

ON THE COVER: BJ Services, a world-wide oil and gas well servicing company, hooked up 20 of their proprietary-design Gorilla fracturing units to perform a high-rate, high-pressure stimulation operation for a major independent gas producer's well in west Texas. Twin Disc re-engineered its powerful 8500 automatic transmission to accommodate the Gorilla's tremendous 2700 hydraulic horsepower. To accomplish the much higher pumping capacity of the 20 Gorilla units would have required 36 old-style frac rigs and a larger work site.



ABOVE: Twin Disc MGX-5135 QuickShift® marine transmissions help this Azimut 62 perform beautifully.

TWIN DISC, INC.

TWIN DISC, INCORPORATED is an international manufacturer and distributor of heavy-duty off-highway power transmission equipment. Company engineers work hand-in-hand with customers and engine manufacturers to design products with characteristics unique to their specific applications. Twin Disc supplies the commercial, pleasure craft and military segments of the marine market with

transmissions, surface and waterjet drives and electronic controls. Its off-highway transmission products are used in agricultural, all-terrain specialty vehicle and military applications. Twin Disc also sells industrial products such as power take-offs, mechanical, hydraulic, and modulating clutches and control systems to the agricultural, environmental and energy and natural resources markets.

The Corporation, which is a multinational organization headquartered in Racine, Wisconsin, currently has a diverse shareholder base with approximately one-third of the outstanding shares held by management, active and retired employees and other long-term investors.

FINANCIAL HIGHLIGHTS

	2004	2003	2002
Net Sales	\$186,089	\$179,591	\$179,385
Net Earnings (Loss)	5,243	(2,368)	2,058
Basic Earnings (Loss) Per Share	1.86	(0.84)	0.73
Diluted Earnings (Loss) Per Share	1.84	(0.84)	0.73
Dividends Per Share	0.70	0.70	0.70
Average Shares Outstanding For The Year	2,814,197	2,804,915	2,807,832
Fully Diluted Shares Outstanding For The Year	2,843,374	2,804,915	2,807,832

SALES AND EARNINGS BY QUARTER

2004	1ST QTR	2ND QTR	3RD QTR	4TH QTR	YEAR
Net Sales	\$37,966	\$42,371	\$48,606	\$57,146	\$186,089
Gross Profit	8,896	10,721	12,917	15,096	47,630
Net Earnings (Loss)	171	508	1,776	2,788	5,243
Basic Earnings (Loss) Per Share	0.06	0.18	0.63	0.99	1.86
Diluted Earnings (Loss) Per Share	0.06	0.18	0.62	0.97	1.84
Dividends Per Share	0.175	0.175	0.175	0.175	0.70
Stock Price Range (High – Low)	17.00 – 14.12	19.54 – 16.55	21.25 – 19.00	25.15 – 19.44	25.15 – 14.12

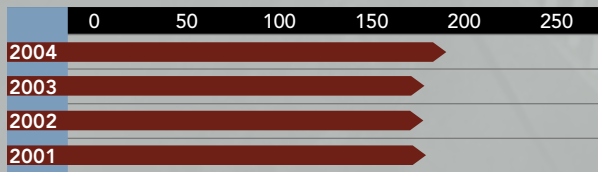
2003

Net Sales	\$36,521	\$42,794	\$47,177	\$53,099	\$179,591
Gross Profit	5,930	6,680	10,425	11,981	35,016
Net Earnings (Loss)	(1,731)	(3,087)	509	1,941	(2,368)
Basic Earnings (Loss) Per Share	(0.62)	(1.10)	0.18	0.70	(0.84)
Diluted Earnings (Loss) Per Share	(0.62)	(1.10)	0.18	0.70	(0.84)
Dividends Per Share	0.175	0.175	0.175	0.175	0.70
Stock Price Range (High – Low)	15.14 – 12.90	13.25 – 11.90	13.35 – 9.90	14.35 – 10.70	15.14 – 9.90

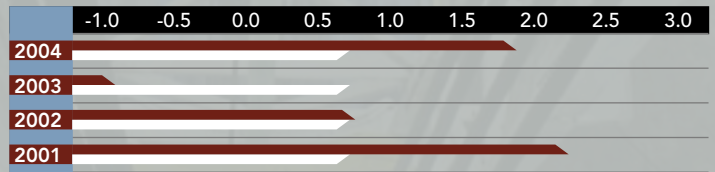
In thousands of dollars except per share and stock price range statistics.



NET SALES (\$ millions)



BASIC EARNINGS [LOSS] (\$ per share)
DIVIDENDS



Because of their large horsepower capacities and rugged reliability, Twin Disc transmissions and torque converters are hard at work in the oil and gas fields.

TO OUR SHAREHOLDERS

This past year was very gratifying for Twin Disc. We are pleased to report strong financial results for fiscal 2004. Nearly 18 months ago, we developed a course of action to restore profitability and financial growth to position Twin Disc to participate more successfully in an increasingly competitive world economy. For the plan to succeed, everyone in the Company had to work together in understanding and implementing actions that would lead to this important result.

The restructuring of our domestic and Belgian operations served as the core of our financial turnaround, which was aided by an improving domestic economy, especially during the latter half of fiscal 2004. In addition to the financial improvements, on an operating basis, we have improved our cost effectiveness, our ability to provide quality products and our sales and engineering support. Further, we have introduced innovative designs and expanded our product offerings. Finally, in May, we

Financial Results

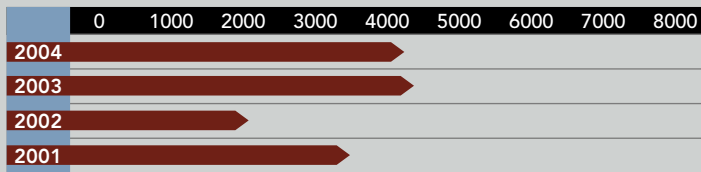
For fiscal 2004, net sales increased 3.6 percent to \$186,089,000 compared to \$179,591,000 for the previous year. However, net income for fiscal 2004 rebounded by \$7,611,000 to \$5,243,000, or \$1.84 per share from a net loss of \$2,368,000, or \$0.84 per share a year ago.

Net favorable currency exchange rates benefited fiscal 2004 net sales by approximately \$10,000,000, or nearly five percent. Further, fiscal year 2003 net sales included \$13,000,000 from our Japanese distribution subsidiary, which, due to a change in our operating agreement, were not recognized in fiscal 2004. This change had no impact on earnings. The implementation of cost reductions and restructuring plans, along with a better product mix and manufacturing efficiencies, improved profitability significantly. In spite of elevated raw material prices, the gross profit margin reached 25.6 percent – the highest level in more than 20 years.

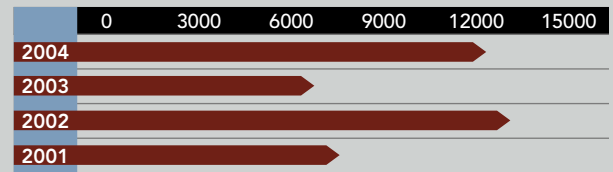
During the year we sold our 25 percent interest in Palmer Johnson Distributors, LLC (PJD) to its majority shareholder for \$3,811,000 in cash. PJD had been a very good investment for Twin Disc, but we decided that we would reinvest our funds in our acquisition program. PJD is well managed and remains one of our major North American distributors. Later in the year we purchased 100 percent of Rolla SP Propellers SA for \$5,085,000. The inclusion of Rolla in the Twin Disc family significantly strengthens our position in the marine propulsion market and adds a great deal to our favorable outlook.



CAPITAL EXPENDITURES (\$ thousands)



NET CASH PROVIDED [USED] BY OPERATING ACTIVITIES (\$ thousands)



completed an important acquisition that will further strengthen our technological leadership and expand our position in the marine propulsion market.

We are encouraged by the progress achieved during the past year in our financial and operating performance. For fiscal 2005, we are optimistic that our results will continue to gain momentum as the year progresses despite a challenging global environment.

For fiscal 2004, we were successful in improving cash flows considerably to \$12,240,000 from \$6,710,000 the previous year. Strong management of our operating cash flows will allow us to make the necessary investments in product development and capital equipment that will maintain our competitive edge in the years ahead. Capital expenditures for the year totaled \$4,180,000 and are expected to increase to nearly \$10,000,000 for fiscal 2005.

Shareholders' equity increased nearly 21 percent during the year to \$60,731,000, or \$21.37 per share, while long-term debt rose modestly.



Aircraft Rescue and Fire Fighting (ARFF) vehicle manufacturers around the world depend on Twin Disc 1175 automatic transmission systems to make their trucks fast and effective.

Operations Review

As we entered fiscal 2004, we had modest expectations about the year ahead. Most of our commercial markets had been through a soft period, although preliminary signs were pointing to a recovery. Also, we had won a military transmission contract, but program delays were being encountered and our production schedule was slipping. Nevertheless, we were optimistic that we would see year-over-year favorable comparisons with the previous recessionary year.

Beginning in the first quarter of fiscal 2004, demand from the oilfield and military vehicles for Iraq began to strengthen considerably and offset the delays in the aforementioned contract. Demand for our transmissions remained strong during the remainder of the year and we began production of the military contract during the fourth quarter.

Demand for our industrial products, mainly clutches and power take-offs for irrigation and recycling applications, remained soft during the first two quarters but showed improvement in the final six months of the year.

Shipments of marine transmissions for the pleasure craft market showed continual improvement during the year primarily in the North American market. Demand in Europe remained soft for most of the year.

Activity in the commercial marine markets was mixed. New boat construction along the US Gulf Coast for use in the offshore oil industry was down, but re-powering projects offset this decline. Demand in the Pacific Basin was brisk, and we expanded our market share in Europe, aided by the favorable currency exchange rates and improved manufacturing efficiencies.



We continued to achieve success in our propulsion business with expanding sales to both pleasure craft and military applications. The addition of Rolla Propellers makes our marine propulsion offering the premier high performance product line in the industry.

Officers and Directors

Paul J. Powers, a director of Twin Disc since 1992, will be retiring from the Board at the October 15, 2004 Annual Meeting. Paul has been an outstanding director and friend providing sound stewardship and counsel. We will miss him.

He will be replaced by Harold M. Stratton II, Chairman and Chief Executive Officer of Strattec Security Corporation, a designer, developer, manufacturer and marketer of mechanical and electro-mechanical locks and related security/access control products. We are excited to have Harry join our Board, as he brings a wealth of business experience and expertise to us.

During the year, Lance J. Melik, an officer and employee of the Company for more than three decades, retired. Lance was a key member of the management team, serving in both senior marketing and corporate development positions. We appreciate his many contributions to the well being of Twin Disc and wish him well in his retirement.

Outlook

During the course of fiscal 2004 our backlog increased more than 60 percent to its June 30, 2004 level of \$49,000,000. The rise in backlog reflected the improving business conditions encountered by the Company during the year.

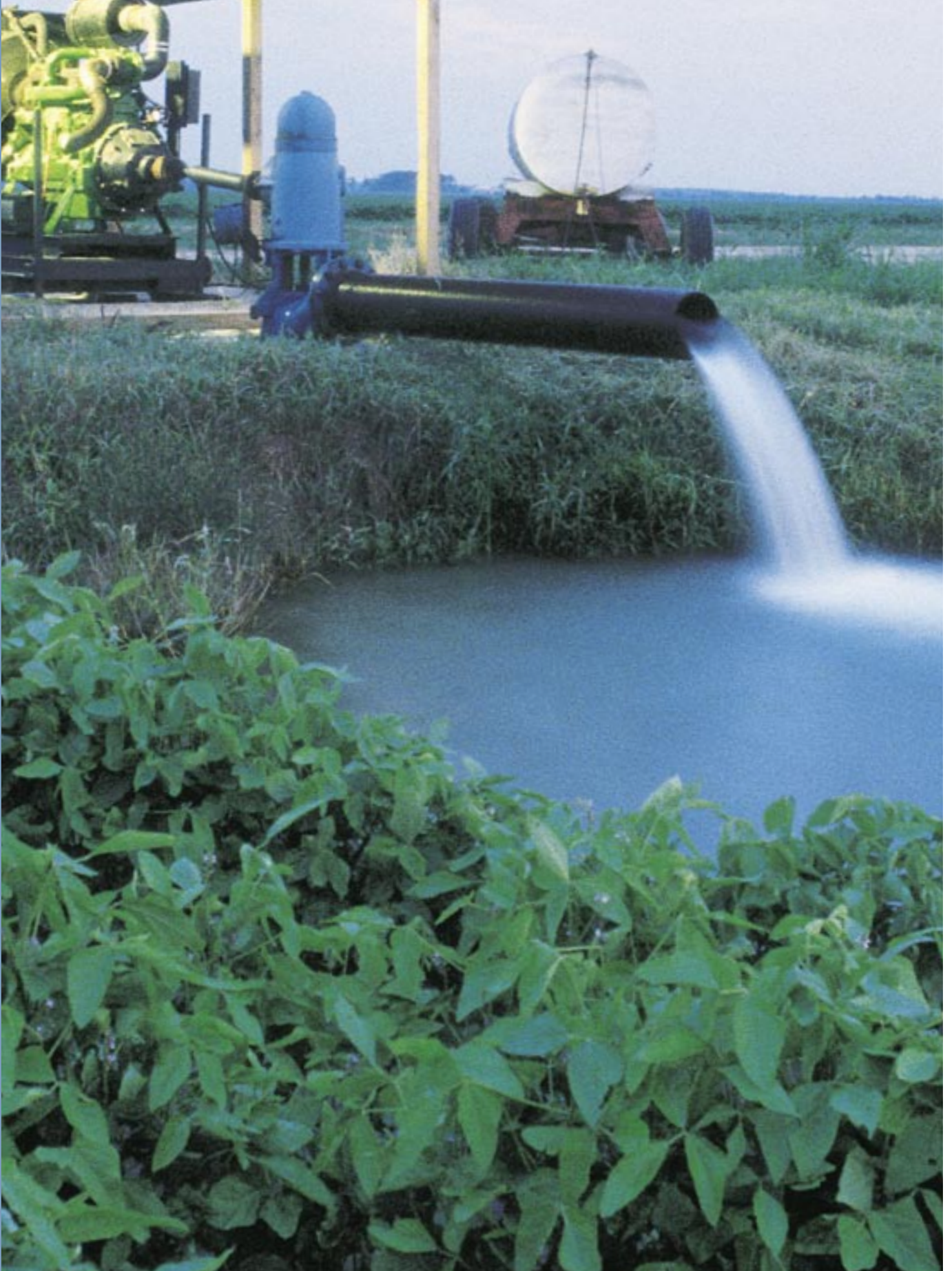
As we enter fiscal 2005 we are optimistic about our prospects for the year ahead. Order rates continue to improve and our production schedules are generally full. We expect continuing favorable year-over-year comparisons for the new fiscal year.



Michael H. Joyce
President, Chief Operating Officer

Michael E. Batten
Chairman, Chief Executive Officer





As one of the largest PTO manufacturers in the world, Twin Disc puts horsepower to work in all sorts of everyday applications.

PRODUCT ACTIVITY



Highlighting Some Of Our Corporate Culture

There is a special sense of optimism at Twin Disc reflecting our growing prominence in the marine, industrial and off-highway transmission markets. Twin Disc is well positioned to face global business challenges because we are able to answer the expanding needs of our customers.

With a physical presence wherever our products are used, we can effectively provide the necessary sales, service and engineering support regardless of how unique and versatile an application is. From design to aftermarket service, we are totally involved in the supply chain.

Much of our work today benefits our results for tomorrow. Our people are committed to the long run and make their decisions on that basis. We do not step away from investing in people, processes and equipment that help serve our customers better.



Transmission Products

The market for our heavy-duty transmissions led the improved performance at Twin Disc during the past year. A strong recovery in the land-based oil and natural gas markets in North America and abroad spurred demand for our 3,000 HP 8500 series transmission. These products are used in fracturing rigs that pump compressed fluids under great pressure to expand the underground caverns containing oil or gas. Additional demand



Industrial Products

Twin Disc's industrial products business reflected the resurgence of the global industrial market in fiscal 2004. Demand for our clutches and power take-offs improved primarily in the irrigation, rock crushing and recycling markets.

During the year we introduced more cost effective products to the market providing better value to our customers. Further, we



was experienced as a result of increased requirements for vehicles needed for military operations in Iraq. The market for Aircraft Rescue and Fire Fighting vehicles also exhibited strength during the year. And, we continue to develop new customers requiring our heavy-duty transmissions for commercial mining and hauling applications.

introduced new models of hydraulic power take-offs, which have been well received by our customers. In addition, we have introduced to the North American market a full line of pump drives produced by our Technodrive subsidiary and are encouraged by its initial acceptance.



Commercial work boats and fishing boats count on Twin Disc marine transmissions to handle the toughest of jobs in the roughest of waters.

Pleasure Craft Market

The continued release of our QuickShift® marine transmissions to the pleasure craft market was the driving force behind our improved results in this market segment. This new and innovative technology continues to receive positive market acceptance, increasing our market share, offsetting generally mixed results in the broader pleasure craft market. Demand has improved in North America while Europe has remained soft.

The benefits of this state-of-the-art transmission are convincing experienced boat owners and captains to insist that QuickShift®



is the only way to go. "You have to feel it to believe it" is often heard around the docks at fishing tournaments and boat builders' rendezvous. An integral part of the QuickShift® feature is the new EC300 Marine Electronic Control that is uniquely suited to provide superior performance to a QuickShift® application and which helped improve our market share. Our Express mode is unique to Twin Disc and allows for a full range of speed from ultra slow to full speed with a single-lever motion.

As we introduce additional QuickShift® models in a broader range of horsepower, we expect to gain additional market share with new classes of boat builders.



QUICKSHIFT®

Work Boat Market

We experienced mixed results for marine transmission demand from the work boat market in fiscal year 2004. New work boat construction in North America declined during the year as the offshore oil and gas industry slowed their drilling activity in the Gulf of Mexico. In spite of sharply higher oil prices, the large exploration companies declined to invest in deep water drilling in this area. However, repower activity offset the declines in new construction. Our development of QuickShift® for the four-engine crew boat market will help grow our sales in the work boat market in future years.

Overseas demand for large work boat transmissions was up significantly because of manufacturing efficiencies as well as the beneficial effect of the weak U.S. dollar compared with other foreign currencies. Sales to Europe and Southeast Asia were strong, as we gained market share.



Somewhat offsetting the growth in our work boat segment, demand from the fishing vessel market was soft due to low prices and higher operating costs. In addition, the shrimp and salmon market segments suffered from increased farm raised competition.



Sales of Twin Disc Arneson Surface Drives posted excellent results for the fiscal year enhancing its strong position in the military and European luxury yacht markets. As a result of heightened emphasis on coastal security, government spending on patrol boats has increased. Patrol boats using Twin Disc propulsion systems are greatly valued for their speed, agility and reliability.

Twin Disc surface drive sales into the domestic high performance boat market have increased steadily over the past three years as boat builders and users alike have begun to appreciate the performance and reliability that an Arneson-equipped boat can provide.



Finally, the recent acquisition of Rolla SP Propellers SA completes the technology of the entire propulsion system. Rolla brings not only the best propellers to the Twin Disc family, it also adds the most comprehensive and best fluid dynamic design technology in the world to the Twin Disc group. We are excited about the future prospects of our propulsion product line.

**UNITED STATES
SECURITIES AND EXCHANGE COMMISSION
Washington, D. C. 20549**

FORM 10-K

**ANNUAL REPORT PURSUANT TO SECTION 13 OR 15(d)
OF THE SECURITIES EXCHANGE ACT OF 1934
For the Fiscal Year Ended June 30, 2004**

Commission File Number 1-7635

TWIN DISC, INCORPORATED

(Exact Name of Registrant as Specified in its Charter)

Wisconsin

(State or Other Jurisdiction of
Incorporation or Organization)

39-0667110

(I.R.S. Employer
Identification Number)

1328 Racine Street, Racine, Wisconsin

(Address of Principal Executive Office)

53403

(Zip Code)

(262) 638-4000

Registrant's Telephone Number, including area code

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

Title of each class

Common stock, no par value

Name of each exchange on which registered:

New York Stock Exchange

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

Common stock, no par value

(Title of Class)

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

Indicate by check mark if disclosure of delinquent filers pursuant to Item 405 of Regulation S-K is not contained herein, and will not be contained, to the best of the registrant's knowledge, in definitive proxy or information statements incorporated by reference in Part III of this Form 10-K or any amendment to this Form 10-K.

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

At August 30, 2004, the aggregate market value of the common stock held by non-affiliates of the registrant was \$66,665,702. Determination of stock ownership by affiliates was made solely for the purpose of responding to this requirement and registrant is not bound by this determination for any other purpose.

At August 30, 2004, the registrant had 2,867,342 shares of its common stock outstanding.

DOCUMENTS INCORPORATED BY REFERENCE:

The incorporated portions of such documents being specifically identified in the applicable Items of this Report.

Portions of the Proxy Statement for the Annual Meeting of Shareholders to be held October 15, 2004 are incorporated by reference into Part III.

ITEM 1. BUSINESS

Twin Disc was incorporated under the laws of the state of Wisconsin in 1918. Twin Disc designs, manufactures and sells heavy duty off-highway power transmission equipment. Products offered include: hydraulic torque converters; power-shift transmissions; marine transmissions and surface drives; universal joints; gas turbine starting drives; power take-offs and reduction gears; industrial clutches; fluid couplings and control systems. The Company sells its products to customers primarily in the construction equipment, industrial equipment, government, marine, energy and natural resources and agricultural markets. The Company's worldwide sales to both domestic and foreign customers are transacted through a direct sales force and a distributor network. At the end of May, 2004, the Company acquired Rolla SP Propellers SA a manufacturer of custom high performance propellers. The products described above have accounted for more than 90% of revenues in each of the last three fiscal years.

Most of the Company's products are machined from cast iron, forgings, cast aluminum and bar steel which generally are available from multiple sources and which are believed to be in adequate supply.

The Company has pursued a policy of applying for patents in both the United States and certain foreign countries on inventions made in the course of its development work for which commercial applications are considered probable. The Company regards its patents collectively as important but does not consider its business dependent upon any one of such patents.

The business is not considered to be seasonal except to the extent that employee vacations are taken mainly in the months of July and August curtailing production during that period.

The Company's products receive direct widespread competition, including from divisions of other larger independent manufacturers. The Company also competes for business with parts manufacturing divisions of some of its major customers. Primary competitive factors for the Company's products are performance, price, service and availability. Ten customers accounted for approximately 32% of the Company's consolidated net sales during the year ended June 30, 2004. Sewart Supply, Inc., an independent distributor of Twin Disc products, accounted for approximately 11% of consolidated net sales in 2004.

Unfilled open orders for the next six months of \$49,400,000 at June 30, 2004 compares to \$30,593,000 at June 30, 2003. Since orders are subject to cancellation and rescheduling by the customer, the six-month order backlog is considered more representative of operating conditions than total backlog. However, as procurement and manufacturing "lead times" change, the backlog will increase or decrease; and thus it does not necessarily provide a valid indicator of the shipping rate. Cancellations are generally the result of rescheduling activity and do not represent a material change in backlog.

Management recognizes that there are attendant risks that foreign governments may place restrictions on dividend payments and other movements of money, but these risks are considered minimal due to the political relations the United States maintains with the countries in which the Company operates or the relatively low investment within individual countries. The Company's business is not subject to renegotiation of profits or termination of contracts at the election of the Government.

Engineering and development costs include research and development expenses for new product development and major improvements to existing products, and other charges for ongoing efforts to refine existing products. Research and development costs charged to operations totaled \$2,840,000, \$2,220,000 and \$1,887,000 in 2004, 2003 and 2002, respectively. Total engineering and development costs were \$7,600,000, \$7,190,000 and \$6,718,000 in 2004, 2003 and 2002, respectively.

Compliance with federal, state and local provisions regulating the discharge of materials into the environment, or otherwise relating to the protection of the environment, is not anticipated to have a material effect on capital expenditures, earnings or the competitive position of the Company.

The number of persons employed by the Company at June 30, 2004 was 860.

A summary of financial data by segment and geographic area for the years ended June 30, 2004, 2003 and 2002 appears in Note M to the consolidated financial statements on pages 30 through 32 of this form.

ITEM 2. PROPERTIES

The Company owns two manufacturing, assembly and office facilities in Racine, Wisconsin, U.S.A., one in Nivelles, Belgium and one in Decima, Italy. The aggregate floor space of these four plants approximates 692,000 square feet. One of the Racine facilities includes office space, which is the location of the Company's corporate headquarters. The Company leases additional manufacturing, assembly and office facilities in Decima, Italy and Balerna, Switzerland

The Company also has operations in the following locations, all of which are used for sales offices, warehousing and light assembly or product service. The following properties are leased:

Jacksonville, Florida, U.S.A.	Edmonton, Alberta, Canada	Singapore
Miami, Florida, U.S.A.	Vancouver, British Columbia, Canada	Shanghai, China
Coburg, Oregon, U.S.A.	Brisbane, Queensland, Australia	Capezzano Planore, Italy
Kent, Washington, U.S.A.	Perth, Western Australia, Australia	

The properties are generally suitable for operations and are utilized in the manner for which they were designed. Manufacturing facilities are currently operating at less than 80% capacity and are adequate to meet foreseeable needs of the Company.

ITEM 3. LEGAL PROCEEDINGS

Twin Disc is a defendant in several product liability or related claims considered either adequately covered by appropriate liability insurance or involving amounts not deemed material to the business or financial condition of the Company.

ITEM 4. SUBMISSION OF MATTERS TO A VOTE OF SECURITY HOLDERS

No matters were submitted to a vote of security holders during the fourth quarter of the year ended June 30, 2004.

Executive Officers of the Registrant

Pursuant to General Instruction G(3) of Form 10-K, the following list is included as an unnumbered Item in Part I of this Report in lieu of being included in the Proxy Statement for the Annual Meeting of Shareholders to be held on October 15, 2004.

Name	Principal Occupation Last Five Years	Age
Michael E. Batten	Chairman, Chief Executive Officer since 1983	64
Michael H. Joyce	President – Chief Operating Officer since 1995	63
James E. Feiertag	Executive Vice President since November 2002; formerly Vice President – Manufacturing since November 2000; formerly Vice President of Manufacturing for the Drives and Systems Group, Rockwell Automation Group since 1999	47
Christopher J. Eperjesy	Vice President – Finance and Treasurer since October 2001; formerly Divisional Vice President – Financial Planning & Analysis, Kmart Corporation since 2001; formerly Senior Manager – Corporate Finance, DaimlerChrysler AG since 1999	36
Henri Claude Fabry	Vice President – Global Distribution since October 2001; formerly Vice President – Marine and Distribution since June 1999	58
Fred H. Timm	Vice President – Administration and Secretary since October 2001; formerly Corporate Controller and Secretary since 1995	58
John H. Batten	Vice President and General Manager – Marine and Propulsion since October 2001; formerly Commercial Manager – Marine and Propulsion since 1998	39

Officers are elected annually by the Board of Directors at the Board meeting held preceding each Annual Meeting of the Shareholders. Each officer holds office until his successor is duly elected, or until he resigns or is removed from office. John H. Batten is the son of Michael E. Batten.

ITEM 5. MARKET FOR THE REGISTRANT'S COMMON STOCK AND RELATED STOCKHOLDER MATTERS

The Company's common stock is traded on the New York Stock Exchange under the symbol TDI. The price information below represents the high and low sales prices for each period:

Fiscal Year Ended June 30, 2004			Fiscal Year Ended June 30, 2003		
	High	Low		High	Low
First Quarter	17.00	14.12	First Quarter	15.14	12.90
Second Quarter	19.54	16.55	Second Quarter	13.25	11.90
Third Quarter	21.25	19.00	Third Quarter	13.35	9.90
Fourth Quarter	25.15	19.44	Fourth Quarter	14.35	10.70

Quarterly dividends of \$0.175 per share were declared and paid for each of the quarters above. As of June 30, 2004 there were 917 shareholder accounts. The sales price of Twin Disc common stock as of August 30, 2004 was \$23.25.

Pursuant to a shareholder rights plan (the "Rights Plan"), on April 17, 1998, the Board of Directors declared a dividend distribution, payable to shareholders of record at the close of business on June 30, 1998, of one Preferred Stock Purchase Right ("Rights") for each outstanding share of Common Stock. The Rights will expire 10 years after issuance, and will be exercisable only if a person or group becomes the beneficial owner of 15% or more of the Common Stock (or 25% in the case of any person or group which currently owns 15% or more of the shares or who shall become the Beneficial Owner of 15% or more of the shares as a result of any transfer by reason of the death of or by gift from any other person who is an Affiliate or an Associate of such existing holder or by succeeding such a person as trustee of a trust existing on the record date) (an "Acquiring Person"), or 10 business days following the commencement of a tender or exchange offer that would result in the offeror beneficially owning 25% or more of the Common Stock. A person who is not an Acquiring Person will not be deemed to have become an Acquiring Person solely as a result of a reduction in the number of shares of Common Stock outstanding due to a repurchase of Common Stock by the Company until such person becomes beneficial owner of any additional shares of Common Stock. Each Right will entitle shareholders who received the Rights to buy one newly issued unit of one one-hundredth of a share of Series A Junior Preferred Stock at an exercise price of \$160, subject to certain anti-dilution adjustments. The Company will generally be entitled to redeem the Rights at \$.05 per Right at any time prior to 10 business days after a public announcement of the existence of an Acquiring Person. In addition, if (i) a person or group accumulates more than 25% of the Common Stock (except pursuant to an offer for all outstanding shares of Common Stock which the independent directors of the Company determine to be fair to and otherwise in the best interests of the Company and its shareholders and except solely due to a reduction in the number of shares of Common Stock outstanding due to the repurchase of Common Stock by the Company), (ii) a merger takes place with an Acquiring Person where the Company is the surviving corporation and its Common Stock is not changed or exchanged, (iii) an Acquiring Person engages in certain self-dealing transactions, or (iv) during such time as there is an Acquiring Person, an event occurs which results in such Acquiring Person's ownership interest being increased by more than 1% (e.g., a reverse stock split), each Right (other than Rights held by the Acquiring Person and certain related parties which become void) will represent the right to purchase, at the exercise price, Common Stock (or in certain circumstances, a combination of securities and/or assets) having a value of twice the exercise price. In addition, if following the public announcement of the existence of an Acquiring Person the Company is acquired in a merger or other business combination transaction, except a merger or other business combination transaction that takes place after the consummation of an offer for all outstanding shares of Common Stock that the independent directors of the Company have determined to be fair, or a sale or transfer of 50% or more of the Company's assets or earning power is made, each Right (unless previously voided) will represent the right to purchase, at the exercise price, common stock of the acquiring entity having a value of twice the exercise price at the time.

The Rights may have certain anti-takeover effects. The Rights will cause substantial dilution to a person or group that attempts to acquire the Company without conditioning the offer on a substantial number of Rights being acquired. However, the Rights are not intended to prevent a take-over, but rather are designed to enhance the ability of the Board of Directors to negotiate with an acquirer on behalf of all of the shareholders. In addition, the Rights should not interfere with a proxy contest.

The Rights should not interfere with any merger or other business combination approved by the Board of Directors since the Rights may be redeemed by the Company at \$.05 per Right prior to 10 business days after the public announcement of the existence of an Acquiring Person.

The news release announcing the declaration of the Rights dividend, dated April 17, 1998, filed as Item 14(a)(3), Exhibit 4(b) of Part IV of the Annual Report on Form 10-K for the year ended June 30, 1998 is hereby incorporated by reference.

Recent Sales of Unregistered Securities

During the period covered by this report, the Company offered participants in the Twin Disc, Incorporated B The Accelerator 401(k) Savings Plan (the "Plan") the option to invest their Plan accounts in a fund comprised of Company stock. Participation interests of Plan participants in the Plan, which may be considered securities, were not registered with the SEC. During the fiscal year ended June 30, 2002, 68 Plan participants allocated an aggregate of \$81,000 toward this investment option. Participant accounts in the Plan consist of a combination of employee deferrals, Company matching contributions, and, in some cases, additional Company profit-sharing contributions. No underwriters were involved in these transactions. On September 6, 2002, the Company filed a Form S-8 to register 100,000 shares of Company common stock offered through the Plan, as well as an indeterminate amount of Plan participation interests.

ITEM 6. SELECTED FINANCIAL DATA

Financial Highlights

(dollars in thousands, except per share amounts and shares outstanding)

Statement of Operations Data:	For the years ended June 30,				
	2004	2003	2002	2001	2000
Net sales	\$186,089	\$179,591	\$179,385	\$180,786	\$177,987
Net earnings (loss)	5,243	(2,368)	2,058	6,169	3,773
Basic earnings (loss) per share	1.86	(.84)	.73	2.20	1.34
Diluted earnings (loss) per share	1.84	(.84)	.73	2.20	1.34
Dividends per share .....	.70	.70	.70	.70	.70
 Balance Sheet Data (at end of period):					
Total assets	176,637	170,358	157,280	156,734	174,190
Total long-term debt	16,813	16,584	18,583	23,404	31,524

Effective May 31, 2004, the company acquired 100% of the common stock of Rolla SP Propellers SA of Balerna, Switzerland. Rolla designs and manufactures custom propellers. Rolla will have a fiscal year ended May 31, since the acquisition was also effective May 31. No results of operations of Rolla are included in consolidated results for the year ended June 30, 2004.

In January 2004, the Company sold its 25% minority interest in Palmer Johnson Distributors, LLC (PJD) to the majority holder, PJD, Inc. for \$3,811,000 cash, which approximated the net book value of the investment. The Company recognized pre-tax earnings of \$240,000, \$414,000 and \$481,000 in fiscal years 2004, 2003 and 2002 respectively, from its investment in PJD. In addition, the Company received cash distributions of \$195,000, \$303,000 and \$400,000 in fiscal years 2004, 2003 and 2002, respectively.

During the third quarter of 2001, the Company sold its investment in Niigata Converter Company, Ltd., resulting in a net gain of \$2,288,000 or \$.81 per share.

On April 2, 2001, the Company entered into a Joint Venture Agreement with Niigata Engineering Co. LTD., Japan to form NICO Transmissions Co., Inc. (NTC). Effective April 1, 2003, Niigata Engineering Co. LTD's ownership interest was transferred to Hitachi Nico Transmission Co. LTD. and NTC was renamed Twin Disc Nico Co. LTD (TDN). TDN's balance sheet as of March 31, 2004 and 2003 are consolidated with the Company's balance sheet as of June 30, 2004 and 2003, respectively. TDN's statement of operations for the years ended March 31, 2004, 2003 and 2002 are consolidated with the Company's statement of operations for the years ended June 30, 2004, 2003 and 2002, respectively. TDN contributed the following for the years ended June 30 (dollars in thousands, except per share amounts):

	2004	2003	2002
Net sales	\$ 1,180	\$13,708	\$12,217
Net earnings	48	23	263
Basic and diluted earnings per share .....	.02	.01	.09
Total assets	3,162	6,076	6,169
Total long-term debt	0	0	0

ITEM 7. MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

Note on Forward-Looking Statements

Statements in this report (including but not limited to certain statements in Items 1, 3 and 7) and in other Company communications that are not historical facts are forward-looking statements, which are based on management's current expectations. These statements involve risks and uncertainties that could cause actual results to differ materially from what appears here.

Forward-looking statements include the Company's description of plans and objectives for future operations and assumptions behind those plans. The words "anticipates," "believes," "intends," "estimates," and "expects," or similar anticipatory expressions, usually identify forward-looking statements. In addition, goals established by Twin Disc, Incorporated should not be viewed as guarantees or promises of future performance. There can be no assurance the Company will be successful in achieving its goals.

In addition to the assumptions and information referred to specifically in the forward-looking statements, other factors could cause actual results to be materially different from what is presented here.

Results of Operations

<i>(In thousands)</i>	<u>2004</u>	<u>%</u>	<u>2003</u>	<u>%</u>	<u>2002</u>	<u>%</u>
Net sales	\$186,089		\$179,591		\$179,385	
Cost of goods sold	138,459		144,575		139,146	
Gross profit	47,630	25.6%	35,016	19.5%	40,239	22.4%
Marketing, engineering and administrative expenses	37,168	20.0%	34,790	19.4%	34,638	19.3%
Restructuring of operations	—	0%	2,042	1.1%	—	0%
Earnings (loss) from operations	<u>\$ 10,462</u>	<u>5.6%</u>	<u>\$ (1,816)</u>	<u>(1.0%)</u>	<u>\$ 5,601</u>	<u>3.1%</u>

Fiscal 2004 Compared to Fiscal 2003

Net Sales

Net sales increased \$6.5 million, or nearly four percent in fiscal 2004. In fiscal 2004, the joint venture agreement governing Twin Disc Nico Co., LTD (TDN) was amended. Under the new agreement, sales into certain territories have been transferred to the joint venture partner in exchange for which TDN receives a product development fee equal to the gross margin formerly earned on such sales. The effect of this change was to reduce sales by \$13.7 million for the fiscal year ended June 30, 2004, with no effect on net earnings. Product development fees included in net sales in fiscal year 2004 approximated \$0.7 million. In fiscal 2003, the company recognized \$13.0 million of sales that are no longer recognized in accordance with the new agreement. As a result of the strong euro and Asian currencies versus the dollar, foreign currency exchange had a net favorable impact on sales of \$10.4 million in fiscal 2004, compared to fiscal 2003.

In fiscal 2004, sales for our worldwide manufacturing operations, before eliminating intra-segment and inter-segment sales, were \$19.0 million, or 12.3%, higher than in the prior year. Over half of this increase came at our domestic manufacturing operations, which saw a recovery across most of its product markets. Of the remaining increase, approximately \$5.9 million was due to the impact of net favorable exchange rate movements on our European operations in Belgium and Italy.

Net sales for distribution operations were down \$4.2 million, or 6.7%, in fiscal 2004. However, there was a \$13.0 million decrease due to the change in the TDN agreement mentioned above. Adjusting for this change, sales were \$8.8 million, or 17.5%, higher than fiscal 2003. Of this increase, the net positive impact due to the change in foreign exchange rates was \$4.5 million, or 8.9%.

From a product perspective, the Company saw increases in its industrial, transmission and propulsion product sales, and after adjusting for the impact of the change in the TDN agreement, marine product sales were also higher. Of particular note in fiscal 2004 was the continued acceptance of our QuickShift® marine transmissions, the overall recovery of the marine pleasure craft market, the growth in our Arneson Surface Drives (propulsion) and 8500 series transmission for oilfield applications.

Gross Profit

Gross profit as a percentage of sales improved 610 basis points in fiscal 2004 to 25.6%, compared to 19.5% in fiscal 2003. The improvement in fiscal 2004 can be attributed to a number of factors: (1) increased sales and favorable product mix, which accounted for over half of the current year's improvement, (2) increased productivity and absorption, (3) lower fixed costs as a result of cost reduction initiatives, (4) favorable purchase price variances as a result of a material cost reduction program and (5) the absence in fiscal 2004 of a \$0.8 million SFAS 144 impairment charge taken in fiscal 2003. These were partially offset by a \$1 million increase in pension expense in fiscal 2004 compared to fiscal 2003.

Marketing, Engineering and Administrative (ME&A) Expenses

Marketing, engineering, and administrative (ME&A) expenses increased \$2.4 million, or 6.8%, in fiscal 2004 versus fiscal 2003. Over \$1.5 million, or 425 basis points, of this increase can be attributed to the unfavorable exchange rate impact of the weakening dollar on our overseas operations' ME&A expenses. Increased pension expense for salaried and administrative employees accounted for another \$0.8 million of the increase.

Restructuring

During the second quarter of 2003, the Company recorded a pre-tax restructuring charge of \$2.0 million in connection with the reduction of its workforce. These actions were taken in an effort to streamline the Company's cost structure and align its corporate workforce with market conditions. The charge consisted of employee termination and severance benefits for a total of 58 employees; 48 production employees and 10 salaried employees. During 2004 and 2003, the Company made cash payments of \$0.4 million and \$0.6 million, respectively. Accrued restructuring costs were \$0.9 million and \$1.3 million at June 30, 2004 and 2003, respectively.

Interest Expense

Interest expense decreased by \$250,000, or 19%, in fiscal 2004. The average outstanding debt for fiscal 2004 of \$20.4 million (computed monthly) was \$2.3 million lower than fiscal 2003. The decrease in interest expense for the fifth straight year can be attributed to overall lower debt levels and a lower weighted interest rate. The latter is partially due to the fact that the Company continues to pay down its Senior Notes, which carry a fixed rate of 7.37%, which is significantly higher than the interest rate on its other credit facilities.

Equity in Net Earnings of Affiliate

In January 2004, the Company sold its 25% minority interest in Palmer Johnson Distributors, LLC to the majority holder, PJD, Inc. for \$3,811,000 cash, which approximated the net book value of the investment. The Company recognized pre-tax earnings of \$240,000, \$414,000 and \$481,000 in fiscal years 2004, 2003 and 2002 respectively, from its investment in PJD. In addition, the Company received cash distributions of \$195,000, \$303,000 and \$400,000 in fiscal years 2004, 2003 and 2002, respectively.

Income Taxes

In fiscal 2004, the effective income tax rate was adversely impacted by the inability to utilize foreign tax credits and a relatively high proportion of foreign earnings. The low effective tax rate in fiscal 2003 results from the benefit of domestic losses partially offset by taxes incurred on foreign earnings, the inability to utilize foreign tax credits and a reduction in statutory rates at some foreign locations.

Management believes that it is more likely than not that the results of future operations will generate sufficient taxable income to realize deferred tax assets except for certain foreign tax credit carryforwards for which a valuation allowance has been recorded.

Order Rates

In fiscal 2004, we saw an improvement in our order rates for most of our products. As of fiscal year end, our manufacturing facilities in the United States, Belgium and Italy saw year-over-year increases in their six-month backlogs of 15.8%, 10.0% and 21.4%, respectively. The backlog of orders scheduled for shipment during the next six months (six-month backlog) of \$49.4 million at the end of fiscal 2004 compared favorably to the \$30.6 million for fiscal year end 2003. In June 2003, the Company announced that it had received an order to provide transmission systems for medium tactical vehicles to be supplied to Israeli Defense Forces. As of June 30, 2004, \$6.7 million of the six-month backlog related to this military contract. Prior to the over 60% improvement experienced this fiscal year, order rates for most of our products were down throughout much of the prior three fiscal years, contributing along with improved deliveries, to a steady decline in backlog. The year-over-year change in foreign exchange rates resulted in an approximately \$0.8 million increase in the backlog at June 30, 2004 versus June 30, 2003.

Other

On July 15, 2003, the Company announced a number of actions to address rising pension and retiree healthcare costs, meant to ensure both the future strength of our pension fund and the Company's ability to remain globally competitive. In addition to changes to both the pension and post-retirement healthcare plans (see Footnote P to the consolidated financial statements), the Company announced across-the-board wage reductions for corporate officers, and most domestic salaried and hourly employees. Domestic employee groups, including officers, also will forego performance bonuses in both fiscal 2003 and 2004. The 401(k) company match also has been reduced from 75 percent to 50 percent on the first six percent of employees' contributions. The combined effect of these actions approximately offset projected increases for both pension and post-retirement healthcare costs in fiscal 2004. In the first quarter of fiscal 2005, the Company will restore salary and wages to their prior levels and plans to implement a new incentive plan that emphasizes the achievement of earning returns in excess of the Company's cost of capital as well as other financial and non-financial objectives. It is estimated that the annual net pre-tax impact of the salary and wage restoration will be approximately \$0.7 million.

Fiscal 2003 Compared to Fiscal 2002*Net Sales*

Net sales increased less than one percent to \$179.6 million in fiscal 2003 from \$179.4 million in the prior fiscal year. As a result of the strong euro and Asian currencies versus the dollar, foreign currency exchange had a net favorable impact on sales of \$9.6 million in fiscal 2003, compared to fiscal 2002.

In fiscal 2003, our domestic operations experienced a decline in sales versus 2002 in all market segments except for Propulsion, which had a very strong year. After adjusting for the impact of foreign exchange rate changes, sales for overseas operations were slightly higher in fiscal 2003 compared to 2002. Overall, the Company's three major markets, marine, transmission and industrial products, all continued to be impacted by global economic conditions. However, the second half of the fiscal 2003 saw significant contributions from new-product introductions, such as our

high-performance QuickShift® marine transmissions and the 8500 series transmissions for oilfield applications, which supplemented improving core business strength. Our continuing ability to compete successfully for defense applications was underscored by the \$14.8 million contract for transmission systems announced in June 2003, augmenting recently awarded U.S. defense contracts for other land-based transmissions. Sales from this contract were first realized in late fiscal 2004.

For fiscal 2003, the Company's wholly-owned distribution companies posted a 9% improvement in sales, of which 6% can be attributed to the favorable impact of exchange rate fluctuations versus fiscal 2002. In particular, we saw strong sales for Arneson Surface Drives and the Italian Luxury Yacht industry weathered the pleasure craft downturn better than any other segment. Our distribution offices in Italy and the Pacific Rim continued to show strength in spite of weak global market conditions.

We had mixed results in our manufacturing operations in fiscal 2003. Our Italian operations posted another strong sales year versus fiscal 2002. However, the majority of the increase was caused by the strengthening euro. Although our Belgian operations got off to a slow start in fiscal 2003, the second half of the year saw some recovery as we began to produce and see the effects of our new QuickShift® marine transmissions. After adjusting for the impact of a strengthening euro in fiscal 2003, our Belgian operations posted a slight increase in sales, primarily driven by a very strong fourth quarter. In the U.S., our domestic operations were faced with a number of challenges early in fiscal 2003. In the first quarter, quality problems necessitated downtime in order to segregate non-conforming parts received from two of the Company's vendors. By the end of the second quarter, the disruption of production flow as a result of these vendor-supplied off-spec parts was normalized. In the second quarter, the Company announced restructuring actions that impacted both our U.S. and Belgian manufacturing operations (see Footnote S to the consolidated financial statements). These actions were taken in an effort to streamline the Company's cost structure and align its corporate workforce with market conditions. In addition to these challenges, the Company continued to be confronted with softness in many of its key markets. However, propulsion products continued to be a strong area for the Company in fiscal 2003.

Gross Profit

Gross profit as a percentage of sales deteriorated 290 basis points to 19.5% in fiscal 2003 compared to fiscal 2002. Almost half of the deterioration can be attributed to increased pension and medical costs of nearly \$1.6 million, and a \$0.8 million impairment charge taken in the second quarter (see Footnote F to the consolidated financial statements). The remaining deterioration was due to unfavorable volume and mix in fiscal 2003 as well as supplier quality issues the Company experienced in the first and second quarters of fiscal 2003. The latter was somewhat offset by ongoing productivity and cost improvement initiatives in our manufacturing operations. Despite early setbacks caused by the supplier quality issues and restructuring actions taken in the first half of 2003, the second half of the year was much stronger. For example, fourth quarter gross profit as a percentage of sales of 22.7% compared favorably with fiscal 2002 at 22.9%.

Marketing, Engineering and Administrative (ME&A) Expenses

In fiscal 2003, marketing, engineering, and administrative (ME&A) expenses remained flat versus the prior year, in spite of an almost \$1.4 million increase attributable to the unfavorable exchange rate impact of the weakening dollar on our overseas operations. This was achievable primarily as a result of ongoing cost reduction initiatives, including the restructuring actions announced in the 2nd quarter. For fiscal 2003, total engineering related expenses were approximately \$1 million higher than the prior year as the Company continued to invest in engineering projects related to the development of new marine, industrial, surface drive and electronic control products. This increase was more than offset by reductions in marketing and administrative expenses, even with the negative foreign exchange impact. Approximately one-half of the \$2.9 million increase in fiscal 2002 spending was due to the first-year expenses of NTC, and the balance consisted of added marketing and engineering expenses related to a new product introduction.

Restructuring

During the second quarter of 2003, the Company recorded a pre-tax restructuring charge of \$2.0 million in connection with the reduction of its workforce. These actions were taken in an effort to streamline the Company's cost structure and align its corporate workforce with market conditions. The charge consisted of employee termination and severance benefits for a total of 58 employees; 48 production employees and 10 salaried employees. During 2003, the Company made cash payments of \$0.6 million. Accrued restructuring costs were \$1.3 million at June 30, 2003.

Interest Expense

Interest expense declined for the fourth straight year in fiscal 2003 as debt was further reduced by \$2 million, excluding the impact of foreign exchange, and the company continued to pay down its senior notes, which carry a significantly higher interest rate than its revolver facility.

Income Taxes

The low effective tax rate in fiscal 2003 results from the benefit of domestic losses partially offset by taxes incurred on foreign earnings, the inability to utilize foreign tax credits and a reduction in statutory rates at some foreign locations. In fiscal year 2002, limitations on foreign tax credit utilization, the relatively high proportion of foreign earnings and settlement of some state tax issues resulted in an unusually high tax rate. The effective rate in fiscal 2002 was increased further by two third-quarter adjustments totaling about \$300,000. Also in fiscal 2002, a tax incentive provided by the Belgian government several years ago was disallowed by the European Commission and was refunded to the government, and the United States tax provision was adjusted upward for the taxes due on an asset sale gain recorded in the prior year's third quarter. Statutory rate changes at European operations reduced taxes in 2003 by approximately \$100,000.

Management believes that it is more likely than not that the results of future operations will generate sufficient taxable income to realize deferred tax assets except for certain foreign tax credit carryforwards for which a valuation allowance has been recorded.

Order Rates

Order rates for most of our products were down throughout much of fiscal 2003 and 2002, contributing along with improved deliveries, to a steady decline in backlog. The backlog of orders scheduled for shipment during the next six months (six-month backlog) remained relatively flat at \$31 million at the end of fiscal 2003. However, the year-over-year change in foreign exchange rates resulted in an approximately \$2.1 million increase in the backlog at June 30, 2003 versus June 30, 2002. The year-over-year change in foreign exchange rates resulted in an approximately \$1.0 million increase in the backlog at June 30, 2002 versus June 30, 2001.

Liquidity and Capital Resources

Fiscal Years 2004, 2003 and 2002

The net cash provided by operating activities in fiscal 2004 totaled \$12.2 million versus \$6.7 million in fiscal 2003, for a net increase of \$5.5 million. This increase was primarily driven by an increase in net earnings of \$7.6 million over fiscal 2003's net loss. This was partially offset by increased inventories at our domestic manufacturing location as we prepared to deliver transmission systems for military contracts. Accounts receivable at June 30, 2004 were approximately \$0.6 million lower, adjusted for the impact of exchange rate changes, than at June 30, 2003. The change in the TDN agreement previously discussed resulted in a net reduction in accounts receivable of \$3.6 million. This was offset by increased accounts receivable of \$3.9 million at our domestic manufacturing location, driven by increased sales in fiscal 2004's fourth quarter of over \$7 million versus the prior fiscal year's fourth quarter. The change in the TDN agreement also resulted in a net reduction in accounts payable of \$3.8 million. This was partially offset by a net increase of \$3.0 million in accounts payable at our domestic manufacturing location due to the increased sales activity noted above.

The net cash provided by operating activities in fiscal 2003 totaled \$6.7 million versus \$13.2 million in fiscal 2002. This decline was primarily driven by the net loss experienced in fiscal 2003. In addition, the net change in operating assets and liabilities contributed \$2.8 million to operating cash flow in fiscal 2003, compared to nearly \$5 million in the prior year. While the continued reduction of inventories contributed \$3.7 million to operating cash flow in both 2003 and 2002, accounts receivable at June 30, 2003 were approximately \$3.0 million higher, adjusted for the impact of exchange rate changes, than at June 30, 2002. While fourth quarter sales were flat year-over-year, there was a significant shift from domestic to overseas sales in fiscal 2003's fourth quarter. In general, customer credit terms in both our European and Asian markets are longer, partially explaining this increase. Additionally, our domestic operations had a past due balance of \$0.6 million from one overseas customer, of which \$0.5 million had been collected subsequent to year-end.

The net cash used for investing activities in fiscal 2004 consisted of the net acquisition price for Rolla SP Propellers SA for \$5.1 million, net of \$1.2 million cash acquired, and nearly \$4.2 million in investments in capital equipment offset by the net proceeds from the sale of the Company's 25% minority interest in PJD, Inc. to the majority holder for \$3.8 million.

With the acquisition of Rolla SP Propellers SA in Balerna, Switzerland in May 2004, the Company is in the process of constructing a new state-of-the-art facility for the design and manufacturing of high-performance, custom propellers. As a result, management expects capital expenditures in fiscal 2005 to significantly exceed recent years, reversing a trend of below depreciation capital spending.

In fiscal 2003 and 2002, the net cash used for investing activities consisted primarily of capital expenditures at our domestic and European manufacturing locations.

In fiscal 2004, 2003 and 2002, the net cash flow used by financing activities consisted primarily of dividends paid to shareholders of \$2.0 million and the repayment of long-term debt. In each fiscal year, the Company repaid \$2.9 million of its 7.37% Senior Notes due 2006. The net payments/proceeds from long-term debt were payments or borrowings on the Company's revolving credit facility.

Future Liquidity and Capital Resources

Twin Disc has a three-year \$20 million revolving credit facility that expires in October 2005. This credit facility is used to fund seasonal working capital requirements and other financing needs. This facility and Twin Disc's other indebtedness contain certain restrictive covenants as are fully disclosed in Note J of the Notes to the Consolidated Financial Statements. Twin Disc is currently renegotiating its revolving credit agreement and plans to have a new agreement negotiated by the end of fiscal 2005's first quarter. At this time, we do not foresee any difficulties in securing an extension as well as an increase in the available borrowings under the agreement.

The overall liquidity of the Company remains strong. We continue to reduce total borrowings, have over \$7.2 million of available borrowings on our \$20 million revolving loan agreement, and continue to generate enough cash from operations to meet our operating and investing needs. In fiscal 2005, the Company expects to contribute \$7.5 million to its pension plans, an increase of nearly \$3 million over fiscal 2004. The Company intends to meet this funding requirement from cash from operations and, if necessary, from available borrowings under existing credit facilities. Working capital increased \$5 million to about \$56 million in fiscal 2004, and the current ratio has been unchanged at between 2.1 and 2.2 for the past four fiscal years. The Company's balance sheet is strong, there are no off-balance sheet arrangements, and we continue to have sufficient liquidity for near-term needs.

Twin Disc expects capital expenditures to be up to \$10 million in fiscal 2005, partially reflecting the impact of the cost of a new facility under construction in Switzerland noted above. These anticipated expenditures reflect our plans to continue to reinvest in modern equipment and facilities, and new products.

Management believes that available cash, the credit facility, cash generated from future operations, existing lines of credit and access to debt markets will be adequate to fund Twin Disc's capital requirements for the foreseeable future.

Off Balance Sheet Arrangements and Contractual Obligations

The Company had no off-balance sheet arrangements, guarantees or obligations except for normal open purchase orders and operating leases as of June 30, 2004 and 2003. Obligations for operating leases are listed in the table below.

The Company has obligations under non-cancelable operating lease contracts and loan and senior note agreements for certain future payments. A summary of those commitments follows (in thousands):

Contractual obligations	Total	Less than 1 Year	1-3 Years	4-5 Years	After 5 Years
Short-term debt	\$ 1,607	\$1,607	—	—	—
Revolving loan borrowing	\$12,800	—	\$12,800	—	—
Long-term debt	\$ 7,031	\$3,018	\$ 4,013	—	—
Operation leases	\$10,285	\$2,700	\$ 3,711	\$2,404	\$1,470

The Company believes the capital resources available in the form of existing cash, lines of credit (see Footnote J to the consolidated financial statements), and funds provided by operations will be adequate to meet anticipated capital expenditures and other foreseeable future business requirements, including pension funding requirements. As noted above, the Company is currently in discussions to increase the borrowings available under and extend its \$20,000,000 revolving loan agreement, which expires on October 31, 2005. Management expects to have the amended agreement finalized before the end of fiscal 2005's first quarter.

Other Matters

Environmental Matters

The Company has been involved in various stages of investigation relative to hazardous waste sites, two of which were on the United States EPA National Priorities List (Superfund sites). The Company's involvement in one of the Superfund sites was settled in 2003 for approximately \$191,000. The Company has made a \$117,000 payment in trust in settlement of its exposure related to the second Superfund site and anticipates that no further payments will be required. The excess reserve for these sites of \$300,000 was reversed against cost of sales in 2003.

Critical Accounting Policies

The preparation of this Annual Report requires management's judgment to make estimates and assumptions that affect the reported amounts of assets and liabilities, disclosure of contingent assets and liabilities at the dates of the financial statements, and the reported amounts of revenues and expenses during the reporting period. There can be no assurance that actual results will not differ from those estimates.

Twin Disc's significant accounting policies are described in Note A to the consolidated financial statements on pages 22 through 23 of this form. Not all of these significant accounting policies require management to make difficult, subjective, or complex judgments or estimates. However, the policies management considers most critical to understanding and evaluating our reported financial results are the following:

Revenue Recognition

Twin Disc recognizes revenue from product sales at the time of shipment and passage of title. While we respect the customer's right to return products that were shipped in error or do not function properly, historical experience shows those types of adjustments have been immaterial and thus no provision is made. With respect to other revenue recognition issues, management has concluded that its policies are appropriate and in accordance with the guidance provided by Securities and Exchange Commissions' Staff Accounting Bulletin (SAB) No. 104, "Revenue Recognition."

Accounts Receivable

Twin Disc performs ongoing credit evaluations of our customers and adjusts credit limits based on payment history and the customer's credit-worthiness as determined by review of current credit information. We continuously monitor collections and payments from our customers and maintain a provision for estimated credit losses based upon our historical experience and any specific customer-collection issues. In addition, senior management reviews the accounts receivable aging on a monthly basis to determine if any receivable balances may be uncollectible. Although our accounts receivable are dispersed among a large customer base, a significant change in the liquidity or financial position of any one of our largest customers could have a material adverse impact on the collectibility of our accounts receivable and future operating results.

Inventory

Inventories are valued at the lower of cost or market. Cost has been determined by the last-in, first-out (LIFO) method for the majority of the inventories located in the United States, and by the first-in, first-out (FIFO) method for all other inventories. Management specifically identifies obsolete products and analyzes historical usage, forecasted production based on future orders, demand forecasts, and economic trends when evaluating the adequacy of the reserve for excess and obsolete inventory. The adjustments to the reserve are estimates that could vary significantly, either favorably or unfavorably, from the actual requirements if future economic conditions, customer demand or competitive conditions differ from expectations.

Warranty

Twin Disc engages in extensive product quality programs and processes, including actively monitoring and evaluating the quality of its suppliers. However, its warranty obligation is affected by product failure rates, the extent of the market affected by the failure and the expense involved in satisfactorily addressing the situation. The warranty reserve is established based on our best estimate of the amounts necessary to settle future and existing claims on products sold as of the balance sheet date. When evaluating the adequacy of the reserve for warranty costs, management takes into consideration the term of the warranty coverage, historical claim rates and costs of repair, knowledge of the type and volume of new products and economic trends. While we believe the warranty reserve is adequate and that the judgment applied is appropriate, such amounts estimated to be due and payable in the future could differ materially from what actually transpires.

Income Taxes

As part of the process of preparing our consolidated financial statements, income taxes in each of the jurisdictions in which we operate must be estimated. This process involves estimating the actual current tax exposure and assessing the realizability of deferred tax assets. If it is deemed more likely than not that a deferred tax asset will not be realized, a valuation allowance is recorded.

ITEM 7(a). QUANTITATIVE AND QUALITATIVE DISCLOSURE ABOUT MARKET RISK

The Company is exposed to market risks from changes in interest rates, commodities and foreign exchange. To reduce such risks, the Company selectively uses financial instruments and other pro-active management techniques. All hedging transactions are authorized and executed pursuant to clearly defined policies and procedures, which prohibit the use of financial instruments for trading or speculative purposes. Discussions of the Company's accounting policies and further disclosure relating to financial instruments is included in Note A to the consolidated financial statements on pages 22 through 23 of this form.

Interest rate risk – The Company's earnings exposure related to adverse movements of interest rates is primarily derived from outstanding floating rate debt instruments that are indexed to the prime and LIBOR interest rates. During fiscal 2003, the Company entered into a \$20,000,000 revolving loan agreement, which expires on October 31, 2005. In accordance with the loan agreement, the Company has the option of borrowing at the prime interest rate or LIBOR plus an additional "Add-On", between 1% and 2.75%, depending on the Company's Total Funded Debt to EBITDA ratio. Due to the relative stability of interest rates, the Company did not utilize any financial instruments at June 30, 2004 to manage interest rate risk exposure. A 10 percent increase or decrease in the applicable interest rate would result in a change in pretax interest expense of approximately \$30,000.

Commodity price risk – The Company is exposed to fluctuation in market prices for such commodities as steel and aluminum. The Company does not utilize commodity price hedges to manage commodity price risk exposure.

Currency risk – The Company has exposure to foreign currency exchange fluctuations. Approximately one-third of the Company's revenues in the years ended June 30, 2004, 2003 and 2002 were denominated in currencies other than the U.S. dollar. Of that total, approximately two-thirds was denominated in euros with the balance composed of Japanese yen and the Australian and Singapore dollars. The Company does not hedge the translation exposure represented by the net assets of its foreign subsidiaries. Foreign currency translation adjustments are recorded as a component of shareholders' equity. Forward foreign exchange contracts are used to hedge the currency fluctuations on significant transactions denominated in foreign currencies.

Derivative Financial Instruments – The Company has written policies and procedures that place all financial instruments under the direction of the Company corporate treasury and restrict derivative transactions to those intended for hedging purposes. The use of financial instruments for trading purposes is prohibited. The Company uses financial instruments to manage the market risk from changes in foreign exchange rates.

The Company primarily enters into forward exchange contracts to reduce the earnings and cash flow impact of non-functional currency denominated receivables and payables. These contracts are highly effective in hedging the cash flows attributable to changes in currency exchange rates. Gains and losses resulting from these contracts offset the foreign exchange gains or losses on the underlying assets and liabilities being hedged. The maturities of the forward exchange contracts generally coincide with the settlement dates of the related transactions. Gains and losses on these contracts are recorded in Other Income (Expense), net in the Consolidated Statement of Operations as the changes in the fair value of the contracts are recognized and generally offset the gains and losses on the hedged items in the same period. The primary currency to which the Company was exposed in 2004, 2003 and 2002 was the euro. At June 30, 2004, the Company had net outstanding forward exchange contracts to purchase euros in the value of \$2,901,000 with a weighted average maturity of 45 days. The fair value of the Company's contracts was a loss of approximately \$58,000 at June 30, 2004. At June 30, 2003, the Company had net outstanding forward exchange contracts to purchase euros in the value of \$2,701,000 with a weighted average maturity of 50 days. The fair value of the Company's contracts was approximately zero at June 30, 2003.

ITEM 8. FINANCIAL STATEMENTS AND SUPPLEMENTARY DATA

See Consolidated Financial Statements and Financial Statement Schedule on Pages 16 through 40 of this form.

Sales and Earnings by Quarter (dollars in thousands, except per share amounts)

2004	1st Qtr.	2nd Qtr.	3rd Qtr.	4th Qtr.	Year
Net sales	\$37,966	\$42,371	\$48,606	\$57,146	\$186,089
Gross profit	8,896	10,721	12,917	15,096	47,630
Net earnings	171	508	1,776	2,788	5,243
Basic earnings per share . . . . .	.06	.18	.63	.99	1.86
Diluted earnings per share . . . . .	.06	.18	.62	.97	1.84
Dividends per share . . . . .	.175	.175	.175	.175	.70
2003	1st Qtr.	2nd Qtr.	3rd Qtr.	4th Qtr.	Year
Net sales	\$36,521	\$42,794	\$47,177	\$53,099	\$179,591
Gross profit	5,930	6,680	10,425	11,981	35,016
Net earnings (loss)	(1,731)	(3,087)	509	1,941	(2,368)
Basic earnings (loss) per share	(.62)	(1.10)	.18	.70	(.84)
Diluted earnings (loss) per share	(.62)	(1.10)	.18	.70	(.84)
Dividends per share . . . . .	.175	.175	.175	.175	.70

ITEM 9. CHANGE IN AND DISAGREEMENTS WITH ACCOUNTANTS ON ACCOUNTING AND FINANCIAL DISCLOSURE

None.

ITEM 9(a). CONTROLS AND PROCEDURES

(a) Evaluation of Disclosure Controls and Procedures.

As required by Rules 13a-15 and 15d-15 of the Securities Exchange Act of 1934, as of the end of the period covered by this report and under the supervision and with the participation of management, including the Chief Executive Officer and the Chief Financial Officer, the Company has evaluated the effectiveness of the design and operation of its disclosure controls and procedures. Based on such evaluation, the Chief Executive Officer and Chief Financial Officer have concluded that such disclosure controls and procedures are effective in ensuring that material information relating to the Company, including its consolidated subsidiaries, is made known to the certifying officers by others within the Company and its consolidated subsidiaries during the period covered by this report.

(b) Changes in Internal Controls.

There were no changes in the Company's internal controls for financial reporting or other factors during the fourth quarter of the most recent fiscal year that could significantly affect such internal controls. However, in connection with the new rules, the Company has been engaged in the process of further reviewing and documenting its disclosure controls and procedures, including its internal accounting controls. The Company may from time to time make changes aimed at enhancing the effectiveness of its disclosure controls and procedures, including its internal controls, to ensure that the Company's systems evolve with its business.

ITEM 10. DIRECTORS AND EXECUTIVE OFFICERS OF THE REGISTRANT

For information with respect to the executive officers of the Registrant, see "Executive Officers of the Registrant" at the end of Part I of this report.

For information with respect to the Directors of the Registrant, see "Election of Directors" in the Proxy Statement for the Annual Meeting of Shareholders to be held October 15, 2004, which is incorporated into this report by reference.

For information with respect to compliance with Section 16(a) of the Securities Exchange Act of 1934, see "Section 16(a) Beneficial Ownership Reporting Compliance" in the Proxy Statement for the Annual Meeting of Shareholders to be held October 15, 2004, which is incorporated into this report by reference.

For information with respect to the Company's Code of Ethics, see "Code of Ethics" in the Proxy Statement for the Annual Meeting of Shareholders to be held October 15, 2004, which is incorporated into this report by reference. The Company's Code of Ethics, entitled, "Guidelines for Business Conduct and Ethics," is included on the Company's website, www.twindisc.com.

For information with respect to changes to procedures by which shareholders may recommend nominees to the Company's Board of Directors, see "Selection of Nominees for the Board" in the Proxy Statement for the Annual Meeting of Shareholders to be held October 15, 2004, which is incorporated into this report by reference.

For information with respect to the Audit Committee Financial Expert, see "Roles of the Board's Committees: Audit Committee" in the Proxy Statement for the Annual Meeting of Shareholders to be held October 15, 2004, which is incorporated into this report by reference.

For information with respect to the Audit Committee Disclosure, see "Roles of the Board's Committees: Audit Committee" in the Proxy Statement for the Annual Meeting of Shareholders to be held October 15, 2004, which is incorporated into this report by reference.

ITEM 11. EXECUTIVE COMPENSATION

The information set forth under the captions "Compensation of Executive Officers", "Stock Options", "Retirement Income Plan", "Supplemental Retirement Benefit Plan", "Compensation of Directors" and "Employment Contracts" in the Proxy Statement for the Annual Meeting of Shareholders to be held on October 15, 2004 is incorporated into this report by reference. Discussion in the Proxy Statement under the captions "Board Compensation Committee Report on Executive Compensation" and "Corporate Performance Graph" is incorporated by reference but shall not be deemed "soliciting material" or to be "filed" as part of this report.

ITEM 12. SECURITY OWNERSHIP OF CERTAIN BENEFICIAL OWNERS AND MANAGEMENT

Security ownership of certain beneficial owners and management is set forth in the Proxy Statement for the Annual Meeting of Shareholders to be held on October 15, 2004 under the caption "Principal Shareholders, Directors and Executive Officers" and incorporated into this report by reference.

There are no arrangements known to the Registrant, the operation of which may at a subsequent date result in a change in control of the Registrant.

The following table summarizes certain information regarding the Company's equity-based compensation plans:

Plan category	# of securities to be issued upon exercise of outstanding options, warrants and rights	Weighted average price of outstanding options, warrants and rights	# of securities remaining available for future issuance under equity compensation plans
Equity Compensation Plans Approved by Shareholders	188,200	\$19.69	\$24,250
Equity Compensation Plans Not Approved by Shareholders	0	n/a	0
Total	<u>188,200</u>	<u>\$19.69</u>	<u>\$24,250</u>

ITEM 13. CERTAIN RELATIONSHIPS AND RELATED TRANSACTIONS

None.

ITEM 14. PRINCIPAL ACCOUNTING FEES AND SERVICES

The Company incorporates by reference the information contained in the Company's definitive Proxy Statement dated October 15, 2004 under the heading "Fees to Independent Registered Public Accounting Firm."

ITEM 15. Exhibits, Financial Statement Schedules and Reports on Form 8-K

(a)(1) Consolidated Financial Statements

See "Index to Consolidated Financial Statements and Financial Statement Schedule" on page 16, the Report of Independent Registered Public Accounting Firm on page 17 and the Consolidated Financial Statements on pages 18 to 39, all of which are incorporated by reference.

Individual financial statements of the 50% or less owned entities accounted for by the equity method are not required because the 50% or less owned entities do not constitute significant subsidiaries.

(a)(2) Consolidated Financial Statement Schedules

See "Index to Consolidated Financial Statements and Financial Statement Schedule" on page 16, the Consolidated Financial Statement Schedule on page 40 is incorporated by reference.

(a)(3) Exhibits. See Exhibit Index included as the last page of this form, which is incorporated by reference.

Copies of exhibits filed as a part of this Annual Report on Form 10-K may be obtained by shareholders of record upon written request directed to the Secretary, Twin Disc, Incorporated, 1328 Racine Street, Racine, Wisconsin 53403.

(b) A Form 8-K was filed on April 16, 2004 announcing the financial results for the third fiscal quarter of 2004.

INDEX TO CONSOLIDATED FINANCIAL STATEMENTS AND FINANCIAL STATEMENT SCHEDULE

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Schedules, other than those listed, are omitted for the reason that they are inapplicable, are not required, or the information required is shown in the financial statements or the related notes.

REPORT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

To the Shareholders of
Twin Disc, Incorporated:

In our opinion, the consolidated financial statements listed in the index appearing under Item 15(a)(1) present fairly, in all material respects, the financial position of Twin Disc, Incorporated and Subsidiaries at June 30, 2004 and 2003, and the results of their operations and their cash flows for each of the three years in the period ended June 30, 2004 in conformity with accounting principles generally accepted in the United States of America. In addition, in our opinion, the financial statement schedule listed in the index appearing under Item 15(a)(2) present fairly, in all material respects, the information set forth therein when read in conjunction with the related consolidated financial statements. These financial statements and the financial statement schedule are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements and financial statement schedule based on our audits. We conducted our audits of these statements in accordance with the standards of the Public Company Accounting Oversight Board (United States). Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.



PricewaterhouseCoopers LLP

Milwaukee, Wisconsin
July 30, 2004

FINANCIALS

TWIN DISC, INCORPORATED AND SUBSIDIARIES CONSOLIDATED BALANCE SHEETS

JUNE 30, 2004 and 2003

(Dollars in thousands)	<u>2004</u>	<u>2003</u>
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 9,127	\$ 5,908
Trade accounts receivable, net	37,091	35,367
Inventories, net	52,079	47,247
Deferred income taxes	4,216	4,469
Other	3,111	4,104
Total current assets	105,624	97,095
Property, plant and equipment, net	33,222	30,210
Investment in affiliate	—	2,550
Goodwill, net	12,717	12,876
Deferred income taxes	15,668	20,164
Intangible pension asset	—	24
Other assets	9,406	7,439
	\$176,637	\$170,358
LIABILITIES and SHAREHOLDERS' EQUITY		
Current liabilities:		
Notes payable	\$ 1,607	\$ 2,429
Current maturities on long-term debt	3,018	2,857
Accounts payable	17,241	16,115
Accrued liabilities	27,262	24,885
Total current liabilities	49,128	46,286
Long-term debt	16,813	16,584
Accrued retirement benefits	49,456	56,732
	115,397	119,602
Minority interest	509	485
Shareholders' equity:		
Preferred shares authorized: 200,000; issued: none; no par value	—	—
Common shares authorized: 15,000,000; issued: 3,643,630; no par value	11,653	11,653
Retained earnings	86,443	83,191
Unearned compensation	(304)	—
Accumulated other comprehensive loss	(20,301)	(26,978)
	77,491	67,866
Less treasury stock, at cost	16,760	17,595
Total shareholders' equity	60,731	50,271
	\$176,637	\$170,358

The notes to consolidated financial statements are an integral part of these statements.

TWIN DISC, INC.

TWIN DISC, INCORPORATED and SUBSIDIARIES CONSOLIDATED STATEMENTS OF OPERATIONS

for the years ended June 30, 2004, 2003 and 2002

(In thousands, except per share data)	<u>2004</u>	<u>2003</u>	<u>2002</u>
Net sales	\$186,089	\$179,591	\$179,385
Cost of goods sold	138,459	144,575	139,146
Gross profit	47,630	35,016	40,239
Marketing, engineering and administrative expenses	37,168	34,790	34,638
Restructuring of operations	—	2,042	—
Earnings (loss) from operations	10,462	(1,816)	5,601
Other income (expense):			
Interest income	252	167	294
Interest expense	(1,078)	(1,323)	(1,700)
Equity in net earnings of affiliate	240	414	481
Other, net	101	(81)	467
	<u>(485)</u>	<u>(823)</u>	<u>(458)</u>
Earnings (loss) before income taxes and minority interest	9,977	(2,639)	5,143
Income taxes	4,709	(283)	2,950
Earnings (loss) before minority interest	5,268	(2,356)	2,193
Minority interest	(25)	(12)	(135)
Net earnings (loss)	<u>\$ 5,243</u>	<u>\$ (2,368)</u>	<u>\$ 2,058</u>
Earnings (loss) per share data:			
Basic earnings (loss) per share	\$ 1.86	\$ (0.84)	\$ 0.73
Diluted earnings (loss) per share	1.84	(0.84)	0.73
Weighted average shares outstanding data:			
Basic shares outstanding	2,814	2,805	2,808
Dilutive stock options	29	—	—
Diluted shares outstanding	<u>2,843</u>	<u>2,805</u>	<u>2,808</u>

The notes to consolidated financial statements are an integral part of these statements.

FINANCIALS

TWIN DISC, INCORPORATED and SUBSIDIARIES CONSOLIDATED STATEMENTS OF CASH FLOWS

for the years ended June 30, 2004, 2003 and 2002

(In thousands)	<u>2004</u>	<u>2003</u>	<u>2002</u>
Cash flows from operating activities:			
Net earnings (loss)	\$ 5,243	\$ (2,368)	\$ 2,058
Adjustments to reconcile net earnings (loss) to net cash provided by operating activities:			
Depreciation and amortization	5,692	5,673	5,709
Write-off of impaired asset	—	773	—
Loss on sale of plant assets	55	105	90
Minority interest	25	12	135
(Gain) loss on restructuring of operations	—	1,278	(53)
Unearned compensation	188	—	—
Equity in net earnings of affiliate	(240)	(414)	(481)
Provision for deferred income taxes	1,312	(1,424)	378
Dividends received from affiliate	195	303	400
Changes in operating assets and liabilities			
Trade accounts receivable, net	622	(2,977)	(995)
Inventories, net	(2,575)	3,725	3,724
Other assets	940	(1,193)	67
Accounts payable	(377)	1,489	2,456
Accrued liabilities	427	577	(3,702)
Accrued/prepaid retirement benefits	733	1,151	3,375
Net cash provided by operating activities	<u>12,240</u>	<u>6,710</u>	<u>13,161</u>
Cash flows from investing activities:			
Proceeds from sale of plant assets	1	20	25
Proceeds from sale of affiliate	3,811	—	—
Acquisitions of plant assets	(4,180)	(4,410)	(2,063)
Acquisition of affiliate, net of cash acquired	(5,085)	—	—
Net cash used by investing activities	<u>(5,453)</u>	<u>(4,390)</u>	<u>(2,038)</u>
Cash flows from financing activities:			
Decreases in notes payable, net	(1,382)	(23)	(3,082)
Payments of long-term debt	(922)	(1,992)	(4,857)
Proceeds from exercise of stock options	343	—	—
Acquisition of treasury stock	—	(114)	—
Dividends paid	(1,991)	(1,965)	(1,965)
Net cash used by financing activities	<u>(3,952)</u>	<u>(4,094)</u>	<u>(9,904)</u>
Effect of exchange rate changes on cash	384	282	220
Net change in cash and cash equivalents	3,219	(1,492)	1,439
Cash and cash equivalents:			
Beginning of year	5,908	7,400	5,961
End of year	<u>\$ 9,127</u>	<u>\$ 5,908</u>	<u>\$ 7,400</u>
Supplemental cash flow information:			
Cash paid during the year for:			
Interest	\$ 1,563	\$ 1,870	\$ 1,882
Income taxes	2,127	1,675	1,908

The notes to consolidated financial statements are an integral part of these statements.

**TWIN DISC, INCORPORATED and SUBSIDIARIES
CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
AND COMPREHENSIVE INCOME**

for the years ended June 30, 2004, 2003 and 2002

(In thousands)	<u>2004</u>	<u>2003</u>	<u>2002</u>
Common stock			
Balance, June 30	\$ 11,653	\$ 11,653	\$ 11,653
Retained earnings			
Balance, July 1	83,191	87,524	87,431
Net earnings (loss)	5,243	(2,368)	2,058
Cash dividends	(1,991)	(1,965)	(1,965)
Balance, June 30	<u>86,443</u>	<u>83,191</u>	<u>87,524</u>
Accumulated other comprehensive loss			
Balance, July 1	(26,978)	(23,187)	(23,181)
Foreign currency translation adjustment			
Balance, July 1	4,409	(1,520)	(5,420)
Current adjustment	2,480	5,929	3,900
Balance, June 30	<u>6,889</u>	<u>4,409</u>	<u>(1,520)</u>
Minimum pension liability adjustment, net			
Balance, July 1	(31,387)	(21,667)	(17,761)
Current adjustment, net of related income taxes [(\$2,683) in 2004 \$6,215 in 2003, and \$2,497 in 2002]	4,197	(9,720)	(3,906)
Balance, June 30	<u>(27,190)</u>	<u>(31,387)</u>	<u>(21,667)</u>
Accumulated other comprehensive loss Balance, June 30	<u>(20,301)</u>	<u>(26,978)</u>	<u>(23,187)</u>
Treasury stock, at cost			
Balance, July 1	(17,595)	(17,481)	(17,481)
Shares issued (acquired)	531	(114)	—
Balance, June 30	<u>(17,064)</u>	<u>(17,595)</u>	<u>(17,481)</u>
Shareholders' equity balance, June 30	<u>\$ 60,731</u>	<u>\$ 50,271</u>	<u>\$ 58,509</u>
Comprehensive income (loss)			
Net earnings (loss)	\$ 5,243	\$ (2,368)	\$ 2,058
Other comprehensive income (loss)			
Foreign currency translation adjustment	2,480	5,929	3,900
Minimum pension liability adjustment, net	4,197	(9,720)	(3,906)
Other comprehensive income (loss)	<u>6,677</u>	<u>(3,791)</u>	<u>(6)</u>
Comprehensive income (loss)	<u>\$ 11,920</u>	<u>\$ (6,159)</u>	<u>\$ 2,052</u>

The notes to consolidated financial statements are an integral part of these statements.

**TWIN DISC, INCORPORATED AND SUBSIDIARIES
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS****A. SIGNIFICANT ACCOUNTING POLICIES**

The following is a summary of the significant accounting policies followed in the preparation of these financial statements:

Consolidation Principles — The consolidated financial statements include the accounts of Twin Disc, Incorporated and its wholly and partially owned domestic and foreign subsidiaries. Certain foreign subsidiaries are included based on fiscal years ending March 31 or May 31, to facilitate prompt reporting of consolidated accounts. All significant intercompany transactions have been eliminated.

Translation of Foreign Currencies — The financial statements of the Company's non-U.S. subsidiaries are translated using the current exchange rate for assets and liabilities and the weighted average exchange rate for the year for revenues and expenses. Foreign currency translation adjustments are recorded as a component of shareholders' equity. Gains and losses from foreign currency transactions are included in earnings. Included in other income (expense) are foreign currency transaction losses (gains) of \$73,000, \$123,000 and \$(170,000) in 2004, 2003 and 2002, respectively.

Cash Equivalents — The Company considers all highly liquid marketable securities purchased with a maturity date of three months or less to be cash equivalents.

Receivables — Trade accounts receivable are stated net of an allowance for doubtful accounts of \$604,000 and \$502,000 at June 30, 2004 and 2003, respectively.

Fair Value of Financial Instruments — The carrying amount reported in the consolidated balance sheets for cash and cash equivalents, accounts receivable, accounts payable and notes payable approximate fair value because of the immediate short-term maturity of these financial instruments. The fair value of long-term debt exceeds its carrying amount by \$252,000 and \$438,000 at June 30, 2004 and 2003, respectively, based on the current rates that would be offered to the Company for debt with the same remaining maturity.

Derivative Financial Instruments — The Company has written policies and procedures that place all financial instruments under the direction of the Company's corporate treasury and restrict all derivative transactions to those intended for hedging purposes. The use of financial instruments for trading purposes is prohibited. The Company uses financial instruments to manage the market risk from changes in foreign exchange rates.

The Company primarily enters into forward exchange contracts to reduce the earnings and cash flow impact of non-functional currency denominated receivables and payables. These contracts are highly effective in hedging the cash flows attributable to changes in currency exchange rates. Gains and losses resulting from these contracts offset the foreign exchange gains or losses on the underlying assets and liabilities being hedged. The maturities of the forward exchange contracts generally coincide with the settlement dates of the related transactions. Gains and losses on these contracts are recorded in other income (expense), net as the changes in the fair value of the contracts are recognized and generally offset the gains and losses on the hedged items in the same period. The primary currency to which the Company was exposed in 2004, 2003 and 2002 was the euro. At June 30, 2004, the Company had net outstanding forward exchange contracts to purchase euros in the value of \$2,901,000 with a weighted average maturity of 45 days. The fair value of the Company's contracts was a loss of approximately \$58,000 at June 30, 2004. At June 30, 2003, the Company had net outstanding forward exchange contracts to purchase euros in the value of \$2,701,000 with a weighted average maturity of 50 days. The fair value of the Company's contracts was approximately zero at June 30, 2003.

Inventories — Inventories are valued at the lower of cost or market. Cost has been determined by the last-in, first-out (LIFO) method for the majority of inventories located in the United States, and by the first-in, first-out (FIFO) method for all other inventories.

Property, Plant and Equipment and Depreciation — Assets are stated at cost. Expenditures for maintenance, repairs and minor renewals are charged against earnings as incurred. Expenditures for major renewals and betterments are capitalized and depreciated. Depreciation is provided on the straight-line method over the estimated useful lives of the assets for financial reporting and on accelerated methods for income tax purposes. The lives assigned to buildings and related improvements range from 10 to 40 years, and the lives assigned to machinery and equipment range from 5 to 15 years. Upon disposal of property, plant and equipment, the cost of the asset and the related accumulated depreciation are removed from the accounts and the resulting gain or loss is reflected in earnings. Fully depreciated assets are not removed from the accounts until physically disposed.

Impairment of Long-lived Assets — The Company reviews long-lived assets for impairment whenever events or changes in business circumstances indicate that the carrying amount of the assets may not be fully recoverable in accordance with the Statement of Financial Accounting Standards ("SFAS") No. 144, "Accounting for the Impairment of Long-lived Assets". For property, plant and equipment and other long-lived assets, excluding indefinite lived intangible assets, the Company performs undiscounted operating cash flow analyses to determine if an impairment exists. If an impairment is determined to exist, any related impairment loss is calculated based on fair value.

Investments in Affiliates — The Company's investments in 20% to 50%-owned affiliates in which it has significant influence are accounted for using the equity method. Investments in affiliates where significant control does not exist are accounted for using the cost method.

Revenue Recognition — Revenue is recognized by the Company when all of the following criteria are met: persuasive evidence of an arrangement exists; delivery has occurred and ownership has transferred to the customer; the price to the customer is fixed or determinable; and collectibility is reasonably assured.

Goodwill and Other Intangibles — Goodwill is tested for impairment at least annually and more frequently if an event occurs which indicates the goodwill may be impaired in accordance with the Statement of Financial Accounting Standards (“SFAS”) No. 142, “Goodwill and Other Intangible Assets.” Impairment of goodwill is measured according to a two step approach. In the first step, the fair value of a reporting unit, as defined by the statement, is compared to the carrying value of the reporting unit, including goodwill. If the carrying amount exceeds the fair value, the second step of the goodwill impairment test is performed to measure the amount of the impairment loss, if any. In the second step the implied value of the goodwill is estimated as the fair value of the reporting unit less the fair value of all other tangible and identifiable intangible assets of the reporting unit. If the carrying amount of the goodwill exceeds the implied fair value of the goodwill, an impairment loss is recognized in an amount equal to that excess, not to exceed the carrying amount of the goodwill.

Deferred Taxes — The Company recognizes deferred tax liabilities and assets for the expected future income tax consequences of events that have been recognized in the Company’s financial statements. Under this method, deferred tax liabilities and assets are determined based on the temporary differences between the financial statement carrying amounts and the tax bases of assets and liabilities using enacted tax rates in effect in the years in which the temporary differences are expected to reverse.

The Company does not provide for taxes which would be payable if undistributed earnings of its foreign subsidiaries or its foreign affiliate were remitted because the Company either considers these earnings to be invested for an indefinite period or anticipates that if such earnings were distributed, the U.S. income taxes payable would be substantially offset by foreign tax credits.

Stock-Based Compensation — At June 30, 2004, the Company has two stock-based compensation plans, which are described more fully in Note N, “Stock Option Plans.” The Company accounts for these plans under the recognition and measurement provisions of Accounting Principles Board Opinion No. 25, “Accounting for Stock Issued to Employees,” and related Interpretations. No stock-based employee compensation cost related to stock options is reflected in earnings, as all option grants under those plans had an exercise price equal to or greater than the market value of the underlying common stock on the date of grant. The effect on net earnings and earnings per share if the Company had applied the fair value recognition provisions of SFAS No. 123, “Accounting for Stock-Based Compensation,” to stock-based employee compensation is disclosed in Note N.

Management Estimates — The preparation of financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent liabilities at the dates of the financial statements and the reported amounts of revenues and expenses during the reporting periods. Actual amounts could differ from those estimates.

Shipping and Handling Fees and Costs — The Company records revenue from shipping and handling costs in net sales. The cost associated with shipping and handling of products is reflected in cost of sales.

Reclassification — Certain amounts in prior year financial statements have been reclassified to conform to the presentation in the 2004 financial statements.

FINANCIALS

B. ACQUISITION

Effective May 31, 2004, The company acquired 100% of the common stock of Rolla SP Propellers SA of Balerna, Switzerland. Rolla designs and manufactures custom propellers.

Rolla will have a fiscal year ended May 31, since the acquisition was also effective May 31. No results of operations of Rolla are included in consolidated results for the year ended June 30, 2004.

The acquisition cost, including consulting fees, net of cash acquired was \$5,085,000.

The condensed balance sheet of Rolla as of May 31, 2004 is as follows (in thousands):

Current assets	\$ 3,323
Net fixed assets	3,636
Intangibles	3,189
Total	<u>\$ 10,148</u>

Current liabilities	\$ 2,056
Long term debt	1,146
Deferred taxes	655
Stockholders' equity	6,291
Total	<u>\$ 10,148</u>

Intangible Assets Identified and the Amounts

Assigned are as Follows:

Intangible assets subject to amortization:

Proprietary technology	\$ 840
Computer software	860
Other	408
Total	<u>\$ 2,108</u>

The Weighted Average Amortization Period is 7 years.

Intangible assets not subject to amortization:

Goodwill	\$ 927
Tradename	154
Total	<u>\$ 1,081</u>

The goodwill is not expected to be deductible for tax purposes.

C. INVENTORIES

The major classes of inventories at June 30 were as follows (in thousands):

	2004	2003
Finished parts	\$ 39,139	\$ 36,175
Work-in-process	8,187	7,003
Raw materials	4,753	4,069
	\$ 52,079	\$ 47,247

Inventories stated on a LIFO basis represent approximately 45% and 43% of total inventories at June 30, 2004 and 2003, respectively. The approximate current cost of the LIFO inventories exceeded the LIFO cost by \$19,898,000 and \$20,542,000 at June 30, 2004 and 2003, respectively. Inventory quantities were reduced in 2003 resulting in a liquidation of LIFO inventory quantities carried at costs prevailing in prior years which were lower than current costs. The effect was to decrease the 2003 net loss by \$70,000.

D. PROPERTY, PLANT AND EQUIPMENT

Property, plant and equipment at June 30 were as follows (in thousands):

	2004	2003
Land	\$ 3,414	\$ 1,412
Buildings	26,421	24,948
Machinery and equipment	96,749	92,371
	126,584	118,731
Less accumulated depreciation	93,362	88,521
	\$ 33,222	\$ 30,210

E. INVESTMENT IN AFFILIATE

The Company's investment in affiliate consisted of a 25% minority interest in Palmer Johnson Distributors, LLC (PJD) a domestic distributor of Twin Disc products.

In January 2004, the Company sold its 25% minority interest in PJD to the majority holder, PJD, Inc. for \$3,811,000 cash, which approximated the net book value of the investment. The Company recognized pre-tax earnings of \$240,000, \$414,000 and \$481,000 in fiscal years 2004, 2003 and 2002, respectively, from its investment in PJD. In addition, the Company received cash distributions of \$195,000, \$303,000 and \$400,000 in fiscal years 2004, 2003 and 2002, respectively.

Combined condensed financial data for the investment in affiliate accounted for under the equity method of accounting through the date of sale are summarized below (in thousands). The statement of operations information includes the results of operations of the domestic distributor from June 1 through December 31 for 2004 and from June 1 through May 31 for 2003 and 2002.

			2003
Current assets			\$ 12,792
Other assets			2,125
			\$ 14,917
Current liabilities			\$ 2,662
Other liabilities			2,164
Shareholders' equity			10,091
			\$ 14,917
	2004	2003	2002
Net sales	\$ 15,165	\$ 27,008	\$ 23,774
Gross profit	4,710	8,831	8,300
Net earnings	962	1,607	1,925

At June 30, 2003, trade receivables from the 25% owned distributor were \$1,719,000.

Sales to the Company's 25% owned domestic distributor were the same terms and conditions as sales to independent distributors. Sales to this distributor were \$6,240,000, \$10,886,000 and \$9,250,000 in fiscal 2004, 2003 and 2002, respectively.

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F. GOODWILL AND OTHER INTANGIBLES

The Company performed impairment tests of its goodwill during 2004, 2003 and 2002 and determined that no impairment of goodwill existed. Goodwill at June 30, 2004 and 2003 is net of accumulated amortization of \$789,000. There were no other significant indefinite lived intangible assets identified by the Company at June 30, 2004 or 2003.

The changes in the carrying amount of goodwill, substantially all of which is allocated to the manufacturing segment, for the years ended June 30, 2004 and 2003 were as follows (in thousands):

Balance at June 30, 2002	\$ 12,311
Translation adjustment	565
Balance at June 30, 2003	<u>12,876</u>
Disposal	(1,188)
Translation adjustment	102
Acquisition	<u>927</u>
Balance at June 30, 2004	<u><u>\$ 12,717</u></u>

Included in Other assets in the Company's Consolidated Balance Sheet as of the end of June 30, 2004 and 2003, respectively, are the following acquired intangible assets (in thousands):

Intangible assets with finite lives:	<u>2004</u>	<u>2003</u>
Licensing agreements	\$ 3,015	\$ 5,490
Other	<u>2,865</u>	<u>1,259</u>
	5,880	6,749
Accumulated amortization	2,475	4,211
Write off of impaired asset	—	773
Total	<u><u>\$ 3,405</u></u>	<u><u>\$ 1,765</u></u>

In the second quarter of 2003, a charge of \$773,000 was recorded based on SFAS 144 impairment tests. This charge was classified as a component of cost of sales pertaining to the Company's manufacturing segment.

The weighted average remaining useful life of the intangible assets included in the table above is approximately 11 years.

Intangible amortization expense for the year ended June 30, 2004, 2003 and 2002 was \$466,000, \$601,000 and \$726,000, respectively. Estimated intangible amortization expense for each of the subsequent five fiscal years is as follows (in thousands):

Fiscal Year	
2005	\$ 495
2006	382
2007	374
2008	374
2009	374
Thereafter	<u>1,406</u>
	<u><u>\$ 3,405</u></u>

G. JOINT VENTURE

On April 2, 2001, the Company entered into a joint venture agreement with Niigata Engineering Co. LTD., Japan to form NICO Transmissions Co., Inc. (NTC). NTC is an engineering and marketing company supporting the Company's expanding global marine product line as well as a distribution company for Niigata's family of transmission products.

In 2002, Niigata filed for creditor protection in Japan under the local bankruptcy code. Niigata was acquired out of bankruptcy in 2003 and the acquiring company is participating in the joint venture under the original terms of the joint agreement. Subsequent to the acquisition of Niigata, the name of the Joint Venture was changed to Twin Disc Nico Co. LTD. During 2002 the Company fully reserved for its receivable from Niigata in the amount of \$237,000 as a result of this filing.

H. ACCRUED LIABILITIES

Accrued liabilities at June 30 were as follows (in thousands):

	<u>2004</u>	<u>2003</u>
Salaries and wages	\$ 4,911	\$ 4,756
Retirement benefits	7,559	6,309
Warranty	6,478	6,070
Other	8,314	7,750
	<u>\$ 27,262</u>	<u>\$ 24,885</u>

I. WARRANTY

The Company warrants all assembled products and parts (except component products or parts on which written warranties are issued by the respective manufacturers thereof and are furnished to the original customer, as to which the Company makes no warranty and assumes no liability) against defective materials or workmanship. Such warranty generally extends from periods ranging from 12 months to 24 months.

The Company engages in extensive product quality programs and processes, including actively monitoring and evaluating the quality of its suppliers. However, its warranty obligation is affected by product failure rates, the extent of the market affected by the failure and the expense involved in satisfactorily addressing the situation. The warranty reserve is established based on the Company's best estimate of the amounts necessary to settle future and existing claims on products sold as of the balance sheet date. When evaluating the adequacy of the reserve for warranty costs, management takes into consideration the term of the warranty coverage, historical claim rates and costs of repair, knowledge of the type and volume of new products and economic trends. While the Company believes the warranty reserve is adequate and that the judgment applied is appropriate, such amounts estimated to be due and payable in the future could differ materially from what actually transpires.

The following is a listing of the activity in the warranty reserve during the years ended June 30 (in thousands):

	<u>2004</u>	<u>2003</u>
Reserve balance, July 1	\$ 6,070	\$ 5,294
Current period expense	4,764	4,417
Payments or credits to customers	(4,356)	(3,766)
Adjustments to pre-existing warranties	—	125
Reserve balance, June 30	<u>\$ 6,478</u>	<u>\$ 6,070</u>

J. DEBT

Notes payable consists of amounts borrowed under unsecured line of credit agreements. Unused lines of credit total \$8,969,000 at June 30, 2004. These lines of credit may be withdrawn at the option of the banks. The weighted average interest rate on the lines outstanding was 2.8% and 3.4% at June 30, 2004 and 2003, respectively.

Included in long-term debt is \$2,841,000 and \$5,698,000 of 7.37% ten-year unsecured notes at June 30, 2004 and 2003, respectively. The current portion of these notes was \$2,857,000 at June 30, 2004 and 2003. These notes contain certain covenants, including the maintenance of a current ratio of not less than 1.5 and the maintenance of an EBITDA to fixed charges ratio greater than 1.75. Consolidated net worth must be at least equal to the sum of \$60,310,000 plus 35% of consolidated net earnings for each quarter from July 1, 1996, however, the Company may exclude up to \$34,000,000 of net worth adjustments that result from changes to the assumptions used by the Company in determining its pension liability or changes in the market value of plan assets. As of June 30, 2004, the Company was in compliance with all debt covenants.

In December, 2002, the Company entered into a \$20,000,000 revolving loan agreement which expires on October 31, 2005. This agreement contains certain covenants, including restrictions on investments, acquisitions and indebtedness. Financial covenants include a minimum consolidated net worth calculated consistently with the net worth covenant discussed in the above paragraph, minimum EBITDA of \$11,000,000 at June 30, 2004 and a maximum total funded debt to EBITDA ratio of 2.5 at June 30, 2004. As of June 30, 2004, the Company was in compliance with all debt covenants. The outstanding balance of \$12,800,000 and \$10,865,000 at June 30, 2004 and 2003, respectively, is classified as long-term debt. Notes under this agreement bear interest on a schedule determined by the Company's leverage ratio and the LIBOR interest rate (LIBOR plus 1.25% and 2.75% at June 30, 2004 and 2003, respectively). The rate was 2.375% and 4.07% at June 30, 2004 and 2003, respectively.

As part of the acquisition of Rolla SP Propellers S.A., the Company assumed \$1,077,020 of secured long term debt which is due May 28, 2008. The long term debt bears interest of 4.25%. The debt is to be used for the construction of a new manufacturing facility and is secured by that facility. An additional secured line of credit of \$1,777,000 is available for the construction of the new facility and is secured by the facility. The line of credit bears interest of 3.0% at June 30, 2004. In addition, the Company assumed short and long-term capital lease obligations of \$161,000 and \$69,000, respectively.

The aggregate scheduled maturities of outstanding long term debt obligations in subsequent years are as follows (in thousands):

Fiscal Year	
2005.....	\$ 3,018
2006.....	15,736
2007.....	—
2008.....	1,077
	<u>\$ 19,831</u>

K. LEASE COMMITMENTS

Approximate future minimum rental commitments under noncancellable operating leases are as follows (in thousands):

Fiscal Year	
2005.....	\$ 2,700
2006.....	2,205
2007.....	1,506
2008.....	1,257
2009.....	1,147
Thereafter	1,470
	<u>\$ 10,285</u>

Total rent expense for operating leases approximated \$3,587,000, \$3,320,000, and \$3,135,000 in 2004, 2003, and 2002 respectively.

L. SHAREHOLDERS' EQUITY

At June 30, 2004 and 2003, treasury stock consisted of 792,748 and 845,798 shares of common stock, respectively. The Company issued 23,050 shares of treasury stock in 2004 to fulfill its obligations under the stock option plans and 25,000 shares were issued as restricted stock grants. The difference between the cost of treasury shares and the option price is recorded in retained earnings. The fair value of the stock grants are recorded as unearned compensation and amortized over 2 and 4 year periods. The Company acquired 10,000 shares of treasury stock in 2003 for \$114,000.

Cash dividends per share were \$0.70 in 2004, 2003 and 2002.

In 1998, the Company's Board of Directors established a Shareholder Rights Plan and distributed to shareholders one preferred stock purchase right for each outstanding share of common stock. Under certain circumstances, a right may be exercised to purchase one one-hundredth of a share of Series A Junior Preferred Stock at an exercise price of \$160, subject to certain anti-dilution adjustments. The rights become exercisable ten (10) days after a public announcement that a party or group has either acquired at least 15% (or at least 25% in the case of existing holders who currently own 15% or more of the common stock), or commenced a tender offer for at least 25% of the Company's common stock. Generally, after the rights become exercisable, if the Company is a party to certain merger or business combination transactions, or transfers 50% or more of its assets or earnings power, or certain other events occur, each right will entitle its holders, other than the acquiring person, to buy a number of shares of common stock of the Company, or of the other party to the transaction, having a value of twice the exercise price of the right. The rights expire June 30, 2008, and may be redeemed by the Company for \$.05 per right at any time until ten (10) days following the stock acquisition date. The Company is authorized to issue 200,000 shares of preferred stock, none of which have been issued. The Company has designated 50,000 shares of the preferred stock for the purpose of the Shareholder Rights Plan.

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M. BUSINESS SEGMENTS AND FOREIGN OPERATIONS

The Company and its subsidiaries are engaged in the manufacture and sale of power transmission equipment. Principal products include industrial clutches, hydraulic torque converters, fluid couplings, power-shift transmissions, marine transmissions, universal joints, power take-offs and reduction gears. The Company sells to both domestic and foreign customers in a variety of market areas, principally construction, industrial, energy and natural resources and marine and agricultural.

The Company has two reportable segments: manufacturing and distribution. These segments are managed separately because each provides different services and requires different technology and marketing strategies. The accounting practices of the segments are the same as those described in the summary of significant accounting policies. Transfers among segments are at established inter-company selling prices.

Information about the Company's segments is summarized as follows (in thousands):

	<u>Manufacturing</u>	<u>Distribution</u>	<u>Total</u>
2004			
Net sales	\$ 172,688	\$ 59,176	\$ 231,864
Intra-segment sales	8,930	2,512	11,442
Inter-segment sales	30,081	4,252	34,333
Interest income	395	36	431
Interest expense	1,176	111	1,287
Income taxes	3,734	1,671	5,405
Depreciation and amortization	5,284	355	5,639
Segment earnings	5,356	2,975	8,331
Segment assets	166,049	30,247	196,296
Expenditures for segment assets	8,980	285	9,265
2003			
Net sales	\$ 153,713	\$ 63,413	\$ 217,126
Intra-segment sales	6,587	2,890	9,477
Inter-segment sales	25,848	2,210	28,058
Interest income	470	25	495
Interest expense	1,480	137	1,617
Income taxes	(1,054)	1,073	19
Depreciation and amortization	5,291	292	5,583
Segment (loss) earnings	(1,866)	1,943	77
Segment assets	152,093	32,761	184,854
Expenditures for segment assets	3,882	528	4,410
2002			
Net sales	\$ 155,730	\$ 61,848	\$ 217,578
Intra-segment sales	6,696	1,870	8,566
Inter-segment sales	22,784	6,843	29,627
Interest income	468	43	511
Interest expense	1,783	131	1,914
Income taxes	1,940	1,362	3,302
Depreciation and amortization	5,409	210	5,619
Segment earnings	2,247	2,366	4,613
Segment assets	139,810	30,275	170,085
Expenditures for segment assets	1,851	212	2,063

TWIN DISC, INC.

The following is a reconciliation of reportable segment net sales, earnings and assets, to the Company's consolidated totals (in thousands):

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Net sales			
Total net sales from reportable segments	\$231,864	\$217,126	\$217,578
Elimination of inter-company sales	(45,775)	(37,535)	(38,193)
Total consolidated net sales	<u>\$186,089</u>	<u>\$179,591</u>	<u>\$179,385</u>
Earnings (loss)			
Total earnings from			
reportable segments	\$ 8,331	\$ 77	\$ 4,613
Other corporate expenses	(3,088)	(2,445)	(2,555)
Total consolidated net earning (loss)	<u>\$ 5,243</u>	<u>\$ (2,368)</u>	<u>\$ 2,058</u>
Assets			
Total assets for reportable segments	\$196,296	\$184,854	
Elimination of inter-company assets	(21,100)	(19,402)	
Corporate assets	1,441	4,906	
Total consolidated assets	<u>\$176,637</u>	<u>\$170,358</u>	

Other significant items:

	Segment Totals	Elimination & Corporate Adjustments	Consolidated Totals
2004			
Interest income	\$ 431	\$ (179)	\$ 252
Interest expense	1,287	(209)	1,078
Income taxes	5,405	(696)	4,709
Depreciation and amortization	5,639	53	5,692
Expenditures for segment assets and business acquired	9,265	—	9,265
2003			
Interest income	\$ 495	\$ (328)	\$ 167
Interest expense	1,617	(294)	1,323
Income taxes	19	(302)	(283)
Depreciation and amortization	5,583	90	5,673
Expenditures for segment assets	4,410	—	4,410
2002			
Interest income	\$ 511	\$ (217)	\$ 294
Interest expense	1,914	(214)	1,700
Income taxes	3,302	(352)	2,950
Depreciation and amortization	5,619	90	5,709
Expenditures for segment assets	2,063	—	2,063

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Geographic information about the Company is summarized as follows (in thousands):

	2004	2003	2002
Net sales			
United States.	\$107,146	\$ 95,813	\$108,288
Other countries.	78,943	83,778	71,097
Total.	\$186,089	\$179,591	\$179,385
	2004	2003	
Long-lived assets			
United States.	\$ 55,774	\$ 63,865	
Belgium.	11,490	11,228	
Other countries.	12,995	6,646	
Elimination of inter-company assets.	(9,246)	(8,476)	
Total.	\$ 71,013	\$ 73,263	

One customer accounted for approximately 11%, 10% and 11% of consolidated net sales in 2004, 2003 and 2002, respectively.

N. STOCK OPTION PLANS

During fiscal 1999, the Company adopted the Twin Disc, Incorporated 1998 Stock Option Plan for Non-Employee Directors, a non-qualified plan for non-employee directors to purchase up to 35,000 shares of common stock, and the Twin Disc, Incorporated 1998 Incentive Compensation Plan, a plan where options are determined to be non-qualified or incentive at the date of grant, for officers and key employees to purchase up to 165,000 shares of common stock. The plans are administered by the Executive Selection and Compensation Committee of the Board of Directors which has the authority to determine which officers and key employees will be granted options. The grant of options to non-employee directors is fixed at options to purchase 1,000 shares of common stock per year or 600 at time of appointment. Except as described in the following sentence, all options allow for exercise prices not less than the grant date fair market value, vest immediately and expire ten years after the date of grant. For options under the Incentive Compensation Plan, if the optionee owns more than 10% of the total combined voting power of all classes of the Company's stock, the price will be not less than 110% of the grant date fair market value and the options expire five years after the grant date. In addition, the Company has 34,200 incentive stock option plan options and 31,300 non-qualified stock option plan options outstanding at June 30, 2004 under the Twin Disc, Incorporated 1988 Incentive Stock Option plan and the Twin Disc, Incorporated 1988 Non-Qualified Stock Option Plan for Officers, Key Employees and Directors, respectively. Options can no longer be issued from the 1988 plans.

Shares available for future options as of June 30 were as follows:

	2004	2003
1998 Stock Option Plan for Non-Employee Directors	6,400	6,400
1998 Incentive Compensation Plan	17,850	47,250

Stock option transactions under the plans during 2004, 2003 and 2002 were as follows:

	2004	Weighted Average Price	2003	Weighted Average Price	2002	Weighted Average Price
Non-qualified stock options:						
Options outstanding						
at beginning of year	133,150	\$18.54	102,350	\$20.46	88,350	\$21.31
Granted	—	—	48,800	14.37	14,500	15.05
Canceled	(15,450)	19.89	(18,000)	18.14	(500)	14.00
Exercised	(13,350)	14.18	—	—	—	—
Options outstanding at June 30	104,350	\$18.90	133,150	\$18.54	102,350	\$20.46
Options price range (\$14.45 – \$20.00)						
Number of shares	72,650					
Weighted average price	\$ 16.28					
Weighted average remaining life	8.40 years					
Options price range (\$21.875 – \$28.75)						
Number of shares	31,700					
Weighted average price	\$ 24.90					
Weighted average remaining life	4.83 years					

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	2004	Weighted Average Price	2003	Weighted Average Price	2002	Weighted Average Price
Incentive stock options:						
Options outstanding at beginning of year	106,700	\$20.55	146,000	\$20.75	125,650	\$22.29
Granted	—	—	—	—	30,200	15.25
Canceled	(13,150)	23.16	(39,300)	21.32	(9,850)	23.47
Exercised	(9,700)	15.86	—	—	—	—
Options outstanding at June 30	<u>83,850</u>	<u>\$20.68</u>	<u>106,700</u>	<u>\$20.55</u>	<u>146,000</u>	<u>\$20.75</u>
Options price range (\$15.05 - \$20.00)						
Number of shares	51,450					
Weighted average price	\$ 17.77					
Weighted average remaining life	7.40 years					
Options price range (\$21.875 - \$28.75)						
Number of shares	32,400					
Weighted average price	\$ 25.30					
Weighted average remaining life	4.99 years					

The Company accounts for its stock option plans under the guidelines of Accounting Principles Board Opinion No. 25. Had the Company recognized compensation expense determined based on the fair value at the grant date for awards under the plans, the net earnings and earnings per share would have been as follows (in thousands, except per share amounts):

	2004	2003	2002
Net earnings (loss)			
As reported	\$ 5,243	\$ (2,368)	\$ 2,058
Pro forma	5,243	(2,442)	1,954
Basic earnings (loss) per share			
As reported	\$ 1.86	\$ (0.84)	\$ 0.73
Pro forma	1.86	(0.87)	0.70
Diluted earnings (loss) per share			
As reported	\$ 1.84	\$ (0.84)	\$ 0.73
Pro forma	1.84	(0.87)	0.70

There were no options granted during 2004. The above pro forma net earnings and earnings per share were computed using the fair value of options at the date of grant (for options granted after June 1995) as calculated by the Black-Scholes option-pricing method and the following assumptions: 22% volatility, 4.8% annual dividend yield, risk free interest rates of 3.58% and 2.71% in 2003 and 23% volatility, 4.5% annual dividend yield, risk free interest rate of 4.53% in 2002, a 5 year term and an exercise price equal to the fair market value on the date of grant except for incentive options granted to greater than 10% shareholders which are calculated using a 3 year term and an exercise price equal to 110% of the fair market value on the date of grant. For those options granted during 2003 and 2002 with exercise prices equal to the grant date fair market value, the exercise prices and weighted average fair values of the options were \$14.34 and \$1.83 in 2003 and \$15.05 and \$2.37 in 2002, respectively. For those options granted with exercise prices greater than the grant date fair market value, the exercise prices and weighted average fair values of the options were none in 2003 and \$16.56 and \$1.83 in 2002, respectively.

In fiscal 2004, the Company issued restricted stock grants for 25,000 shares, 12,500 of these shares vest in two years from the date of grant and 12,500 vest in four years. The fair value of the grants based on the market price at the date of grant was \$421,000. The grants are recorded as Unearned Compensation and amortized over two and four year periods. Amortization expense in fiscal 2004 approximated \$188,500.

O. ENGINEERING AND DEVELOPMENT COSTS

Engineering and development costs include research and development expenses for new products, development and major improvements to existing products, and other charges for ongoing efforts to refine existing products. Research and development costs charged to operations totaled \$2,840,000, \$2,220,000, and \$1,887,000 in 2004, 2003 and 2002 respectively. Total engineering and development costs were \$7,600,000, \$7,190,000, and \$6,718,000 in 2004, 2003 and 2002 respectively.

P. PENSION AND OTHER POSTRETIREMENT BENEFIT PLANS

The Company has non-contributory, qualified defined benefit pension plans covering substantially all domestic employees hired prior to October 1, 2003 and certain foreign employees. Domestic plan benefits are based on years of service, and, for salaried employees, on average compensation for benefits earned prior to January 1, 1997 and on a cash balance plan for benefits earned after January 1, 1997. The Company's funding policy for the plans covering domestic employees is to contribute an actuarially determined amount which falls between the minimum and maximum amount that can be deducted for federal income tax purposes. Domestic plan assets consist principally of listed equity and fixed income securities.

On June 20, 2003 the Board of Directors amended the defined benefit pension plans covering domestic salaried and hourly employees to exclude all employees hired after October 1, 2003 from the plans. In addition, a portion of the medical supplement for post-1992 retirees that is payable prior to Medicare eligibility has been removed from the plan. The \$19.24 per month benefit times years of service has been reduced to \$4.42 per month times years of service. This is effective October 1, 2003 for all participants. The \$14.82 benefit removed is now provided through the retiree health plan discussed below. The remaining medical supplement will be calculated using service frozen as of October 1, 2003.

In addition, the Company has unfunded, non-qualified retirement plans for certain management employees and directors. Benefits are based on final average compensation and vest upon retirement from the Company.

In addition to providing pension benefits, the Company provides health care and life insurance benefits for certain domestic retirees. All employees retiring after December 31, 1992, and electing to continue coverage through the Company's group plan, are required to pay 100% of the premium cost. On June 20, 2003 the Board of Directors amended the coverage under the plans as follows:

- Pre-1993 retirees are required to pay any cost increases after 2003 for retiree medical coverage.
- Dental and vision coverage for Pre-1993 retirees was eliminated.
- Life insurance coverage for individuals who retire on or after October 1, 2003 was eliminated.
- Access to retiree medical coverage after age 65 for individuals who retire on or after October 1, 2003 and their spouses was eliminated.
- Retiree medical coverage was eliminated for all employees hired on or after October 1, 2003.
- A Healthcare Reimbursement Account ("HRA") program will be established for individuals who retire after January 1, 1993 but before age 65.

Obligations and Funded Status

The following table sets forth the Company's defined benefit pension plans' and other post-retirement benefit plan's funded status and the amounts recognized in the Company's balance sheets and income statements as of June 30 (dollars in thousands):

	Pension Benefits		Other Postretirement Benefits	
	2004	2003	2004	2003
Change in benefit obligation:				
Benefit obligation, beginning of year	\$115,960	\$115,147	\$ 32,369	\$ 32,999
Service cost	1,260	1,344	45	17
Interest cost	7,475	8,277	2,057	2,362
Amendments	—	(6,376)	—	(6,106)
Actuarial loss	9,603	7,034	(633)	6,678
Benefits paid	(10,147)	(9,466)	(4,043)	(3,581)
Benefit obligation, end of year	<u>\$124,151</u>	<u>\$115,960</u>	<u>\$ 29,795</u>	<u>\$ 32,369</u>
Change in plan assets:				
Fair value of assets, beginning of year	\$ 75,278	\$ 92,405	\$ —	\$ —
Actual return on plan assets	19,325	(9,403)	—	—
Employer contribution	4,582	1,742	4,043	3,581
Benefits paid	(10,147)	(9,466)	(4,043)	(3,581)
Fair value of assets, end of year	<u>\$ 89,038</u>	<u>\$ 75,278</u>	<u>\$ —</u>	<u>\$ —</u>
Funded status	\$ (35,113)	\$ (40,682)	\$ (29,795)	\$ (32,369)
Unrecognized net transition obligation	358	391	—	—
Unrecognized actuarial loss	50,252	58,128	14,979	17,159
Unrecognized prior service cost	(5,467)	(5,842)	(5,427)	(6,106)
Net amount recognized	<u>\$ 10,030</u>	<u>\$ 11,995</u>	<u>\$ (20,243)</u>	<u>\$ (21,316)</u>

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	Pension Benefits		Other Postretirement Benefits	
	2004	2003	2004	2003
Amounts recognized in the balance sheet consist of:				
Accrued benefit liability	(34,544)	(39,483)	(20,243)	(21,316)
Intangible asset	—	24	—	—
Deferred tax asset	17,384	20,067	—	—
Minimum pension liability adjustment	27,190	31,387	—	—
Net amount recognized	<u>\$ 10,030</u>	<u>\$ 11,995</u>	<u>\$ (20,243)</u>	<u>\$ (21,316)</u>

The accumulated benefit obligation for all defined benefit pension plans was \$124,151,000 and \$115,960,000 at June 30, 2004 and 2003, respectively.

Information for pension plans with an accumulated benefit obligation in excess of plan assets:

	June 30	
	2004	2003
Projected and accumulated benefit obligation	\$124,151	\$115,960
Fair value of plan assets	89,038	75,278

Components of Net Periodic Benefit Cost

	Pension Benefits		
	2004	2003	2002
Service cost	\$ 1,260	\$ 1,344	\$ 1,361
Interest cost	7,475	8,277	8,203
Expected return on plan assets	(6,361)	(7,883)	(8,476)
Amortization of prior service cost	124	624	625
Amortization of transition obligation	60	56	49
Unrecognized net loss	3,990	2,492	1,802
Net periodic benefit cost	<u>\$ 6,548</u>	<u>\$ 4,910</u>	<u>\$ 3,564</u>

	Postretirement Benefits		
	2004	2003	2002
Service cost	\$ 45	\$ 17	\$ 17
Interest cost	2,057	2,362	2,281
Recognized prior service cost	(678)	—	—
Recognized net actuarial loss	1,547	798	580
Net periodic benefit cost	<u>\$ 2,971</u>	<u>\$ 3,177</u>	<u>\$ 2,878</u>

Additional Information

	Pension Benefits		Other Benefits	
	2004	2003	2004	2003
Increase (decrease) in minimum liability included in other comprehensive income	\$ 4,197	\$ (9,720)	N/A	N/A

Assumptions

	2004	2003	2004	2003
Weighted average assumptions used to determine benefit obligations at June 30:				
Discount rate	6.00%	6.75%	6.00%	6.75%
Expected return on plan assets	8.50%	9.00%		
Weighted average assumptions used to determine net periodic benefit cost for years ended June 30:				
Discount rate	6.75%	7.50%	6.75%	7.50%
Expected return on plan assets	9.00%	9.00%		
Rate of compensation increase	5.00%	5.00%		

The assumed weighted average health care cost trend rate was 8% in 2004. A 1% increase in the assumed health care cost trend would increase the accumulated postretirement benefit obligation by approximately \$401,000 and the service and interest cost by approximately \$24,000. A 1% decrease in the assumed health care cost trend would decrease the accumulated postretirement benefit obligation by approximately \$376,000 and the service and interest cost by approximately \$22,000.

The Medicare Prescription Drug Improvement and Modernization Act of 2003 provides for a prescription drug benefit beginning in 2006 under Medicare Part D as well as a subsidy to sponsors of retiree health care benefit plans that provide a benefit that is at least actuarially equivalent to Medicare Part D. Based on the benefits provided and expected future prescription costs it has been estimated that the Company's plans will be actuarially equivalent through fiscal 2008. The effect of this will be to reduce the Company's benefit obligation by approximately \$1,600,000 and reduced related expense in fiscal 2005 by approximately \$225,000.

Plan Assets

The Company's pension plan weighted-average asset allocations at June 30, 2004 and 2003, by asset category are as follows:

Asset Category	Target Allocation	June 30	
		2004	2003
Equity securities	61%	66%	58%
Debt securities	35%	30%	42%
Real Estate	4%	4%	—
	<u>100%</u>	<u>100%</u>	<u>100%</u>

Due to market conditions and other factors, actual asset allocation may vary from the target allocation outlined above. The pension plans held 62,402 shares of Company stock with a fair market value of \$1,522,609 (1.7% percent of total plan assets) and \$882,988 (1.2% percent of total plan assets) at June 30, 2004 and 2003, respectively.

The Company employs a total return on investment approach whereby a mix of equities and fixed income investments are used to maximize long-term return of plan assets while avoiding excessive risk. Pension plan guidelines have been established based upon an evaluation of market conditions, tolerance for risk, and cash requirements for benefit payments. Investment risk is measured and monitored on an ongoing basis through quarterly investment portfolio reviews, and annual liability measurements.

The plans have a long-term return assumption of 8.50%. This rate was derived based upon historical experience and forward-looking return expectations for major asset class categories.

Cash Flows

Contributions

The Company expects to contribute \$7,476,000 to its pension plans in fiscal 2005.

Estimated Future Benefit Payments

The following benefit payments, which reflect expected future service, as appropriate, are expected to be paid:

	Pension Benefits	Other Benefits
2005	\$ 9,269	\$ 3,799
2006	8,931	4,603
2007	9,129	5,273
2008	9,259	5,673
2009	9,350	6,131
Years 2010–2014	\$ 47,273	\$ 33,776

The Company sponsors defined contribution plans covering substantially all domestic employees and certain foreign employees. These plans provide for employer contributions based primarily on employee participation. The total expense under the plans was \$1,266,000, \$1,568,000 and \$1,780,000 in 2004, 2003, and 2002 respectively.

FINANCIALS

Q. INCOME TAXES

United States and foreign earnings (loss) before income taxes were as follows (in thousands):

	<u>2004</u>	<u>2003</u>	<u>2002</u>
United States.	\$ 3,243	\$ (6,808)	\$ 694
Foreign	6,734	4,169	4,440
	<u>\$ 9,977</u>	<u>\$ (2,639)</u>	<u>\$ 5,134</u>

The provision (credit) for income taxes is comprised of the following (in thousands):

	<u>2004</u>	<u>2003</u>	<u>2002</u>
Currently payable:			
Federal.	\$ 545	\$ (176)	\$ 168
State	50	48	70
Foreign	2,802	1,269	2,334
	<u>3,397</u>	<u>1,141</u>	<u>2,572</u>
Deferred:			
Federal.	826	(1,281)	441
State	279	(587)	(83)
Foreign	207	444	20
	<u>1,312</u>	<u>(1,424)</u>	<u>378</u>
	<u>\$ 4,709</u>	<u>\$ (283)</u>	<u>\$ 2,950</u>

The components of the net deferred tax asset as of June 30 are summarized in the table below (in thousands):

	<u>2004</u>	<u>2003</u>
Deferred tax assets:		
Retirement plans and employee benefits.	\$ 20,280	\$ 23,571
Alternative minimum tax credit carryforwards	986	509
Foreign tax credit carryforwards.	1,403	641
State net operating loss and other state credit carryforwards	406	553
Federal net operating loss carryforward	—	1,206
Other.	3,590	3,610
	<u>26,665</u>	<u>30,090</u>
Deferred tax liabilities:		
Property, plant and equipment.	3,996	4,222
Intangibles.	1,382	594
	<u>5,378</u>	<u>4,816</u>
Valuation allowance	(1,403)	(641)
Total net deferred tax assets	<u>\$ 19,884</u>	<u>\$ 24,633</u>

Management believes that it is more likely than not that the results of future operations will generate sufficient taxable income to realize deferred tax assets except for certain foreign tax credit carryforwards. Of the \$1,403,000 in foreign tax credit carryforwards at June 30, 2004, \$257,000 will expire in 2005, \$223,000 will expire in 2006, \$161,000 will expire in 2007 and \$762,000 will expire in 2009. The alternative minimum tax credit carryforwards will be carried forward indefinitely. Of the \$347,000 of state net operating loss carryforwards, net of federal tax, at June 30, 2004, \$326,000 will expire in 2014, \$17,000 will expire in 2015 and \$4,000 will expire in 2017. Of the \$58,000 net of federal tax of state credit carryforwards, any credits not used by 2006 will be deducted in 2007 and 2008.

TWIN DISC, INC.

Following is a reconciliation of the applicable U.S. federal income taxes to the actual income taxes reflected in the statements of operations (in thousands):

	<u>2004</u>	<u>2003</u>	<u>2002</u>
U.S. federal income tax at 34%	\$ 3,384	\$ (901)	\$ 1,749
Increases (reductions) in tax resulting from:			
Foreign tax items	1,082	291	144
State taxes	313	(366)	(298)
Valuation allowance	—	—	920
Disposition of investment in subsidiary	—	—	522
Statutory rate change	—	97	—
Other, net	(70)	596	(87)
	<u>\$ 4,709</u>	<u>\$ (283)</u>	<u>\$ 2,950</u>

The Company has not recorded deferred income taxes applicable to undistributed earnings of foreign subsidiaries that are indefinitely reinvested in foreign operations. The undistributed earnings amount to approximately \$20.8 million at June 30, 2004. If these earnings were remitted to the U.S., they would be subject to U.S. income tax. However this tax would be substantially less than the U.S. statutory income tax because of available foreign tax credits.

R. CONTINGENCIES

The Company is involved in litigation of which the ultimate outcome and liability to the Company, if any, is not presently determinable. Management believes that final disposition of such litigation will not have a material impact on the Company's results of operations or financial position.

S. RESTRUCTURING OF OPERATIONS

During the second quarter of fiscal 2003, the Company recorded a pre-tax restructuring charge of \$2.0 million in connection with the reduction of its workforce. These actions were taken in an effort to streamline the Company's cost structure and align its corporate workforce with market conditions. The charge consists of employee termination and severance benefits for a total of 58 employees; 48 production employees and 10 salaried employees. During 2004 and 2003, the Company made cash payments of \$358,000 and \$600,000, respectively. Accrued restructuring costs were \$942,000 and \$1,300,000 at June 30, 2004 and 2003, respectively.

FINANCIALS

TWIN DISC, INCORPORATED AND SUBSIDIARIES SCHEDULE II – VALUATION AND QUALIFYING ACCOUNTS

for the years ended June 30, 2004, 2003 and 2002 (in thousands)

Description	Balance at Beginning of Period	Additions Charged to Costs and Expenses	Deductions ¹	Balance at End of of Period
2004:				
Allowance for losses on accounts receivable	\$ 502	\$ 208	\$ 106	\$ 604
Reserve for inventory obsolescence	\$5,413	\$1,873	\$2,614	\$4,672
2003:				
Allowance for losses on accounts receivable	\$ 756	\$ 135	\$ 389	\$ 502
Reserve for inventory obsolescence	\$4,593	\$1,822	\$1,002	\$5,413
2002:				
Allowance for losses on accounts receivable	\$ 699	\$ 336	\$ 279	\$ 756
Reserve for inventory obsolescence	\$3,346	\$2,178	\$ 931	\$4,593

¹ Accounts receivable written-off and inventory disposed of during the year and other adjustments (primarily foreign currency translation adjustments).

SIGNATURES

Pursuant to the requirements of Section 13 or 15(d) 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.

TWIN DISC, INCORPORATED

By /s/ **FRED H. TIMM**
Fred H. Timm, Vice President –
Administration and Secretary
(Chief Accounting Officer)

September 15, 2004

Pursuant to the requirements of the Securities Exchange Act of 1934, this Report has been signed below by the following persons on behalf of the registrant and in the capacities and on the dates indicated.

By /s/ **MICHAEL E. BATTEN**
Michael E. Batten, Chairman,
Chief Executive Officer and Director

September 15, 2004

By /s/ **MICHAEL H. JOYCE**
Michael H. Joyce, President,
Chief Operating Officer and Director

By /s/ **CHRISTOPHER J. EPERJESY**
Christopher J. Eperjesy, Vice President –
Finance, Treasurer and Chief Financial Officer

September 15, 2004

Paul J. Powers, Director
David L. Swift, Director
John A. Mellowes, Director
George E. Wardeberg, Director
David R. Zimmer, Director
David B. Rayburn, Director
John H. Batten, Director

By /s/ **CHRISTOPHER J. EPERJESY**
Christopher J. Eperjesy, Attorney in Fact

FINANCIALS

EXHIBIT INDEX

TWIN DISC, INCORPORATED

10-K for Year Ended June 30, 2004

Exhibit	Description	Included Herewith
3a)	Articles of Incorporation, as restated October 21, 1988 (Incorporated by reference to Exhibit 3(a) of the Company's Form 10-K for the year ended June 30, 2004).	
b)	Corporate Bylaws, as amended through July 30, 2004 (Incorporated by reference to Exhibit 3(b) of the Company's Form 10-K for the year ended June 30, 2004).	
4a)	Form of Rights Agreement dated as of April 17, 1998 by and between the Company and the Firststar Trust Company, as Rights Agent, with Form of Rights Certificate (Incorporated by reference to Exhibits 1 and 2 of the Company's Form 8-A dated May 4, 1998).	
b)	Announcement of Shareholder Rights Plan per news release dated April 17, 1998 (Incorporated by reference to Exhibit 6(a), of the Company's Form 10-Q dated May 4, 1998).	
Material Contracts		
10a)	The 1988 Incentive Stock Option Plan (Incorporated by reference to Exhibit 10(a) of the Company's Form 10-K for the year ended June 30, 2004).	
b)	The 1988 Non-Qualified Stock Option Plan for Officers, Key Employees and Directors (Incorporated by reference to Exhibit 10(b) of the Company's Form 10-K for the year ended June 30, 2004).	
c)	Amendment to 1988 Incentive Stock Option Plan of Twin Disc, Incorporated (Incorporated by reference to Exhibit 10(c) of the Company's Form 10-K for the year ended June 30, 2004).	
d)	Amendment to 1988 Non-Qualified Incentive Stock Option Plan for Officers, Key Employees and Directors of Twin Disc, Incorporated (Incorporated by reference to Exhibit 10(d) of the Company's Form 10-K for the year ended June 30, 2004).	
e)	Form of Severance Agreement for Senior Officers and form of Severance Agreement for Other Officers (Incorporated by reference to Exhibit 10(e) of the Company's Form 10-K for the year ended June 30, 2004).	
f)	Supplemental Retirement Plan (Incorporated by reference to Exhibit 10(f) of the Company's Form 10-K for the year ended June 30, 1998).	
g)	Director Tenure and Retirement Policy (Incorporated by reference to Exhibit 10(g) of the Company's Form 10-K for the year ended June 30, 2004).	
10h)	Form of Twin Disc, Incorporated Corporate Short Term Incentive Plan (Incorporated by reference to Exhibit 10(h) of the Company's Form 10-K for the year ended June 30, 2004).	
i)	The 1998 Incentive Compensation Plan (Incorporated by reference to Exhibit A of the Proxy Statement for the Annual Meeting of Shareholders held on October 16, 1998).	
j)	The 1998 Stock Option Plan for Non-Employee Directors (Incorporated by reference to Exhibit B of the Proxy Statement for the Annual Meeting of Shareholders held on October 16, 1998).	
21	Subsidiaries of the Registrant	X
23	Consent of Independent Registered Public Accounting Firm	X
24	Power of Attorney	X
31a	Certification	X
31b	Certification	X
32a	Certification pursuant to 18 U.S.C. Section 1350	X
32b	Certification pursuant to 18 U.S.C. Section 1350	X

EXHIBIT 21

SUBSIDIARIES OF THE REGISTRANT

Twin Disc, Incorporated, the registrant (a Wisconsin Corporation) owns directly or indirectly 100% of the following subsidiaries:

1. Twin Disc International, S.A. (a Belgian corporation)
2. Twin Disc Technodrive Srl (an Italian corporation)
3. Rolla Sp Propellers SA (a Swiss corporation)
4. Twin Disc Srl (an Italian corporation)
5. Twin Disc (Pacific) Pty. Ltd. (an Australian corporation)
6. Twin Disc (Far East) Ltd. (a Delaware corporation operating in Singapore and Hong Kong)
7. Mill-Log Equipment Co., Inc. (an Oregon corporation)
8. Twin Disc Southeast, Inc. (a Florida corporation)
9. Technodrive SARL (a French corporation)

Twin Disc, Incorporated also owns 66% of Twin Disc Nico Co. LTD. (a Japanese corporation)

The registrant has no parent nor any other subsidiaries. All of the above subsidiaries are included in the consolidated financial statements.

EXHIBIT 23

CONSENT OF INDEPENDENT REGISTERED PUBLIC ACCOUNTING FIRM

We hereby consent to the incorporation by reference in the Registration Statements on Form S-8 (File Nos. 333-9929, 333-69361, 333-69015, 33-26816, 33-26817) of Twin Disc, Incorporated of our report dated July 30, 2004 relating to the financial statements and financial statement schedules, which appears in this Form 10-K.



PricewaterhouseCoopers LLP

Milwaukee, Wisconsin
July 30, 2004

EXHIBIT 24

POWER OF ATTORNEY

The undersigned directors of Twin Disc, Incorporated hereby severally constitute Michael E. Batten and Christopher J. Eperjesy, and each of them singly, true and lawful attorneys with full power to them, and each of them, singly, to sign for us and in our names as directors the Form 10-K Annual Report for the fiscal year ended June 30, 2004 pursuant to Section 13 or 15(d) of the Securities Exchange Act of 1934, and generally do all such things in our names and behalf as directors to enable Twin Disc, Incorporated to comply with the provisions of the Securities and Exchange Act of 1934 and all requirements of the Securities and Exchange Commission, hereby ratifying and confirming our signatures so they may be signed by our attorneys, or either of them, as set forth below.

July 30, 2004

/s/ **JOHN A. MELLOWES**
John A. Mellowes, Director

/s/ **DAVID L. SWIFT**
David L. Swift, Director

/s/ **PAUL J. POWERS**
Paul J. Powers, Director

/s/ **GEORGE E. WARDEBERG**
George E. Wardeberg, Director

/s/ **DAVID B. RAYBURN**
David B. Rayburn, Director

/s/ **DAVID R. ZIMMER**
David R. Zimmer, Director

EXHIBIT 31a
CERTIFICATIONS

I, Michael E. Batten, certify that:

1. I have reviewed this annual report on Form 10-K of Twin Disc, Incorporated;
2. Based on my knowledge, this annual 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 annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual 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 annual report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures, as defined in Exchange Act Rules 13(a)-15(e) and 15(d)-15(e) for the registrant and have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls 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 annual report is being prepared;
 - b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this annual report based on such evaluation; and
 - c) disclosed in this annual 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 fourth fiscal quarter in the case of this annual 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 officers 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 functions):
 - a) all significant deficiencies 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 control over financial reporting.

Date: September 15, 2004

/s/ **MICHAEL E. BATTEN**
Michael E. Batten
Chairman, Chief Executive Officer

EXHIBIT 31b CERTIFICATIONS

I, Christopher J. Eperjesy, certify that:

1. I have reviewed this annual report on Form 10-K of Twin Disc, Incorporated;
2. Based on my knowledge, this annual 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 annual report;
3. Based on my knowledge, the financial statements, and other financial information included in this annual 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 annual report;
4. The registrant's other certifying officers and I are responsible for establishing and maintaining disclosure controls and procedures, as defined in Exchange Act Rules 13(a)-15(e) and 15(d)-15(e) for the registrant and have:
 - a) designed such disclosure controls and procedures, or caused such disclosure controls 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 annual report is being prepared;
 - b) evaluated the effectiveness of the registrant's disclosure controls and procedures and presented in this annual report our conclusions about the effectiveness of the disclosure controls and procedures, as of the end of the period covered by this annual report based on such evaluation; and
 - c) disclosed in this annual 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 fourth fiscal quarter in the case of this annual 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 officers 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 functions):
 - a) all significant deficiencies 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 control over financial reporting.

Date: September 15, 2004

/s/ **CHRISTOPHER J. EPERJESY**
Christopher J. Eperjesy
Vice President – Finance, Treasurer,
Chief Financial Officer

EXHIBIT 32a

**CERTIFICATION PURSUANT TO
18 U.S.C. SECTION 1350,
AS ADOPTED PURSUANT TO
SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002**

In connection with the Annual Report of Twin Disc, Incorporated (the "Company") on Form 10-K for the fiscal year ending June 30, 2004, as filed with the Securities and Exchange Commission as of the date hereof (the "Report"), I, Michael E. Batten, Chairman and Chief Executive Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

- (1) the Report fully complies with Section 13(a) of the Securities Exchange Act of 1934, and
- (2) the information contained in the report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: September 15, 2004

/s/ **MICHAEL E. BATTEN**
Michael E. Batten
Chairman, Chief Executive Officer

EXHIBIT 32b

CERTIFICATION PURSUANT TO 18 U.S.C. SECTION 1350, AS ADOPTED PURSUANT TO SECTION 906 OF THE SARBANES-OXLEY ACT OF 2002

In connection with the Annual Report of Twin Disc, Incorporated (the "Company") on Form 10-K for the fiscal year ending June 30, 2004, as filed with the Securities and Exchange Commission as of the date hereof (the "Report"), I, Christopher J. Eperjesy, Vice President – Finance, Treasurer and Chief Financial Officer of the Company, certify, pursuant to 18 U.S.C. Section 1350, as adopted pursuant to Section 906 of the Sarbanes-Oxley Act of 2002, that, to the best of my knowledge:

- (1) the Report fully complies with Section 13(a) of the Securities Exchange Act of 1934, and
- (2) the information contained in the report fairly presents, in all material respects, the financial condition and results of operations of the Company.

Date: September 15, 2004

/s/ **CHRISTOPHER J. EPERJESY**
Christopher J. Eperjesy
Vice President – Finance, Treasurer,
Chief Financial Officer

(In thousands of dollars, except where noted)

	2004	2003	2002
STATEMENT OF OPERATIONS			
Net sales	\$186,089	\$179,591	\$179,385
Costs and expenses, including marketing, engineering and administrative	175,627	181,407	173,784
Earnings (loss) from operations	10,462	(1,816)	5,601
Other income (expense)	(485)	(823)	(458)
Earnings (loss) before income taxes and minority interest	9,977	(2,639)	5,143
Income taxes (credits)	4,709	(283)	2,950
Minority Interest	(25)	(12)	(135)
Net earnings (loss)	5,243	(2,368)	2,058
BALANCE SHEET			
<i>Assets</i>			
Cash and cash equivalents	9,127	5,908	7,400
Receivables, net	37,091	35,367	29,255
Inventories, net	52,079	47,247	44,504
Other current assets	7,327	8,573	8,631
Total current assets	105,624	97,095	89,790
Investments and other assets	37,791	43,053	37,941
Fixed assets less accumulated depreciation	33,222	30,210	29,549
Total assets	176,637	170,358	157,280
<i>Liabilities and Shareholders' Equity</i>			
Current liabilities	49,128	46,286	39,919
Long-term debt	16,813	16,584	18,583
Deferred liabilities	49,456	56,732	39,797
Minority Interest	509	485	472
Shareholders' equity	60,731	50,271	58,509
Total liabilities and shareholders' equity	176,637	170,358	157,280
<i>Comparative Financial Information</i>			
Per share statistics:			
Basic earnings (loss)	1.86	(0.84)	0.73
Diluted earnings (loss)	1.84	(0.84)	0.73
Dividends	0.70	0.70	0.70
Shareholders' equity	21.58	17.92	20.84
Return on equity	8.6%	(4.7)%	3.5%
Return on assets	3%	(1.4)%	1.3%
Return on sales	2.8%	(1.3)%	1.1%
Average shares outstanding	2,814,197	2,804,915	2,807,832
Diluted shares outstanding	2,843,374	2,804,915	2,807,832
Number of shareholder accounts	917	966	1,003
Number of employees	860	832	936
Additions to plant and equipment	4,180	4,410	2,063
Depreciation	5,228	5,072	5,012
Net working capital	56,496	50,809	49,871

TEN YEAR FINANCIAL SUMMARY

2001	2000	1999	1998	1997	1996	1995
\$180,786	\$177,987	\$168,142	\$202,643	\$189,942	\$176,657	\$164,232
170,260	168,105	164,816	186,607	177,342	164,486	154,347
10,526	9,882	3,326	16,036	12,600	12,171	9,885
2,565	(1,815)	(3,312)	9	80	(1,264)	(1,301)
13,091	8,067	14	16,045	12,680	10,907	8,584
6,922	4,294	1,032	6,682	4,951	4,348	2,912
-	-	-	-	-	-	-
6,169	3,773	(1,018)	9,363	7,729	6,559	5,672
5,961	5,651	4,136	5,087	8,983	2,043	3,741
27,058	28,828	27,201	28,320	32,428	34,917	29,247
46,492	50,190	54,500	53,280	47,844	51,083	47,157
12,255	5,333	11,910	6,893	8,707	8,597	10,345
91,766	90,002	97,747	93,580	97,962	96,640	90,490
33,384	49,885	40,218	31,646	26,544	30,344	30,463
31,584	34,303	38,935	35,728	34,249	35,715	37,348
156,734	174,190	176,900	160,954	158,755	162,699	158,301
41,450	40,908	54,761	29,553	29,621	34,002	36,852
23,404	31,254	17,112	19,949	19,944	19,938	14,000
33,121	23,795	37,567	29,457	35,393	33,578	32,827
337	-	-	-	-	-	-
58,422	78,233	67,460	81,995	73,797	75,181	74,622
156,734	174,190	176,900	160,954	158,755	162,699	158,301
2.20	1.34	(.36)	3.30	2.78	2.36	2.03
2.20	1.34	(.36)	3.24	2.75	2.34	2.02
0.70	0.70	0.805	0.76	0.70	0.70	0.70
20.81	27.84	23.79	28.94	26.48	27.07	26.75
10.6%	4.8%	(1.5)%	11.4%	10.5%	8.7%	7.6%
3.9%	2.2%	(0.6)%	5.8%	4.9%	4.0%	3.6%
3.4%	2.1%	(0.6)%	4.6%	4.1%	3.7%	3.5%
2,807,832	2,820,534	2,834,909	2,833,663	2,781,174	2,776,805	2,790,111
2,807,955	2,820,730	2,843,877	2,886,209	2,808,226	2,805,123	2,812,703
1,060	1,480	1,138	774	845	913	996
986	999	1,029	1,078	1,081	1,080	1,097
3,492	2,134	6,439	7,154	4,734	4,140	4,290
5,316	5,766	5,648	5,205	5,141	5,071	4,792
50,316	49,094	42,986	64,027	68,341	62,638	53,638

DIRECTORS

MICHAEL E. BATTEN

Chairman, Chief Executive Officer

MICHAEL H. JOYCE

President, Chief Operating Officer

JOHN H. BATTEN

Vice President and General Manager
Marine and Propulsion

JOHN A. MELLOWES

Chairman and Chief Executive Officer
Charter Manufacturing Co.
(A privately held producer of bar, rod wire
and wire parts)
Mequon, Wisconsin

PAUL J. POWERS

Retired Chairman, President – Chief Executive Officer
Commercial Intertech Corp.
(Manufacturer of Hydraulic Components,
Fluid Purification Products, Pre-Engineered
Buildings and Stamped Metal Products)
Youngstown, Ohio

DAVID B. RAYBURN

President and Chief Executive Officer
Modine Manufacturing Company
(Manufacturer of Heat Exchange Equipment)
Racine, Wisconsin

HAROLD M. STRATTON II

Chairman and Chief Executive Officer,
Strattec Security Corporation
(A manufacturer of mechanical locks,
electromagnetical locks and related security
access control products)
Milwaukee, Wisconsin

DAVID L. SWIFT

Retired Chairman, President – Chief Executive Officer
Acme-Cleveland Corporation
(Manufacturer of Diversified Industrial Products)
Pepper Pike, Ohio

GEORGE E. WARDEBERG

Retired Vice Chairman
Wisconsin Energy Corp.
(A holding company with subsidiaries in electric,
natural gas, energy services and manufacturing)
Milwaukee, Wisconsin

DAVID R. ZIMMER

Former Chief Executive Officer
Twitchell Corporation
(A privately held manufacturer and marketer
of highly engineered, synthetic yarns,
fabrics, extrusions, and coatings)
Dothan, Alabama

OFFICERS

MICHAEL E. BATTEN

Chairman, Chief Executive Officer

MICHAEL H. JOYCE

President, Chief Operating Officer

CHRISTOPHER J. EPERJESY

Vice President – Finance & Treasurer

JAMES E. FEIERTAG

Executive Vice President

JOHN H. BATTEN

Vice President and General Manager – Marine and Propulsion

HENRY-CLAUDE FABRY

Vice President – Global Distribution

FRED H. TIMM

Vice President – Administration and Secretary

CORPORATE DATA

ANNUAL MEETING

Twin Disc Corporate Offices
 Racine, Wisconsin
 2:00 P.M.
 October 15, 2004

SHARES TRADED

New York Stock Exchange: Symbol TDI

ANNUAL REPORT ON SECURITIES AND EXCHANGE COMMISSION FORM 10-K

Single copies of the Company's 2004 Annual Report on Securities and Exchange Commission Form 10-K, including exhibits, will be provided without charge to shareholders after September 30, 2004, upon written request directed to Fred H. Timm, Secretary, Twin Disc, Incorporated, 1328 Racine Street, Racine, Wisconsin 53403.

TRANSFER AGENT & REGISTRAR

Mellon Human Resources and Investor Solutions
 Chicago, Illinois

INDEPENDENT ACCOUNTANTS

PricewaterhouseCoopers LLP
 Milwaukee, Wisconsin

GENERAL COUNSEL

von Briesen & Roper, s.c.
 Milwaukee, Wisconsin

CORPORATE OFFICES

Twin Disc, Incorporated
 Racine, Wisconsin 53403
 Telephone: (262) 638-4000

WHOLLY-OWNED SUBSIDIARIES

Twin Disc International S.A.
 Nivelles, Belgium
 Twin Disc Srl
 Capezzano Pianore, Italy
 Twin Disc Technodrive Srl
 Decima, Italy
 Technodrive SARL
 Chambery, France
 Twin Disc (Pacific) Pty. Ltd.
 Brisbane, Queensland, Australia
 Twin Disc (Far East) Ltd.
 Singapore

Mill-Log Equipment Co., Inc.
 Coburg, Oregon
 Twin Disc Southeast, Inc.
 Miami, Florida
 Rolla SP Propellers SA
 Balerna, Switzerland

PARTIALLY OWNED SUBSIDIARIES

Twin Disc Nico Co. Ltd.

MANUFACTURING FACILITIES

Racine, Wisconsin
 Nivelles, Belgium
 Decima, Italy
 Balerna, Switzerland

SALES OFFICES

Domestic
 Racine, Wisconsin
 Coburg, Oregon
 Kent, Washington
 Miami, Florida
 Jacksonville, Florida
Foreign
 Nivelles, Belgium
 Brisbane and Perth, Australia
 Singapore
 Capezzano Pianore, Italy
 Decima, Italy
 Balerna, Switzerland
 Chambery, France
 Edmonton, Canada
 Vancouver, Canada
 Saitama, Japan
 Shanghai, China

MANUFACTURING LICENSES

Hitachi-Nico Transmission Co., Ltd.
 Tokyo, Japan

TWIN DISC, INC.

1328 RACINE STREET
RACINE, WISCONSIN 53403 USA
WWW.TWINDISC.COM

