any vote or further action by the stockholders.

The classification system of electing directors and the removal provision may tend to discourage a third-party from making a tender offer or otherwise attempting to obtain control of us and may maintain the incumbency of our board of directors, as the classification of the board of directors increases the difficulty of replacing a majority of the directors. These provisions may have the effect of deferring hostile takeovers, delaying changes in our control or management, or may make it more difficult for stockholders to take certain corporate actions. The amendment of any of these provisions would require approval by holders of at least 85% of the outstanding common stock.

Israel-Related Risks

A significant portion of our operations takes place in Israel, and we could be adversely affected by the economic, political and military conditions in that region.

The offices and facilities of three of our subsidiaries, EFL, MDT and Epsilor, are located in Israel (in Beit Shemesh, Lod and Dimona, respectively, all of which are within Israel's pre-1967 borders). Most of our senior management is located at EFL's facilities. Although we expect that most of our sales will be made to customers outside Israel, we are nonetheless directly affected by economic, political and military conditions in that country. Accordingly, any major hostilities involving Israel or the interruption or curtailment of trade between Israel and its present trading partners could have a material adverse effect on our operations. Since the establishment of the State of Israel in 1948, a number of armed conflicts have taken place between Israel and its Arab neighbors and a state of hostility, varying in degree and intensity, has led to security and economic problems for Israel.

Historically, Arab states have boycotted any direct trade with Israel and to varying degrees have imposed a secondary boycott on any company carrying on trade with or doing business in Israel. Although in October 1994, the states comprising the Gulf Cooperation Council (Saudi Arabia, the United Arab Emirates, Kuwait, Dubai, Bahrain and Oman) announced that they would no longer adhere to the secondary boycott against Israel, and Israel has entered into certain agreements with Egypt, Jordan, the Palestine Liberation Organization and the Palestinian Authority, Israel has not entered into any peace arrangement with

Syria or Lebanon. Moreover, since September 2000, there has been a significant deterioration in Israel's relationship with the Palestinian Authority, and a significant increase in terror and violence. Efforts to resolve the problem have failed to result in an agreeable solution. Continued hostilities between the Palestinian community and Israel and any failure to settle the conflict may have a material adverse effect on our business and us. Moreover, the current political and security situation in the region has already had an adverse effect on the economy of Israel, which in turn may have an adverse effect on us.

Service of process and enforcement of civil liabilities on us and our officers may be difficult to obtain.

We are organized under the laws of the State of Delaware and will be subject to service of process in the United States. However, approximately 35% of our assets are located outside the United States. In addition, two of our directors and all of our executive officers are residents of Israel and a portion of the assets of such directors and executive officers are located outside the United States.

There is doubt as to the enforceability of civil liabilities under the Securities Act of 1933, as amended, and the Securities Exchange Act of 1934, as amended, in original actions instituted in Israel. As a result, it may not be possible for investors to enforce or effect service of process upon these directors and executive officers or to judgments of U.S. courts predicated upon the civil liability provisions of U.S. laws against our assets, as well as the assets of these directors and executive officers. In addition, awards of punitive damages in actions brought in the U.S. or elsewhere may be unenforceable in Israel.

Exchange rate fluctuations between the U.S. dollar and the Israeli NIS may negatively affect our earnings.

Although a substantial majority of our revenues and a substantial portion of our expenses are denominated in U.S. dollars, a portion of our costs, including personnel and facilities-related expenses, is incurred in New Israeli Shekels (NIS). Inflation in Israel will have the effect of increasing the dollar cost of our operations in Israel, unless it is offset on a timely basis by a devaluation of the NIS relative to the dollar. In 2003, the inflation adjusted NIS appreciated against the dollar, which raised the dollar cost of our Israeli operations.

Some of our agreements are governed by Israeli law.

Israeli law governs some of our agreements, such as our lease agreements on our subsidiaries' premises in Israel, and the agreements pursuant to which we purchased IES, MDT and Epsilor. While Israeli law differs in certain respects from American law, we do not believe that these differences materially adversely affect our rights or remedies under these agreements.

ITEM 3. QUANTITATIVE AND QUALITATIVE DISCLOSURES ABOUT MARKET RISK.

Interest Rate Risk

It is our policy not to enter into interest rate derivative financial instruments, except for hedging of foreign currency exposures discussed below. We do not currently have any significant interest rate exposure.

Foreign Currency Exchange Rate Risk

Since a significant part of our sales and expenses are denominated in U.S. dollars, we have experienced only insignificant foreign exchange gains and losses to date, and do not expect to incur significant gains and losses in 2004. Our research, development and production activities are primarily carried out by our Israeli subsidiary, EFL, at its facility in Beit Shemesh, and accordingly we have sales and expenses in NIS. Additionally, our MDT and Epsilor subsidiaries operate primarily in NIS. However, the majority of our sales are made outside Israel in U.S. dollars, and a substantial portion of our costs are incurred in U.S. dollars. Therefore, our functional currency is the U.S. dollar.

While we conduct our business primarily in U.S. dollars, some of our agreements are denominated in foreign currencies, and we occasionally hedge part of the risk of a devaluation of the U.S dollar, which could have an adverse effect on the revenues that we incur in foreign currencies. We do not hold or issue derivative financial instruments for trading or speculative purposes

ITEM 4. CONTROLS AND PROCEDURES.

As of the end of the third quarter of 2004, our management, including the principal executive officer and principal financial officer, evaluated the effectiveness of our disclosure controls and procedures related to the

recording, processing, summarization, and reporting of information in our periodic reports that we file with the SEC. These disclosure controls and procedures have been designed to ensure that material information relating to us, including our subsidiaries, is made known to our management, including these officers, by other of our employees, and that this information is recorded, processed, summarized, evaluated and reported, as applicable, within the time periods specified in the SEC's rules and forms. Due to the inherent limitations of control systems, not all misstatements may be 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. Our controls and procedures can only provide reasonable, not absolute, assurance that the above objectives have been met.

As of September 30, 2004, based upon their evaluations, these officers concluded that the design of the disclosure controls and procedures are effective in ensuring that information required to be disclosed by us in the reports that we file or submit under the Exchange Act is recorded, processed, summarized, evaluated and reported, as applicable, within the time periods specified in the SEC's rules and forms. We intend to continually strive to improve our disclosure controls and procedures to enhance the quality of our financial reporting.

There have been no changes in our internal control over financial reporting that occurred during the fiscal quarter to which this Quarterly Report on Form 10-Q relates that have materially affected, or are reasonably likely to materially affect, our internal control over financial reporting.

Pursuant to Section 404 of the Sarbanes-Oxley Act of 2002, beginning with our Annual Report on Form 10-K for the fiscal year ending December 31, 2004, we will be required to furnish a report by management on our internal control over financial reporting. Such report will contain, among other matters, an assessment of the effectiveness of our internal control over financial reporting as of December 31, 2004, including a statement as to whether or not our internal control over financial reporting is effective. This assessment must include disclosure of any material weaknesses in our internal control over financial reporting identified by management. Such report must also contain a statement that our auditors have issued an attestation report on management's assessment of such internal controls. Public Company Oversight Board Auditing Standard No. 2 provides the professional standards and related performance guidance for auditors to attest to, and report on, management's assessment of the effectiveness of internal control over financial reporting under Section 404.

While we currently believe that our internal control over financial reporting is effective, we are still performing the system and process documentation and evaluation needed to comply with Section 404, which is both costly and challenging. During this process, if our management identifies one or more material weaknesses in our internal control over financial reporting, we will be unable to assert that such internal control is effective. If we are unable to assert that our internal control over financial reporting is effective as of December 31, 2004 (or if our auditors are unable to attest that our management's report is fairly stated or are unable to express an opinion on the effectiveness of our internal controls), we could lose investor confidence in the accuracy and completeness of our financial reports, which could have an adverse effect on our stock price.

While we currently anticipate being able to satisfy the requirements of Section 404 in a timely fashion, we cannot be certain as to the timing of completion of our evaluation, testing and any required remediation, especially with respect to certain entities that we have acquired during 2004, due in large part to the fact that there is no precedent available by which to measure compliance with the new Auditing Standard No. 2.

PART II

ITEM 2. CHANGES IN SECURITIES AND USE OF PROCEEDS.

Issuance of Warrants to Investors

In July 2004, warrants to purchase 8,814,235 shares of common stock, having an aggregate exercise price of $16,494,194, were exercised. In connection with this exercise, we issued to those exercising warrants an aggregate of 8,717,265 new five-year warrants to purchase shares of common stock at an exercise price of $1.38 per share.

We issued the above new warrants in reliance on the exemption from registration provided by Section 4(2) of the Securities Act as transactions by an issuer not involving a public offering. The issuance of these securities was without the use of an underwriter, and the shares of common stock currently bear restrictive legends permitting transfer thereof only upon registration or an

exemption under the Act.

ITEM 5. OTHER INFORMATION.

We will be holding a Special Meeting of Stockholders on Tuesday, December 14, 2004, to consider and act upon a proposal to ratify, for purposes of NASD Marketplace Rule 4350(i)(1)(C)(ii), the issuance in July 2004 of five-year warrants to purchase up to 8,717,265 shares of our common stock at a price of $1.38 per share. We mailed our Notice and Proxy Statement for the 2004 Special Meeting of Stockholders on or about November 8, 2004.

ITEM 6. EXHIBITS AND REPORTS ON FORM 8-K.

(a) The following documents are filed as exhibits to this report:

Exhibit Number	Description
*10.1	Securities Purchase Agreement dated July 15, 2004
**10.2	Stock Purchase Agreement dated as of July 15, 2004 between Arotech Corporation and Armour of America, Incorporated and its sole shareholder
31.1	Certification of Chief Executive Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
31.2	Certification of Chief Financial Officer pursuant to Section 302 of the Sarbanes-Oxley Act of 2002
32.1	Certification of Chief Executive Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002
32.2	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

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* Incorporated by reference to our Current Report on Form 8-K filed on July 15, 2004

** Incorporated by reference to our Quarterly Report on Form 10-Q for the quarter ended June 30, 2004, filed on August 16, 2004

(b) The following reports on Form 8-K or Form 8-K/A were filed or furnished during the third quarter of 2004:

Date Filed	Item Reported
July 15, 2004	Item 5 - Other Events and Regulation FD Disclosure; and Item 7 - Financial Statements, Pro Forma Financial Information and Exhibits
August 10, 2004	Item 7 - Financial Statements, Pro Forma Financial Information and Exhibits; and Item 12 - Results of Operations and Financial Condition (furnished but not filed)
August 23, 2004	Item 2.01 - Completion of Acquisition or Disposition of Assets; and Item 9.01 - Financial Statements and Exhibits

SIGNATURES

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

Dated: November 22, 2004

AROTECH CORPORATION

By: /s/ Robert S. Ehrlich

Name: Robert S. Ehrlich
Title: Chairman, President and CEO
(Principal Executive Officer)

By: /s/ Avihai Shen

Name: Avihai Shen
Title: Vice President - Finance
(Principal Financial Officer)

AROTECH CORPORATION

EXHIBIT INDEX

Exhibit Number	Description
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32.2	Certification of Chief Financial Officer pursuant to Section 906 of the Sarbanes-Oxley Act of 2002

Exhibit 31.1

CERTIFICATION

I, Robert S. Ehrlich, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Arotech Corporation;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) for the registrant and we have:

(a) designed such disclosure controls and procedures, or caused such disclosure control and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

(b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this quarterly report based on such evaluation; and

(c) disclosed in this quarterly report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's first fiscal quarter in the case of this quarterly report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

(a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Dated: November 22, 2004

/s/ Robert S. Ehrlich

Robert S. Ehrlich, Chairman, President and CEO
(Principal Executive Officer)

A signed original of this written statement required by Section 302 has been provided to Arotech Corporation and will be retained by Arotech Corporation and furnished to the Securities and Exchange Commission or its staff upon request.

The foregoing certification is being furnished solely pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) and is not being filed as part of the Form 10-Q or as a separate disclosure document.

Exhibit 31.2

CERTIFICATION

I, Avihai Shen, certify that:

1. I have reviewed this quarterly report on Form 10-Q of Arotech Corporation;

2. Based on my knowledge, this quarterly report does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this quarterly report;

3. Based on my knowledge, the financial statements, and other financial information included in this quarterly report, fairly present in all material respects the financial condition, results of operations and cash flows of the registrant as of, and for, the periods presented in this quarterly report;

4. The registrant's other certifying officer and I are responsible for establishing and maintaining disclosure controls and procedures (as defined in Exchange Act Rules 13a-15(e) and 15d-15(e) for the registrant and we have:

(a) designed such disclosure controls and procedures, or caused such disclosure control and procedures to be designed under our supervision, to ensure that material information relating to the registrant, including its consolidated subsidiaries, is made known to us by others within those entities, particularly during the period in which this quarterly report is being prepared;

(b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this quarterly report our conclusions about the effectiveness of the disclosure controls and procedures as of the end of the period covered by this quarterly report based on such evaluation; and

(c) disclosed in this quarterly report any change in the registrant's internal control over financial reporting that occurred during the registrant's most recent fiscal quarter (the registrant's first fiscal quarter in the case of this quarterly report) that has materially affected, or is reasonably likely to materially affect, the registrant's internal control over financial reporting; and

5. The registrant's other certifying officer and I have disclosed, based on our most recent evaluation of internal control over financial reporting, to the registrant's auditors and the audit committee of registrant's board of directors (or persons performing the equivalent function):

(a) all significant deficiencies and material weaknesses in the design or operation of internal control over financial reporting which are reasonably likely to adversely affect the registrant's ability to record, process, summarize and report financial information; and

(b) any fraud, whether or not material, that involves management or other employees who have a significant role in the registrant's internal controls over financial reporting.

Dated: November 22, 2004

/s/ Avihai Shen

Avihai Shen, Vice President - Finance
(Principal Financial Officer)

A signed original of this written statement required by Section 302 has been provided to Arotech Corporation and will be retained by Arotech Corporation and furnished to the Securities and Exchange Commission or its staff upon request.

The foregoing certification is being furnished solely pursuant to Section 302 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) and is not being filed as part of the Form 10-Q or as a separate disclosure document.

Exhibit 32.1

WRITTEN STATEMENT

In connection with the Quarterly Report of Arotech Corporation (the "Company") on Form 10-Q for the quarterly period ended September 30, 2004 filed with the Securities and Exchange Commission (the "Report"), I, Robert S. Ehrlich, Chairman, President and Chief Executive Officer of the Company, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, hereby certify that to my knowledge, the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and the information contained in the Report fairly presents, in all material respects, the consolidated financial condition of the Company and its subsidiaries as of the dates presented and the consolidated results of operations of the Company and its subsidiaries for the periods presented.

Dated: November 22, 2004

By: /s/ Robert S. Ehrlich

Robert S. Ehrlich, Chairman, President and CEO
(Chief Executive Officer)

A signed original of this written statement required by Section 906 has been provided to Arotech Corporation and will be retained by Arotech Corporation and furnished to the Securities and Exchange Commission or its staff upon request.

The foregoing certification is being furnished solely pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) and is not being filed as part of the Form 10-Q or as a separate disclosure document.

Exhibit 32.2

WRITTEN STATEMENT

In connection with the Quarterly Report of Arotech Corporation (the "Company") on Form 10-Q for the quarterly period ended September 30, 2004 filed with the Securities and Exchange Commission (the "Report"), I, Avihai Shen, Vice President - Finance and Chief Financial Officer of the Company, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, hereby certify that to my knowledge, the Report fully complies with the requirements of Section 13(a) or 15(d) of the Securities Exchange Act of 1934, and the information contained in the Report fairly presents, in all material respects, the consolidated financial condition of the Company and its subsidiaries as of the dates presented and the consolidated results of operations of the Company and its subsidiaries for the periods presented.

Dated: November 22, 2004

By: /s/ Avihai Shen

Avihai Shen, Vice President - Finance
(Chief Financial Officer)

A signed original of this written statement required by Section 906 has been provided to Arotech Corporation and will be retained by Arotech Corporation and furnished to the Securities and Exchange Commission or its staff upon request.

The foregoing certification is being furnished solely pursuant to Section 906 of the Sarbanes-Oxley Act of 2002 (subsections (a) and (b) of Section 1350, Chapter 63 of Title 18, United States Code) and is not being filed as part of the Form 10-Q or as a separate disclosure document.