To Our Stockholders, Customers and Employees:

During fiscal 2004, with overall economic conditions improving, the Company's operating environment showed signs of stability and, in certain markets, steady growth as the commercial airline industry continued to recover from the most significant economic downturn in its history. Our government and defense business remained strong as the U.S. Military continued to transform into a more rapidly deployable force and reduce costs by partnering with industry for supply chain management support. While the commercial airline industry took a few small steps toward recovery, AAR made a number of healthy strides.

Through the hard work and dedication of our employees and an intense focus on cost control, the Company was once again profitable for the year—a claim we could not make in our two previous annual reports.

During the course of the year we made significant progress on our financial goals, ultimately leading to a strong year-end finish. We grew sales by 7.5%, improved our earnings per share by $0.50 and achieved sequential sales and earnings improvement for each quarter. Our fourth quarter results were particularly strong as sales increased 24% over the prior year, reflecting growth in each of our four segments and representing the best sales and earnings figures since September 11, 2001. We ended the year having increased our backlog by 58% to one of the highest levels in the Company's history.

We generated positive cash flow from operations and issued $75 million of 2.875% convertible notes during the year. We extended our average recourse debt maturity from 3.8 years to 4.8 years, ending the year with $91 million of cash and available lines of credit, an increase of $66 million from the end of fiscal 2003. We also reduced our weighted average cost of recourse debt from 6.2% to 5.6% and reduced our net obligations by $47.7 million. As a result, we expect net interest expense savings of approximately $2.5 million in fiscal 2005. Our performance for the year is reflected in our stockholders' equity which surpassed $300 million.

With leading industry indicators such as available seat miles, revenue passenger miles and passenger load factors strengthening, revenues for most airlines are stable or on the rise. Nevertheless, many of our airline customers are struggling to return to profitability in the face of high fuel costs and low yields. As more airlines focus on the cost side of the ledger, we anticipate a fundamental shift in the way they manage their businesses, including the increased use of third-party maintenance (MRO) providers like AAR to provide total solutions at the best value.

> *"As an entrepreneurial Company with solid principles and an enduring vision, capitalizing on challenges and opportunities is one of our core strengths."*

Throughout the year, and in the months that followed, we implemented several initiatives and took a number of actions to position AAR to meet anticipated demand for high-quality, low-cost solutions in the aviation market. In perhaps our most ambitious move, in June of 2004 we announced that AAR would become the new tenant of the Indianapolis Maintenance Center (IMC), an airframe maintenance facility that is regarded as one of the finest in the world. We expect to be operational by the second half of fiscal 2005, setting in motion a new era for our aircraft services business.

We continue to establish and strengthen long-term relationships with customers. During the year, we signed multi-year contracts with Alaska Airlines, Avio, Boeing, Lockheed Martin, Mesa Airlines, Northrop Grumman and the U.S. Government, among others. We are looking to provide customers with additional value by increasing the engineering and technical content in our products and enhancing our processes to align with our customers' businesses — to make outsourcing as seamless as it is cost-effective.

Sales to the U.S. Government and its contractors remain robust and represented 34% of total sales in fiscal 2004. We are responding to the changing government market with innovative engineering and design solutions. As a result, we expect demand for our manufactured shelters, containers and pallets, as well as our logistics and maintenance services supporting military products and aircraft, to remain strong. In addition, we expect service opportunities for our mobility products to increase as the number of units in service grows, and we are investing accordingly.

Engine and airframe parts sales increased for the second consecutive year as our customers replenish their parts inventories in response to the improving commercial aviation market, though sales still remain well below historical levels. Our strategy to de-emphasize low-margin new parts distribution sales to general aviation customers and our prudent inventory acquisitions contributed to higher margins for the year.

As our customers add new-generation and regional aircraft to their fleets, we continue to invest in tooling and training to develop repair capabilities supporting these aircraft. As a result, we experienced growth in sales and income for our airframe maintenance operation in Oklahoma City. We have not yet seen a sustained increase in demand for our component repair services, but we are encouraged by improved results during the fourth quarter.

Our cargo systems business finished the year strong, with backlog more than tripling since the beginning of the fiscal year. During the year, we received orders to provide cargo systems for C-130J aircraft from Lockheed Martin, for MD-11 aircraft operated by Lufthansa and UPS, and for A310 aircraft operated by FedEx, to name a few. In addition, we were selected to develop the cargo handling system for the C-X aircraft, the Japanese Defense Agency's next-generation military transport aircraft.

We are focused on opportunistic buys of used aircraft and recently entered into a joint venture agreement with a global financial institution to capitalize on the imbalance in the used aircraft market for select aircraft. In connection with the joint venture, the Company signed a servicing agreement to provide portfolio management services that include aircraft remarketing, technical evaluations and lease management. As industry conditions improve, we anticipate that a stronger market for used aircraft and engines will emerge.

During fiscal 2004, the Company strengthened its capabilities, as well as its relationships with customers. We also shared AAR's unique value proposition with a growing list of new and potential customers throughout the world. Lastly, we made meaningful progress on generating cash and improving our balance sheet, ending the fiscal year with positive momentum.

In July 2004, we elected Ronald B. Woodard to our Board of Directors. Ron is the former President of the Boeing Commercial Airplane Group. He also founded and is currently the Chairman of MagnaDrive, Inc. His experience with Boeing brings a new element to AAR's Board and adds to the depth and breadth of its industry knowledge.

In Closing

Although the airline industry is in the midst of uncertain times, I believe we are well positioned to benefit from changing industry dynamics. The industry tends to undergo eight-to-ten-year economic cycles. However, after each previous down cycle, AAR has emerged a stronger and more profitable Company. I expect that this most recent down cycle will be no exception and that we will continue

> *"This year's financial results mark the 51st year of profitability in the Company's 53 years of operation."*

the momentum we established during the year by consistently applying our "close to the customer" business model.

Our government and aviation customers' requirements are evolving as they refine and implement new strategies for operating in the post-9/11 era. This creates a whole new marketplace for AAR, one abundant with challenges and opportunities. As an entrepreneurial Company with solid principles and an enduring vision, capitalizing on challenges and opportunities is one of our core strengths.

This year's financial results mark the 51st year of profitability in the Company's 53 years of operation. Going forward, I believe we have the right products, the right team and the right attitude to grow the business and provide exceptional value for our customers and stockholders.

I'd like to thank our Board of Directors for their valuable guidance and for their leadership in actively embracing new corporate governance initiatives. I'd also like to thank our customers for their business and the ongoing dialogue that enables us to improve our products and services. A special thanks to the employees of AAR for persevering through the turbulent times.

And, thanks to you, our stockholders, for your continued interest in our Company and your investment in our future.

Sincerely,

David P. Storch
President and Chief Executive Officer

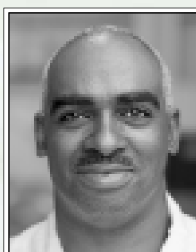
August 12, 2004

We Support.

Around the clock and around the world, AAR supports its customers with a wide range of maintenance, repair and overhaul (MRO) services that help minimize downtime and maximize the return on aircraft investments.

With a backdrop of rising fuel costs and increasing competition, our customers are changing the way they do business to reduce their operating costs while maintaining the highest levels of safety, service and quality. Outsourcing maintenance, repair and overhaul to AAR provides the competitive edge our customers need to rise above a turbulent marketplace.

AAR is better equipped than ever to provide light-to-heavy airframe maintenance checks and aircraft modifications. Our broad range of capabilities also includes the maintenance, repair and overhaul of landing gear systems, composite structures, avionics, instruments, pneumatics, hydraulics, electronics, fuel controls and engine components.



Customers rely on our experience to make sure that when their plane leaves our hangar it's 100% airworthy. It makes us proud when that plane returns for its next scheduled maintenance after carrying thousands of people safely to their destinations.

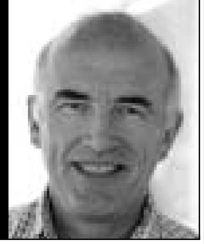
Byron Brookins – Maintenance, Repair and Overhaul

As a member of the Safety and Environmental team it's my job to bridge the gap between policy and practice. Teaming with our production leaders, we develop practical procedures to ensure that our facility is safe for our employees and our neighboring communities.

Terri Pace – Maintenance, Repair and Overhaul

We think it's important to build a strong rapport with our customers and get to know them on a first-name basis. It's how we do business and it serves as the foundation for our great long-term partnerships.

Dean Vivian – Manufacturing



For our customers, responsiveness is critical. By providing price quotes for our custom products in hours instead of days, we help customers meet their commitments and make their decision to work with us in the future easier.

Tina Swanson – Manufacturing

We Create.

At the core of military preparedness is a critical balance between steadfast stability and rapid mobility. In response to growing demand from our government customers during fiscal 2004, AAR stepped up its efforts to manufacture more of the pallets, containers and shelters used to support the U.S. Military's tactical deployment activities. These rugged, field-proven mobility products provide utility that ranges from transporting life-line supplies to providing sterile and climate-controlled environments for medical facilities.

AAR also designs and manufactures customized in-aircraft cargo systems for military and commercial customers as well as interior and exterior composite structures for the aviation and transportation industries.

Our approach to manufacturing begins with an in-depth understanding of our customers' requirements. By combining imagination, innovation and engineering expertise, we create products that surpass standards for quality and reliability—as defined by our customers.

We Deliver.

The right parts delivered to the right place at the right time. That's the foundation of AAR's extensive portfolio of supply chain management services. From a single component to an entire parts inventory management program, we serve our commercial and government customers and their contractors by providing high-quality components and customized end-to-end supply chain management services.

Our vast inventory includes new and refurbished airframe and engine parts for virtually every commercial aircraft and engine type. We also stock and deliver airframe and engine parts for private aircraft and military jets and helicopters. We provide a full range of parts services, including parts provisioning, repair and exchange, on-site warehouse management, inventory management and logistics programs.

Our dedicated inventory management and parts exchange programs help customers reduce costs, increase parts availability and reduce lead times. When customers need parts supply or total logistics support—we deliver.

Long-term relationships in this industry are built on personal and professional integrity. We stand behind our commitments to earn our customers' respect and gain their repeat business.

Dave Perri – Inventory and Logistics

My team works hard to anticipate our customers' parts requirements. We keep our finger on the pulse of the market and are constantly monitoring the composition of our inventory to maximize our ability to provide the components our customers need.

Sal Marino – Inventory and Logistics

Our job is to make complex transactions seem simple. We clearly summarize the capabilities and technical features of each aircraft to help our customers reach the decision that best fits their operational and financial requirements.

Laura Dyrstad – Sales and Leasing

We go the extra mile to locate exactly what our customers need. Then we leverage the strengths of our other AAR businesses to ensure that every engine and aircraft meets our uncompromising standards for quality and safety.

Christopher Olds – Sales and Leasing

We Connect.

In one part of the world an airline needs to modernize its fleet. Meanwhile, on the other side of the world an inventory of underutilized aircraft sits idle. Enter AAR. With our global network of contacts and unmatched aviation expertise, we have both the reach and the resources to locate, evaluate and acquire aircraft and engines to meet virtually every aviation need. On the "sell side," we improve our customers' liquidity by turning a surplus asset into working capital.

AAR also manages the many complexities that come with the remarketing of aircraft, including all related records management and aircraft preparation, modifications, transport and storage. Our financial stability and innovative financing solutions help speed the availability of aircraft, enabling our customers to offer revenue-generating services without delay.

AAR's industry experience and expansive network of relationships set us apart from the competition. From a single engine to a fleet of aircraft, we can connect our customers to a world of available resources.

*At AAR, we **support** our aviation customers with a broad range of maintenance and repair services. We **create** best-in-class products that endure years of use in some of the most severe conditions. We **deliver** on our promise to provide the parts and service our customers need – when and where they need them. And, we are a success because we **connect** with our customers, providing them with a world of solutions, service and support.*

Board of Directors

Ira A. Eichner
Chairman of the Board and Founder,
AAR CORP.

David P. Storch
President and Chief Executive Officer,
AAR CORP.

A. Robert Abboud
President, A. Robert Abboud & Co.

James G. Brocksmith, Jr.
Independent Business Consultant
Retired Deputy Chairman and Chief
Operating Officer, KPMG LLP

General Ronald R. Fogleman, USAF (Ret.)
President and Chief Operating Officer,
B Bar J Cattle Company
President and Chief Operating Officer,
Durango Aerospace, Inc.

James E. Goodwin
Independent Business Consultant
Retired Chairman and Chief Executive
Officer, UAL Corporation

Joel D. Spungin
Managing Partner, DMS Enterprises, L.P.
Retired Chairman and Chief Executive
Officer, United Stationers, Inc.

Marc J. Walfish
Founder, Merit Capital Partners

Ronald B. Woodard
Chairman of MagnaDrive, Inc.
Retired President of the Boeing
Commercial Airplane Group

Board Committees

Audit
A. Robert Abboud, Chairman
James G. Brocksmith, Jr.
James E. Goodwin
Joel D. Spungin

Compensation
James G. Brocksmith, Jr., Chairman
A. Robert Abboud
Ronald R. Fogleman
Joel D. Spungin

Executive
Ira A. Eichner, Chairman
David P. Storch
A. Robert Abboud

Nomination & Governance
James E. Goodwin, Chairman
Ronald R. Fogleman
Marc J. Walfish

Corporate Officers

David P. Storch
President and Chief Executive Officer

Michael K. Carr
Vice President, Tax

Peter K. Chapman
Vice President, Marketing and
Business Development

James J. Clark
Group Vice President, Maintenance,
Repair and Overhaul Services

Michael S. Cohen
Vice President, Operations
and Engineering

Kevin M. Larson
Vice President, Chief Information Officer

J. Mark McDonald
Group Vice President, Manufacturing

David E. Prusiecki
Vice President, Defense Systems
and Logistics

Howard A. Pulsifer
Vice President, General Counsel
and Secretary

Timothy J. Romenesko
Vice President, Chief Financial Officer
and Treasurer

Michael J. Sharp
Vice President, Controller and
Chief Accounting Officer

Timothy O. Skelly
Vice President, Human Resources