AVCORP

annual report 2012

ABOUT AVCORP INDUSTRIES INC. Avcorp designs and builds major airframe structures for some of the world's leading aircraft companies, including BAE Systems, Boeing and Bombardier. With more than 50 years of experience, over 400 skilled employees and 354,000 square feet of facilities in Delta BC and Burlington ON, Avcorp offers integrated composite and metallic aircraft structures to aircraft manufacturers, a distinct advantage in the pursuit of contracts for new aircraft designs, which require lower-cost, light-weight, strong, reliable structures. Our Burlington location also offers composite repairs for commercial aircraft. Avcorp is a Canadian public company traded on the Toronto Stock Exchange (TSX:AVP).

management discussion & analysis

This Management Discussion and Analysis has been prepared as of March 25, 2013, and should be read in conjunction with the Company's consolidated financial statements and notes thereto for the year ended December 31, 2012.

Description of Business

Avcorp Industries Inc. (the Company) supplies major airframe structures to aircraft manufacturers and to their suppliers. Our capabilities are product design, tool design, parts fabrication, assembly and repair, all of which are governed by strong program management.

We operate from two locations in Canada. Comtek Advanced Structures Ltd. (Comtek), a wholly owned subsidiary, is located in Ontario and is dedicated to composites manufacturing and repairs. Avcorp Industries Inc. is located in British Columbia and is dedicated to light weight metal manufacturing and assembly.

Avcorp is in compliance with industry standard quality requirements.

Financial Overview

Three-Year Results

The following table provides selected financial information for the three years to December 31, 2012.

THREE-YEAR RESULTS

unaudited, prepared in accordance with IFRS, expressed in thousands of Canadian dollars except per share amounts, ratios and shares outstanding

FOR THE YEAR ENDED DECEMBER 31	2012	2011	2010
OPERATIONS			
Revenues	**$ 89,337**	$ 86,018	$ 77,258
EBITDA[1]	**29,035**	3,847	(1,617)
Operating income (loss) before tax	**24,002**	(362)	(4,893)
Net income (loss)	**20,641**	(2,452)	(7,402)
Basic income (loss) per share	**0.09**	(0.01)	(0.04)
Diluted income (loss) per share	**0.09**	(0.01)	(0.04)
FINANCIAL POSITION			
Net capital expenditures	**557**	1,224	1,228
Total assets	**68,635**	54,961	45,680
Bank indebtedness and long-term debt	**7,114**	13,532	16,853
Shareholders' equity	**24,587**	1,112	2,478
Net book value per share	**0.10**	0.01	0.01
Ratio: debt/equity	**0.29**	12.17	6.80
Ratio: current assets/current liabilities	**2.63**	1.66	0.80
Shares outstanding at period end	**254,898,072**	201,994,113	195,505,323

1. EBITDA = earnings before interest, taxes, depreciation and amortization. This is not a recognized term under International Financial Reporting Standards (IFRS)

Quarterly Results

The following table provides selected unaudited quarterly financial information for the eight most recent fiscal quarters to December 31, 2012.

QUARTERLY RESULTS

unaudited, prepared in accordance with IFRS, expressed in thousands of Canadian dollars except per share amounts

	2012				2011			
FOR THE THREE MONTHS ENDED	**Dec 31**	Sep 30	Jun 30	Mar 31	Dec 31	Sep 30	Jun 30	Mar 31
Revenue	**$ 19,815**	$ 19,324	$ 25,192	$ 25,006	$ 24,227	$ 20,383	$ 20,492	$ 20,916
Operating (loss) profit	**24,177**	(1,446)	411	860	1,093	(186)	(752)	(517)
EBITDA[1]	**26,633**	(1,205)	1,656	1,951	1,920	1,455	259	213
Net income (loss)	**23,206**	(2,729)	13	151	293	(150)	(1,337)	(1,258)
EBITDA per share[1]								
Basic	**0.10**	(0.01)	0.01	0.01	0.01	0.01	0.00	0.00
Diluted	**0.10**	(0.01)	0.01	0.01	0.01	0.01	0.00	0.00
Net income (loss) per share								
Basic	**0.09**	(0.01)	0.00	0.00	0.00	(0.00)	(0.01)	(0.01)
Diluted	**0.09**	(0.01)	0.00	0.00	0.00	(0.00)	(0.01)	(0.01)
Long-term debt	**4,300**	4,409	11,800	12,081	12,027	12,555	6,516	3,129[2]

1. EBITDA = earnings before interest, taxes, depreciation and amortization. This is not a recognized term under IFRS
2. Exclusive of convertible debenture held by Export Development Canada which was classified as current portion of long-term debt

2012 and 2011 Results Overview

During the year ended December 31, 2012, the Company recorded income from operations of $24,002,000 on $89,337,000 revenue, as compared to a $362,000 operating loss on $86,018,000 revenue for the preceding year; and net income for the current year of $20,641,000 as compared to a net loss of $2,452,000 for the year ended December 31, 2011.

On November 16, 2012, Avcorp received the determination of an appointed arbitration panel constituted to adjudicate outstanding issues relating to cost reimbursements and compensation payable to Avcorp in connection with the transition of Cessna Aircraft Company (Cessna) production work back to Cessna and other suppliers. The transition of Cessna production work was first announced by the Company on December 17, 2010 and immediately following notification by Cessna, the Company had attempted to negotiate compensation payments as contemplated by the Cessna Strategic Alliance Agreement (SAA). Only when negotiations and mediation were unsuccessful did the Company refer the matter to binding arbitration.

The binding arbitration award, delivered to the Company on November 16, 2012, determined that: the SAA was an exclusive agreement between Cessna and Avcorp; Cessna could not unilaterally transition production work from Avcorp; Avcorp had fulfilled the requirements of the SAA; and, Avcorp suffered damages as a result of Cessna transitioning production work from Avcorp. In addition, all counterclaims that were advanced by Cessna were denied. The quantum of damages was assessed by the arbitration panel at $27,391,000, which amount was payable to Avcorp within thirty days of the arbitration award.

On November 26, 2012 Cessna filed a complaint in the United States District Court For The District Of Kansas seeking to vacate the award as a manifest disregard for the law and in violation of public policy.

On December 21, 2012 Avcorp filed a memorandum in support of a motion to confirm final arbitration award, dismiss complaint, and for prejudgement interest, attorney's fees and costs in the United States District Court For The District Of Kansas.

The Company intends to vigorously pursue the confirmation of the arbitration award and the dismissal of Cessna's motion to vacate with the U.S. District.

During the year-ended December 31, 2012, the Company incurred $5,963,000 (December 31, 2011: $315,000) in costs associated with this arbitration process and the customer contract termination.

Current year revenues have increased from the preceding year primarily as a result of significant increases in sales to The Boeing Company (Boeing) and BAE Systems (Operations) Limited (BAE), offset by the wind-down of Cessna programs. During the third quarter 2012, the Company renewed its long-term agreement with the Boeing Commercial Airplane Group (Boeing CA) which is forecasted to provide in excess of $83 million revenue over the next five years. Start-up and commencement of production deliveries for BAE Systems (Operations) Limited (BAE) F35 program has also contributed to an overall $146 million increase in order backlog during the current year.

However, there remains within operations significant levels of unutilized plant capacity. The Company has expensed $4,660,000 of overhead costs during the current year (December 31, 2011: $4,149,000) in respect of unutilized plant capacity. Further revenue growth would benefit Company profitability via a contribution to the recovery of fixed overhead expenditures.

The current year income includes a $193,000 foreign exchange loss resulting from holding foreign currency denominated cash, accounts receivable and payable; while the loss for the year ended December 31, 2011 included a $333,000 foreign exchange gain.

The Company recorded a $397,000 loss on repayment of certain debt (December 31, 2011: $Nil), as a non-cash charge against income resulting from the write-down of the fair value of warrants issued with the debt.

During 2012 the value of certain machinery, equipment, tooling, computer hardware and software was written down by $655,000 (December 31, 2011: $Nil). The equipment which was no longer in use had a cost of $9,220,000, and an accumulated depreciation of $8,565,000; resulting in a $655,000 charge against income.

On September 27, 2012, the Company secured a three year $12,000,000 operating line of credit in replacement of its three-month-term $4,500,000 operating line of credit. In doing so the Company reduced interest charges from prime plus 5.0% to prime plus 0.5%. The increased working capital financing availability will be used to fund future business growth. Concurrently, the Company repaid its $6,000,000 term loan thereby effectively lowering its cost of capital.

During the current year the Company increased its share capital by $2,966,000: via a $973,000 equity private placement for cash proceeds, a $1,771,000 equity conversion of debt into common shares, $218,000 in repayment of accrued interest by way of issuance of common shares, and a $4,000 equity issue in settlements of other obligations.

Cash flows from operating activities during the year ended December 31, 2012 utilized $3,603,000 of cash as compared to utilizing $924,000 of cash during the year ended December 31, 2011. The Company has a working capital surplus of $34,819,000 as at December 31, 2012 which has significantly increased from the December 31, 2011 $14,663,000 surplus, as a result of the binding arbitration award. The Company's accumulated deficit as at December 31, 2012 was $55,375,000 (December 31, 2011: $76,016,000).

Revenue

Revenue for the year ended December 31, 2012 was $89,337,000 as compared to $86,018,000 for the year ended December 31, 2011. Current year revenues have increased from the preceding year primarily as a result of significant increases in sales to Boeing and BAE offset by the wind-down of Cessna programs.

Revenues from the Company's customers are as follows.

REVENUE DISTRIBUTION

unaudited, prepared in accordance with IFRS, expressed in thousands of Canadian dollars

FOR THE YEAR ENDED DECEMBER 31	2012		2011	
	Revenue	**% of Total**	Revenue	% of Total
BAE Systems	**$ 15,193**	**17.0**	$ 3,666	4.2
Boeing	**29,961**	**33.6**	26,887	31.3
Bombardier	**16,784**	**18.8**	17,062	19.8
Cessna	**14,055**	**15.7**	25,883	30.1
Other	**13,344**	**14.9**	12,520	14.6
Total	**89,337**	**100.0**	86,018	100.0

During the year end December 31, 2012, the Company continued its deliveries of the F-35 Carrier Variant Outboard Wing (CV-OBW) for in-service operation. The CV-OBW is regarded as one of the most complex assemblies that the Canadian aerospace industry contributes to the F-35 program.

Avcorp secured the F-35 Outboard Wing contract in 2009, following a period of close collaboration with Industry Canada, BAE Systems and Lockheed Martin. Planning and rollout of manufacturing capabilities and quality systems occurred throughout 2010 with initial production beginning mid-2011.

Avcorp is the single source supplier for this critical assembly under contract with BAE, and delivered directly to Lockheed Martin. The Outboard Wing is the foldable portion of the wing on the carrier version of the F-35 aircraft. It allows for easier handling and storage of the aircraft on the aircraft-carrier's deck and hangers, while keeping its long-range and low-landing speed flight characteristics. The Outboard Wing has been successfully fitted onto the first production standard F-35 carrier version.

The $15,193,000 of revenues generated by the F35 program during 2012 reflects production and non-recurring program introduction revenue streams.

Shipments of large assemblies to Boeing Commercial Airplane Group (Boeing CA), primarily for the 737 commercial jet program, increased by 8% during 2012 relative to 2011; while deliveries of fabricated parts increased by 22%. The Company also delivered components to Boeing Defense, Space & Security (Boeing DSS) for the Chinook CH47 helicopter. This program produced revenues 42% higher in the current year than in 2011. The Company continues to work towards obtaining additional new contracts supporting Boeing commercial jet programs as well as Boeing DSS defense programs.

Revenues from Bombardier Aerospace (Bombardier) programs decreased slightly during the current year relative to the year ended December 31, 2011. Shipments of large assemblies increased by 11%, while deliveries of composite floor boards for the CRJ and Q400 aircraft fell significantly. The Company's primary source of revenues from Bombardier in 2012 will continue to be from components on the CL605 and CL850 business jets, and composite floor boards for the CRJ and Q400 aircraft programs.

Revenues from Cessna Aircraft Company (Cessna) decreased by $11,828,000 during the year ended December 31, 2012, relative to 2011. The primary sources of revenue from Cessna were from deliveries of components for the Citation Sovereign business jet, the Citation CJ3 business jet and the Citation CJ4 business jet. Cessna transitioned the production work from Avcorp during 2011 and 2012. An agreement with regard to the compensation and cost reimbursement in connection with the transition could not be reached, and the matter was referred to arbitration. Refer to 2012 and 2011 Results overview.

Revenues for Comtek increased by 17% during 2012 relative to 2011, as one-time sales of an OEM product were completed during 2012; composite repairs revenue for commercial aircraft grew during the year; while aftermarket product sales declined.

Gross Profit

Gross profit (revenue less cost of sales) for the year ended December 31, 2012 was 13.0% of revenue as compared to 13.5% of revenue for the year ended December 31, 2011.

Gross profit has decreased slightly during 2012 relative to the previous year (December 31, 2012: $11,615,000; December 31, 2011: $11,652,000) as a result of incurring $3,063,000 one-time cost of sales associated with the termination by Cessna of its contracts.

Year-on-year, fixed overhead costs incurred in support of operational capabilities, as well as quality and engineering systems expenditures, have become less significant relative to revenues as customer program deliveries increase. Increased revenues have contributed to absorbing fixed overhead expenses, however costs expensed as a result of idle plant capacity amounted to $4,660,000 during the current year (December 31, 2011: $4,149,000). The cost-revenue imbalance continued to be mitigated in 2012 by new program revenue growth from the BAE Systems F35 program, new composite product sales to an OEM, as well as increased customer demand for Boeing programs.

New program revenue growth will be the largest contributing factor to reducing the Company's cost structure and contributing towards offsetting idle capacity costs.

Administration and General Expenses

As a percentage of revenue, the administration and general expenses increased to 16.2% for the year ended December 31, 2012 from 13.2% for the year ended December 31, 2011. Year-on-year expenses increased by $3,147,000 primarily due to increased expenditures in support of contract terminations. During the year-ended December 31, 2012, the Company incurred $2,436,000 (December 31, 2011: $315,000) in legal, arbitration, and severance costs associated with the Cessna contract termination.

Foreign Exchange Gain or Loss

The Company recorded a $193,000 foreign exchange loss during 2012 (December 31, 2011: $333,000 gain) as a result of holding US dollar denominated receivables, payables and debt.

Earnings Before Interest, Taxes, Depreciation & Amortization

Earnings before interest, taxes, depreciation and amortization (EBITDA) was positive $29,035,000 for the year ended December 31, 2012 compared to a positive EBITDA of $3,847,000 for the year ended December 31, 2011. The increase in EBITDA was primarily as a result of a net of costs arbitration award amounting to $21,548,000.

EBITDA

unaudited, expressed in thousands of Canadian dollars

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Income (loss) for the period	**$ 20,641**	$ (2,452)
Interest expense and financing charges	**2,116**	2,423
Income tax expense	**-**	-
Depreciation	**3,012**	3,494
Amortization of development costs	**3,266**	382
	29,035	3,847

Interest and Financing Charges

Total interest and financing charges on both short- and long-term debt, some to related parties, for the year ended December 31, 2012 was $2,116,000 as compared to $2,423,000 for 2011. The decrease in interest and financing charges for 2012 is primarily as a result of the Company not utilizing its operating line of credit and having cash reserves on hand; as well as repaying and converting into equity $7,771,000 of interest bearing long-term debt during the third quarter 2012. Included within interest expense and financing charges for both years are $756,000 of preferred share dividends.

Income Taxes

The Company has not incurred a tax expense during the current year (December 31, 2011: $Nil).

Income or Loss

Income for the year ended December 31, 2012 was $20,641,000 as compared to a $2,452,000 loss for the year ended December 31, 2011.

On November 16, 2012, Avcorp received the determination of an appointed arbitration panel constituted to adjudicate outstanding issues relating to cost reimbursements and compensation payable to Avcorp in connection with the transition of Cessna production work back to Cessna and other suppliers. A binding arbitration award was delivered to the Company on November 16, 2012. The quantum of damages was assessed by an arbitration panel at $27,391,000. The arbitration award, net of associated costs, amounted to $21,548,000.

Liquidity and Capital Resources

The Company's operating line of credit provides for a total utilization of $12,000,000. As at December 31, 2012 the Company had drawn $2,122,000 on this debt facility offset by $2,597,000 cash compared to utilization of $Nil as at December 31, 2011. The Company's new banking agreement with a Canadian Chartered bank expires on September 27, 2015. The Company has net cash reserves on hand as at December 31, 2012 amounting to $475,000 (December 31, 2011: $3,778,000).

The Company has deferred and therefore not paid $3,024,000 of preferred share dividends which were accrued and payable as at December 31, 2012 (December 31, 2011: $2,268,000). From July 1, 2011, the Company's preferred shares having a $8,168,000 gross book value, and all accrued and unpaid dividends, became redeemable at the option of the holder in whole.

The Company's governing corporate statute is the Canada Business Corporations Act (the "CBCA"). Under the CBCA, the Company may not purchase or otherwise acquire its own shares, including redeeming the preferred shares, if there are reasonable grounds for believing that the Company would after the purchase be unable to pay its liabilities as they become due. The Company's board has determined that honouring any redemption request for preferred shares, regardless of the number of shares involved, would result in the Company being unable to pay its liabilities as they become due.

While the Company currently is able to meet its existing obligations, it is reliant on certain credit and loan facilities for the normal, ongoing operation of its business. Those operating facilities currently provide that it is an event of default if the Company redeems any of its preferred shares. The inability of the Company to access its customary operating facilities would impair the proper operation of the Company's business and prohibit it from meeting, in the normal course, its liabilities as they become due. Accordingly, at this time the Company is prohibited from completing any redemption of preferred shares or paying preferred share dividends.

Management is actively working to secure additional production orders, has completed loan financing and renegotiated debt repayments, will continue to work with existing common and preference shareholders, and will seek additional financing as necessary.

Cash Flows from Operating Activities

Net cash flows from operating activities utilized $3,603,000 of cash for the year ended December 31, 2012 compared to utilizing $924,000 of cash during the previous year.

The increase in cash utilization in 2012 from 2011 is primarily attributable to recognition of revenues which were funded in a previous period, offset by collection of accounts receivable and improved inventory turns. The Company continues to closely monitor accounts receivable in order to ensure cash is collected on a timely basis.

Cash Flows from Investing Activities

During the current year, the Company purchased capital assets totalling $557,000 as compared to $1,224,000 during the year ended December 31, 2011. The Company continues to minimize its capital expenditures in order to conserve cash, with only operation critical expenditures being made.

Additionally, the Company invested $1,071,000 during the current year (December 31, 2011: $1,337,000) in tooling and new program introduction. Current year expenditures primarily relate to investment in start-up costs for the Joint Strike Fighter F-35 military jet aircraft program. As noted below, this investment was fully funded by the customer.

Cash Flows from Financing Activities

The Company finances working capital through a combination of bank debt, equity financings and other financial instruments.

During the year ended December 31, 2012, the Company's cash on hand decreased by $1,181,000 (December 31, 2011: $3,778,000 increased). As at December 31, 2012 the Company had drawn $2,122,000 on its bank debt facility offset by $2,597,000 cash, compared to utilization of $Nil as at December 31, 2011.

Interest paid during the current year on current and long-term debt amounted to $1,144,000 (December 31, 2011: $1,128,000).

On September 28, 2012, the Company completed a private placement of 23,172,552 common shares at $0.042 per share for gross proceeds of approximately $973,000.

For the year ended December 31, 2012, proceeds from funding of program introduction and working capital amounted to $9,712,000 (December 31, 2011: $11,412,000).

Also during the current year, the Company repaid long term debt consisting of $882,000 of equipment financing (December 31, 2011: $863,000), as well as $731,000 of accrued government royalties and a $6,000,000 term loan.

On December 31, 2012, the ratio of the Company's current assets to current liabilities was 2.63:1 (December 31, 2011: 1.66:1), with the debt to equity ratio at 0.29:1 (December 31, 2011: 12.17:1).

Contractual Obligations

PAYMENTS DUE BY PERIOD

unaudited, prepared in accordance with IFRS, expressed in thousands of Canadian dollars

	Total	2013	2014-2016	2017-2018	Post 2018
Convertible debenture	**$ 4,392**	$ 354	$ 4,038	$ -	$ -
Capital lease obligation	**208**	80	128	-	-
Purchase obligation[1]	**28,880**	17,355	7,339	3,766	420
Other long-term obligations[2]	**392**	258	134	-	-
Total contractual obligations	**33,872**	18,047	11,639	3,766	420

1. Purchase obligations include payments for the Company's operating and property leases, as well as committed contractual operational purchase order obligations outstanding.
2. This amount represents obligations the Company has with Industrial Technologies Office.

The Company expects that payment of contractual obligations will come from funds generated by operations, utilization of the bank operating line of credit and proceeds from debt and equity financings.

The Company does not have any off-balance sheet liabilities or transactions that are not recorded or disclosed in the financial statements.

Capital Stock

On January 10, 2012, the Company completed a private placement of 1,173,126 common shares in consideration of \$55,000 interest accrued to December 31, 2011 on the Export Development Canada convertible debenture.

On February 6, 2012, the Company completed a private placement of 1,150,395 common shares in consideration of \$55,000 interest accrued to December 31, 2011 on the Export Development Canada convertible debenture.

On April 4, 2012, the Company completed a private placement of 107,575 common shares in consideration of a \$4,000 payment to the former principal shareholders of Comtek Advanced Structures Ltd., under the terms of a Share Purchase Agreement.

On April 20, 2012, the Company completed a private placement of 1,008,142 common shares in consideration of \$54,000 interest accrued to March 31, 2012 on the Export Development Canada convertible debenture.

On September 21, 2012, the Company completed a private placement of 992,169 common shares in consideration of \$54,000 interest accrued to June 30, 2012 on the Export Development Canada convertible debenture.

On September 27, 2012, the Company issued 25,300,000 common shares at \$0.07 per share for a book value of \$1,771,000, pursuant to the terms of a loan agreement entered into between the Company and Panta Canada B.V. on April 16, 2010.

On September 28, 2012, the Company completed a private placement of 23,172,552 common shares at \$0.042 per share for gross proceeds of approximately \$973,000. The subscriber in the private placement was Panta Canada B.V.

Prior to December 31, 2008, holders of preferred shares converted 383,200 preferred shares resulting in 816,800 preferred shares remaining having a \$8,168,000 gross book value, which net of \$546,000 issuance costs results in a \$7,622,000 net book value.

The preferred shares provide for a 9.25% per annum dividend, payable quarterly in cash on the last day of March, June, September and December. Dividend payments have been deferred since January 2009. Unpaid dividends as at December 31, 2012 amounted to \$3,024,000 (December 31, 2011: \$2,268,000).

Each preferred share is convertible at any time, without the payment of additional consideration, at the option of the holder into 3.64 common shares, at a conversion price of \$2.75 per common share.

At any time after June 30, 2011, the preferred shares are redeemable in whole or in part at the option of the holder.

The Company's governing corporate statute is the Canada Business Corporations Act (the "CBCA"). Under the CBCA, the Company may not purchase or otherwise acquire its own shares, including redeeming the preferred shares, if there are reasonable grounds for believing that the Company would after the purchase be unable to pay its liabilities as they become due. The Company's board has determined that honouring any redemption request for preferred shares, regardless of the number of shares involved, would result in the Company being unable to pay its liabilities as they become due.

While the Company currently is able to meet its existing obligations, it is reliant on certain credit and loan facilities for the normal, ongoing operation of its business. Those operating facilities currently provide that it is an event of default if the Company redeems any of its preferred shares. The inability of the Company to access its customary operating facilities would impair the proper operation of the Company's business and prohibit it from meeting, in the normal course, its liabilities as they become due. Accordingly, at this time the Company is prohibited from completing any redemption of preferred shares or paying preferred share dividends.

The Company is authorized to issue an unlimited number of common shares as well as an unlimited number of first preferred and second preferred shares, issuable in series, the terms of which will be determined by the Company's directors at the time of creation of each series. There were 254,898,072 common shares issued and 21,688,720 reserved for issuance at December 31, 2012 pursuant to a convertible debenture. The book value of common shares issued and outstanding as at December 31, 2012 was \$79,962,000 (December 31, 2011: \$77,128,000).

As at March 25, 2013, there were 254,898,072 common shares, 816,800 preference shares, and 11,266,000 stock options issued and outstanding.

Accounting Standards Issued But Not Yet Applied

The following is a brief summary of the new standards:

IFRS 9 – Financial Instruments

IFRS 9 was issued in November 2009. It addresses classification and measurement of financial assets and replaces the multiple category and measurement models in IAS 39 for debt instruments with a new mixed measurement model having only two categories: Amortized cost and fair value through profit or loss. IFRS 9 also replaces the models for measuring equity instruments and such instruments are either recognized at fair value through profit or loss or at fair value through other comprehensive income. Where such equity instruments are measured at fair value through other comprehensive income, dividends, to the extent not clearly representing a return of investment, are recognized in profit or loss; however, other gains and losses (including impairments) associated with such instruments remain in accumulated comprehensive income indefinitely. This standard is required to be applied for accounting periods beginning on or after January 1, 2015, with earlier adoption permitted. The Company has not yet assessed the impact of the standard or determined whether it will adopt the standard early.

IFRS 10 – Consolidation

IFRS 10 requires an entity to consolidate an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Under existing IFRS, consolidation is required when an entity has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. IFRS 10 replaces SIC-12 Consolidation–Special Purpose Entities and parts of IAS 27 Consolidated and Separate Financial Statements.

IFRS 11 – Joint Arrangements

IFRS 11 requires a venturer to classify its interest in a joint arrangement as a joint venture or joint operation. Joint ventures will be accounted for using the equity method of accounting whereas for a joint operation the venturer will recognize its share of the assets, liabilities, revenue and expenses of the joint operation. Under existing IFRS, entities have the choice to proportionately consolidate or equity account for interests in joint ventures. IFRS 11 supersedes IAS 31, Interests in Joint Ventures, and SIC-13, Jointly Controlled Entities-Non-monetary Contributions by Venturers.

IFRS 12 – Disclosure of Interests in Other Entities

IFRS 12 establishes disclosure requirements for interests in other entities, such as joint arrangements, associates, special purpose vehicles and off balance sheet vehicles. The standard carries forward existing disclosures and also introduces significant additional disclosure requirements that address the nature of, and risks associated with, an entity's interests in other entities.

IFRS 13 – Fair Value Measurement

IFRS 13 is a comprehensive standard for fair value measurement and disclosure requirements for use across IFRS standards. The new standard clarifies that fair value is the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants, at the measurement date. It also establishes disclosures about fair value measurement. Under existing IFRS, guidance on measuring and disclosing fair value is dispersed among the specific standards requiring fair value measurements and in many cases does not reflect a clear measurement basis or consistent disclosures.

IFRS 10, 11, 12 and 13 are effective for annual periods beginning on or after April 1, 2013, with early adoption permitted. The Company has yet to assess the impact of these new standards.

Amendments to Other Standards

In addition, there have been amendments to existing standards, including IAS 27, Separate Financial Statements (IAS 27), and IAS 28, Investments in Associates and Joint Ventures (IAS 28). IAS 27 addresses accounting for subsidiaries, jointly controlled entities and associates in non-consolidated financial statements. IAS 28 has been amended to include joint ventures in its scope and to address the changes in IFRS 10-13.

The standard setting bodies that determine IFRS have significant ongoing projects that could impact the IFRS accounting policies selected. The Company has processes in effect to ensure that potential IFRS accounting policy changes are monitored and evaluated. The impact of any new IFRS and IFRIC Interpretations will be evaluated as they are drafted and published.

Operations Overview

Delivery and Quality Performance

Deliveries and quality performance as at December 31, 2012 were at planned levels for BAE Systems, Boeing and Bombardier programs. The Company has achieved top quality and delivery ratings for the majority of its programs.

Order Backlog

The Company operates within "general terms agreements" with its customers. These agreements are typically for five years or longer. The Company's agreements with Boeing Commercial Airplane Group extend from January 2013 to December 2017 and with Boeing Defense, Space and Security extend into 2014 on a purchase order basis. During the current year the Company's agreements with Boeing CA were renewed and extended to December 2017, generating in excess of $83 million of sales order backlog. Agreements with BAE Systems (Operations) Limited (BAE) extend to March 2014 and continue to generate additional sales order backlog. The Bombardier agreements extend for the life of the individual aircraft programs. Cessna agreements were terminated before the end of the current year.

The Company defines order backlog as the value of purchase orders it expects to receive from these agreements based on manufacturers' projections and current degrees of exclusivity. The order backlog, as at December 31, 2012, is $214 million, ($67 million of which pertains to 2013), compared to $159 million as at December 31, 2011. The changes in order backlog are as follows:

- $89 million decrease in order backlog resulting from revenues recorded during the year ended December 31, 2012;
- $146 million increase in order backlog due to increases in the production rates and contract renewals for various existing programs; and
- $2 million decrease in order backlog resulting from change in the value of the Canadian dollar relative to the US dollar for the Company's US dollar denominated sales. Refer to comments on currency risk.

Supply Chain

Supplier quality and delivery performance met targeted levels during the year; the Company continues to monitor supplier performance in all aspects of quality, delivery and price. The Company will continue to work closely with its supply chain to ensure a stable, uninterrupted delivery of compliant products and is making changes in product sourcing processes where necessary.

The capacity and delivery performance of a limited number of critical vendors continues to be closely monitored to mitigate risks to assembly start dates. Risk mitigation plans have been implemented. The securing of additional long-term contracts with key suppliers continues. The Company continues with the process of setting up a comprehensive supply chain for the Joint Strike Fighter F-35 military jet aircraft program.

Working Capital Utilization

Total current assets less total current liabilities were in a surplus position of $34,819,000 at December 31, 2012 and $14,663,000 at December 31, 2011. The change in working capital during 2012 was primarily due to a decrease in accounts receivable and inventories resulting from the cessation of Cessna production programs, as well as a reduction of cash resulting from repayment of debt during the current year; offset by a receivable related to an arbitration award.

Financial Resources

The Company has invested in its chosen strategies of organic growth, lean manufacturing and strategic sourcing. Management believes that significant investments necessary to better position the Company in the aerospace industry have and continue to be made, and that those investments along with the expected continued financial support of shareholders and lenders position the Company to be able to face and mitigate risks associated with the business.

Non-Financial Resources

The Company's non-financial resources relate to the Company's human resources, operating equipment, systems, technologies and processes. The Company does not have any extended enterprise relationships such as special purpose entities or joint ventures.

Human Resources

The Company has the appropriate human resources at all levels of the organization. The board of directors has considerable aerospace industry, investment, and financial expertise. The management team is experienced in the industry and in all aspects of operations.

The number of employees at December 31, 2012 was 476 (December 31, 2011: 550). Employees have appropriate qualifications and experience to perform their duties and the Company provides ongoing training and opportunities for employee growth.

Equipment, Systems, Technologies and Processes

Manufacturing equipment and information technology assets have been consistently upgraded and further deployed, increasing reliability and utility.

Risk Assessment

The principal risks that the Company faces are summarized as follows:

- additional financing is required to maintain its business;
- no agreement on extension of customer contracts;
- increases in material costs, primarily aluminum plate, titanium, sandwich panels and assembly hardware, and subcontractor costs, without equivalent price protection in customer contracts;
- reduction in production rates of aircraft manufacturers and delays in program introduction;
- consolidation and globalization by competitors;
- potential failure to achieve cost-reduction objectives relative to revenue growth;
- the trend to greater use of composite material in primary structures in each new generation of aircraft; and
- increases in the value of the Canadian dollar, relative to the US dollar, has an adverse effect on the Canadian dollar equivalent value of the Company's revenues which are denominated in US dollars.

The Company's view is that with the refinancing completed and in process, the continued integration of composite design and manufacturing capabilities, and a strategic plan in place the Company should be in a position to face and mitigate these risks. However, there can be no assurance that the Company will be successful with all initiatives.

Additional Financing

The Company's growth strategy requires continued access to capital. From time to time, the Company may require additional financing to enable it to:

- finance unanticipated working capital requirements;
- finance new program development and introduction;

- develop or enhance existing services and capabilities; or
- respond to competitive pressures.

The Company cannot provide assurance that, if it needs to raise additional funds, such funds will be available on favourable terms, or at all. If the Company cannot raise adequate funds on acceptable terms, its business could be materially harmed.

Also certain financing agreements are due for repayment under certain conditions:

The Company has deferred and therefore not paid $3,024,000 of preferred share dividends which were accrued and payable as at December 31, 2012 (December 31, 2011: $2,268,000). At any time after June 30, 2011, the Company's preferred shares having an $8,168,000 gross book value, and all accrued and unpaid dividends are redeemable at the option of the holder in whole.

Customer Contracts

The Company is exposed to the risk that existing customer fixed-term contracts are not renewed at expiration date. The Company's agreements with Boeing CA have been renewed and extend from January 2013 to December 2017. Agreements with Boeing DSS are purchase order to purchase order based, currently extending into 2014. Renewal and awarding of new Boeing contracts has been supported by a performance guarantee provided by a significant shareholder.

BAE customer contracts extend to March 2014. The Company is currently negotiating the extension of these contracts.

Procured Materials and Parts

Delivery of the First Article Inspection parts and components for the Joint Strike Fighter F-35 program successfully met the Companies internal target dates. The Company is working closely with its suppliers to ensure capacity and material availability to meet rate increases on a number of commercial and military programs in 2012.

In addition, affordability projects were initiated in the third quarter 2011 with customers' participation to ensure ongoing cost reductions within the supply chain.

The Company is engaging suppliers and customers to properly align requirements, ensuring uninterrupted delivery of compliant products. Changes in forecasts are closely monitored in order to promptly adjust procured materials and parts quantities with the objective of limiting unwanted inventory build-up.

Aircraft Production Rates

The following industry and program trends impact the Company.

- Company research indicated that the aerostructures markets for commercial aircraft and business jets would continue to grow in 2012. This research also indicates that growth in this market continues into 2013 and beyond.
- Growth in air travel rates has and will further increase production rates on the Boeing 737 and Airbus A320 platforms in the coming years. The regional Aircraft market remains soft around current rates.
- Bombardier Challenger 850 and the Challenger 605 business jet aircraft production remained flat in 2012 relative to 2011; however rates of production are expected to increase in 2013.
- The market for defence aircraft was also expected to continue to grow in 2012 and into 2013 albeit at a slower pace due to general global budget challenges and the gradual decrease of Western allies' involvement in Afghanistan.

  The F35 remains on a global scale one of the largest Defense Airplane programs for the foreseeable future.

  However, under the current North American Federal Governments' initiatives of cost controls regarding defense spending, there exists a risk that the customer demand for defence aircraft components is reduced or delayed.

- Offset opportunities created by Canadian Government procurement within military aerospace programs exist to provide additional revenue from this aerospace sector.

Competitors

Despite the current economic conditions, the long-term trend continues towards more intense competition from larger entities having operations in Asia, Mexico and Europe; while original equipment manufacturers (OEM) continue to increase the size and amount of outsourced components. It can be expected that consolidation on Tier 1 and Tier 2 levels will continue to take place. The Company continues to examine opportunities for mergers or acquisitions, on a global basis, that would improve competitiveness and acquire vertical strengths or additional strategic capabilities.

Cost Reductions

Approximately 55% of the Company's cost of sales is related to labour and overhead and 45% related to procurement of raw materials and finished parts. The Company's wage rates are generally lower than its Western European and US competitors and higher than those in Asia, Eastern Europe and Mexico. The Company negotiated a 3 year collective agreement with its labour force which came into effect on April 1, 2010 and will expire on March 31, 2013.

The Company continues to focus on cost reductions for direct labour, material and overhead costs. These cost reductions will be achieved through continuous improvements in the internal and external parts supply chain using lean manufacturing technology, through continued negotiation of long-term agreements for the majority of key suppliers, through increased efficiency of plant capacity augmented by technological improvements, and through continued focus on cost targets at all levels of the organization. All discretionary spending is being reviewed and controlled by senior management, with expenditures focused on expediting new commercial program business growth and launching of long-term defence programs. However, fixed overhead costs continue to have an adverse impact on the Company's cost structure during this period of reduced revenues. This will be mitigated by increased revenue and facility utilization.

Composite Materials

Through its subsidiary Comtek, the Company has ongoing operations expertise in the design and competitive manufacture and repair of advanced composite aerostructures which provides the opportunity for the Company to compete in a market which is trending, with each new generation of aircraft, to greater use of composite material in primary structures.

US Dollar Revenues

The Company sells a significant proportion of its products in US dollars at prices which are often established well in advance of manufacture and shipment dates. As the value of the Canadian dollar strengthens, the equivalent value of US dollar denominated revenues decreases. The Company is commencing to structure new agreements with customers which mitigate the risk associated with currency fluctuations.

Outlook

Variability of the Canadian dollar relative to the US dollar will continue to cause the value of the Company's current order backlog to fluctuate. The Company continues to work towards securing additional defence programs in order to augment and diversify its backlog. The Company began delivering products under its military contracts in 2009 and is currently negotiating long-term supply agreements. Assuming long-term agreements are secured, the Company believes that revenues from its military customers will increase to 2013 and extend past 2020. The Company expects to primarily finance investment in the start-up of new military defence programs with milestone payments from customers, though this cannot be assured. Boeing will be the Company's largest customer in 2013, followed by BAE Systems and Bombardier.

The Company forecasts its 2013 revenues to maintain the levels achieved in 2011 and 2012. With the exception of capital expenditures required for new programs and information technology infrastructure upgrades, the Company's investment in new equipment will be maintained at 2012 amounts.

The Company has deferred and therefore not paid $3,024,000 of preferred share dividends which were accrued and payable as at December 31, 2012 (December 31, 2011: $2,268,000). At any time after June 30, 2011, the Company's preferred shares having a $8,168,000 gross book value, and all accrued and unpaid dividends, are redeemable at the option of the holder in whole.

The Company forecasts its financing requirements for 2013 to be met by the current availability of the operating line of credit. However, further debt and equity financing may be required.

Transactions with Related Parties

During the current year a performance guarantee was provided by a certain shareholder and director on production contracts with a certain customer. Fees paid to a certain shareholder and director during the year ended December 31, 2012 amounted to $38,000 (December 31, 2011: $Nil). Fees payable to a certain shareholder and director as at December 31, 2012 are $17,000 (December 31, 2011: $Nil). These fees are included in the Statements of Operations as cost of sales and amount to $55,000 for the year ended December 31, 2012 (December 31, 2011: $Nil).

During the year ended December 31, 2012, consulting services were provided by certain directors. Fees paid to certain directors, or companies with which they have beneficial ownership, during the year ended December 31, 2012 amounted to $62,000 (December 31, 2011: $80,000). Fees payable to certain directors or Companies with which they have beneficial ownership, as at December 31, 2012 are $14,000 (December 31, 2011: $Nil). These fees are included in the Statements of Income and Comprehensive Income as administrative and general expenses and amount to $76,000 for the year ended December 31, 2012 (December 31, 2011: $78,000).

Fourth Quarter

The following summarizes financial results for the fourth quarter 2012.

Operating income for the fourth quarter of 2012 was $24,177,000 from $19,815,000 in revenues, as compared to operating income of $1,093,000 from $24,227,000 in revenues for the quarter ended December 31, 2011. The major contributing cause increasing operating income for the fourth quarter of 2012 was on November 16, 2012 Avcorp received the determination of an appointed arbitration panel constituted to adjudicate outstanding issues relating to cost reimbursements and compensation payable to Avcorp in connection with the transition of Cessna production work back to Cessna and other suppliers.

The binding arbitration award was delivered to the Company on November 16, 2012. The quantum of damages was assessed by an arbitration panel at $27,391,000. The arbitration award, net of associated costs, amounted to $21,548,000.

Proposed Transactions

As at the date of this report, no agreements to merge with or acquire another entity have been entered into, other than as disclosed elsewhere in the accompanying financial statements.

Critical Accounting Estimates and Judgement

The preparation of financial statements in conformity with IFRS requires management to make estimates and judgments that affect the amounts which are reported in the consolidated financial statements during the reporting period. Estimates and other judgments are evaluated at each reporting date and are based on management's experience and other factors, including expectations about future events that are believed to be reasonable under the circumstances.

- Management assesses the Company's ability to continue as a going concern at each reporting date, using all quantitative and qualitative information available. This assessment, by its nature, relies on estimates of future cash flows and other future events, whose subsequent changes would materially impact the validity of such an assessment.
- Carrying value of long-lived assets: The Company holds property, plant and equipment, on the balance sheet amounting to $9,633,000 (December 31, 2011: $12,523,000). Reduction in market demand during 2009 for business jet aircraft has resulted in negative operating cash flows during the subsequent years. The recoverability of these assets is dependent on the ability of the company to generate sufficient cash flow from operations over the remaining useful life of the assets, which is contingent on, amongst other factors, the ability of the Company to replace known program losses with new programs as well as ramping up scheduled production for new defence contracts. The recoverability of

the carrying value of these assets is, in part, dependent on the estimates used in determining the expected period of future benefits over which to amortize. In addition, such recoverability is dependent on delivering to the scheduled production ramp-up for new defence programs, as well as dependent on market conditions including demand for such aircraft for which the Company provides its products.

- During 2012 the value of certain machinery, equipment, tooling, computer hardware and software was written down by $655,000 (December 31, 2011: $Nil). The equipment which was no longer in use had a cost of $9,220,000, and an accumulated depreciation of $8,565,000; resulting in a $655,000 charge against income. A portion of this write-down was specifically related to the Cessna production contract termination. The transition of production work back to Cessna was completed in 2012. Accordingly, Cessna program related equipment was written off having a cost of $6,643,000 and an accumulated depreciation of $6,179,000; resulting in a $464,000 charge against income.
- Recoverability of deferred tooling costs: The ability to defer tooling costs is dependent on the future recoverability of the amounts from cash flows generated by the related commercial operations as well as contractually required payments by customers. If operations perform below anticipated recoverable levels, the portion of deferred tooling costs that cannot be recovered is expensed immediately when known. At December 31, 2012, $2,718,000 (December 31, 2011: $5,540,000) in unamortized deferred tooling costs, which are expected to be recoverable from the related future cash flows of operations resulting from continued customer orders or recovery of cash from customers for deferred amounts, are presented as Development Costs in the balance sheet. $587,000 (December 31, 2011: $3,007,000) of deferred tooling costs are not supported by customer advances.
- On a periodic basis the Company provides for its anticipated losses under existing contractual commitments to its customers by comparing its anticipated future costs of production to its contracted future revenues. The December 31, 2012 provision for anticipated losses was $Nil (December 31, 2011: $189,000). The decrease in this provision from December 31, 2011 was primarily as a result of the curtailment of a loss-making program, improvements in certain other program gross margins as well as a reduction in associated anticipated number of aircraft components to be delivered.
- On a periodic basis the Company reviews its plant capacity and estimates the portion of its under-utilized overhead expenditures. The Company has expensed $4,660,000 of overhead costs during the current year (December 31, 2011: $4,149,000) in respect of unutilized plant capacity.
- Warranty provisions are provided for when an actual deficiency is identified, and through working with the customer it is estimated based on the expected cost per unit over the number of units affected. During previous years, the Company provisioned for $85,000 of expected warranty expenditures relating to a manufacturing deficiency. All rectifications have not been completed by the date of this report, and $85,000 remains provisioned for expected future expenditures.
- Deferred program revenues are recognized as revenue straight-line on units-of-production basis over the expected life of the program; where expected life is an estimate based on customer and industry data.
- Other receivable is based on a binding arbitration award under which a quantum of damages was assessed and a period for payment was established.

Financial Instruments and Other Instruments

Interest rate risk

The Company is exposed to interest rate risk on the utilized portion of its operating line of credit at rates of bank prime plus 0.5%. The maximum operating line of credit availability is $12,000,000 of which $2,122,000 is utilized as at December 31, 2012 (December 31, 2011: $Nil). The Company lowers interest rate costs by managing utilization of the operating lines of credit to the lowest amount practical. For the year ended December 31, 2012, with other variables unchanged, a 1% change in the bank prime interest rate would have a $21,000 (December 31, 2011: $Nil) impact on net earnings and cash flow.

The Company primarily finances the purchase of long-lived assets at fixed interest rates.

Currency risk

The Company sells a significant proportion of its products in US dollars at prices which are often established well in advance of manufacture and shipment dates. In addition, the Company purchases a significant proportion of its raw materials in US dollars at prices that are usually established at the order date. All of the Company's operations are based in Canada. As a result of this, the Company is exposed to currency risk to the extent that fluctuations in exchange rates are experienced. The amount of foreign exchange loss recorded in 2012 was $193,000 as compared to a $333,000 gain for the year ended December 31, 2011.

The Company had the following US dollar denominated balances:

FOR THE YEAR ENDED DECEMBER 31	**2012**	2011
Bank cash position	**$ 2,197**	$ 4,598
Accounts receivable	**2,934**	6,041
Accounts payable net of prepayments	**1,329**	2,664
Long-term debt	**-**	713

With other variables unchanged, each $0.10 strengthening (weakening) of the US dollar against the Canadian dollar would result in an increase (decrease) of approximately $380,000 in net earnings for the year ended December 31, 2012 (December 31, 2011: $726,000 increase (decrease) in net earnings) as a result of holding a US dollar net asset position.

Credit Risk

Credit risk is the risk of a financial loss to the Company if a customer or counter-party to a financial instrument fails to meet its contractual obligation. The Company manages credit risk for trade and other receivables through a financial review of the credit worthiness of the prospective customer along with credit monitoring activities. The majority of the Company's trade receivables reside with Boeing Commercial Airplane Group (Boeing), Boeing Defense, Space & Security (BDS), Bombardier Aerospace (Bombardier), BAE Systems (Operations) Limited (BAE) and Cessna Aircraft Company (Cessna). During 2012 and 2011, there were no trade receivables written off by the Company in respect of these customers. The maximum exposure to credit risk is represented by the amount of accounts receivable in the balance sheet.

As at the balance sheet date 73.1% (December 31, 2011: 81.7%) of the Company's trade accounts receivable are attributable to these customers.

Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company seeks to manage liquidity risk through the management of its capital structure and financial leverage as outlined in the Liquidity and Capital Resource discussions.

Other Items

Disclosure Controls and Procedures, and Internal Controls over Financial Reporting

In accordance with the Canadian Securities Administrators Multilateral Instrument 52-109, the Company has filed certificates signed by the Chief Executive Officer and the Head Financial Officer that, among other things, report on the design of disclosure controls and procedures and the design of internal control over financial reporting. These certificates can be found on www.sedar.com.

The Chief Executive Officer and the Vice President, Finance, have evaluated the Company's disclosure controls and procedures, and internal controls over financial reporting, as of December 31, 2012 and concluded that the Company's current disclosure controls and procedures as well as the internal controls over financial reporting are effective. There were therefore no changes to the Company's disclosure controls and procedures, or in the design of internal controls over financial reporting, during the year ended December 31, 2012, that have materially affected, or are reasonably likely to materially affect the Company's internal controls over financial reporting.

Forward Looking Statements

This management discussion and analysis should be read in conjunction with the Company's audited financial statements. Certain statements in this report and other oral and written statements made by the Company from time to time are forward-looking statements, including those that discuss strategies, goals, outlook or other non-historical matters; or projected revenues, income, returns or other financial measures. These forward-looking statements are subject to risks and uncertainties that may cause actual results to differ materially from those contained in the statements, including the following: (a) the ability of the Company to renegotiate its debt agreements under which it is in default; (b) the extent to which the Company is able to achieve savings from its restructuring plans; (c) uncertainty in estimating the amount and timing of restructuring charges and related costs; (d) changes in worldwide economic and political conditions that impact interest and foreign exchange rates; (e) the occurrence of work stoppages and strikes at key facilities of the Company or the Company's customers or suppliers; (f) government funding and program approvals affecting products being developed or sold under government programs; (g) cost and delivery performance under various program and development contracts; (h) the adequacy of cost estimates for various customer care programs including servicing warranties; (i) the ability to control costs and successful implementation of various cost reduction programs; (j) the timing of certifications of new aircraft products; (k) the occurrence of further downturns in customer markets to which the Company products are sold or supplied or where the Company offers financing; (l) changes in aircraft delivery schedules or cancellation of orders; (m) the Company's ability to offset, through cost reductions, raw material price increases and pricing pressure brought by original equipment manufacturer customers; (n) the availability and cost of insurance; (o) the Company's ability to maintain portfolio credit quality; (p) the Company's access to debt financing at competitive rates; and (q) uncertainty in estimating contingent liabilities and establishing reserves tailored to address such contingencies.

report of **management**

The accompanying financial statements of Avcorp Industries Inc. and all other information contained in the Management Discussion and Analysis are the responsibility of management. The financial statements were prepared in conformity with International Financial Reporting Standards (IFRS) appropriate in the circumstances, in a manner consistent with the previous year, and include some amounts based on management's best judgments and estimates. The financial information contained elsewhere in this Management Report and Analysis is consistent with that in the financial statements.

Management is responsible for maintaining a system of internal accounting controls and procedures to provide reasonable assurance. As of the end of the period covered by this report, the system of internal control provides reasonable assurance regarding the reliability of financial reporting and preparation of financial statements for external purposes in accordance with IFRS. During the period covered by this report, there has been no change in internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the issuer’s internal control over financial reporting.

	EDWARD M. MERLO Vice President, Finance and Corporate Secretary		**MARK VAN ROOIJ** President and Chief Executive Officer

report of **auditors**

Independent auditors' report to the Shareholders of Avcorp Industries Inc.

To the Shareholders of Avcorp Industries Inc.

We have audited the accompanying consolidated financial statements of Avcorp Industries Inc., which comprise the consolidated statement of financial position as at December 31, 2012, and the consolidated statement of income and comprehensive income, consolidated statement of changes in equity and cash flows for the year then ended, and a summary of significant accounting policies and other explanatory information.

Management's responsibility for the financial statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audit. We conducted our audit in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements or preparation of financial statements that give a true and fair view in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Avcorp Industries Inc. as at December 31, 2012, and of its financial performance and its cash flows for the year then ended in accordance with International Financial Reporting Standards.

Other matter

The consolidated financial statements of Avcorp Industries Inc. for the year ended December 31, 2011, were audited by another auditor who expressed an unmodified opinion with a going concern emphasis of matter paragraph on those statements on March 28, 2012.

Ernst & Young LLP	**ERNST & YOUNG LLP** Chartered Accountants

Vancouver, British Columbia
March 25, 2013

CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(prepared in accordance with IFRS, expressed in thousands of Canadian dollars)

AS AT DECEMBER 31	2012	2011
ASSETS		
Current assets		
Cash (note 12)	**$ 2,597**	$ 3,778
Accounts receivable (note 8)	**7,944**	12,160
Inventories (notes 9 and 28)	**16,572**	19,418
Prepayments and other assets	**1,634**	1,396
Other receivable (note 28)	**27,391**	-
	56,138	36,752
Non-current assets		
Prepaid rent (note 15)	**146**	146
Development costs (notes 10 and 28)	**2,718**	5,540
Property, plant and equipment, net (notes 11 and 28)	**9,633**	12,523
Total assets	**68,635**	54,961
LIABILITIES AND EQUITY		
Current liabilities		
Bank indebtedness (note 12)	**2,122**	-
Accounts payable and accrued liabilities (note 13)	**7,859**	10,694
Current portion of long-term debt (note 16)	**692**	1,505
Preferred shares (note 19)	**10,646**	9,890
	21,319	22,089
Non-current liabilities		
Deferred gain (note 15)	**263**	311
Lease inducement (note 15)	**567**	666
Deferred program revenues (note 14)	**17,514**	18,671
Long-term debt (note 16)	**4,300**	12,027
Warranty provisions (note 24)	**85**	85
	44,048	53,849
Equity		
Capital stock (note 18)	**76,423**	73,251
Equity component of convertible loan (note 16d)	**-**	453
Contributed surplus (note 18k)	**3,539**	3,424
Deficit	**(55,375)**	(76,016)
	24,587	1,112
Total liabilities and equity	**68,635**	54,961

Nature of operations (note 1)
Critical accounting estimates and judgements (note 4)
Obligations and commitments under capital and operating leases (note 17)

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

Approved by the Board of Directors on March 25, 2013

David Levi
Chairman

Eric Kohn TD
Committee Chair,
Audit & Corporate Governance Committee

CONSOLIDATED STATEMENTS OF INCOME (LOSS) AND COMPREHENSIVE INCOME (LOSS)

(prepared in accordance with IFRS, expressed in thousands of Canadian dollars, except number of shares and per share amounts)

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Revenues (note 28)	**$ 89,337**	$ 86,018
Cost of sales (note 28)	**77,722**	74,366
Gross profit	**11,615**	11,652
Administrative and general expenses (note 28)	**14,517**	11,370
Office equipment depreciation	**487**	644
Other operating income (note 28)	**(27,391)**	-
Operating Income (loss)	**24,002**	(362)
Foreign exchange (gain) loss	**193**	(333)
Finance costs (note 22)	**2,116**	2,423
Loss on repayment of debt (note 16e)	**397**	-
Income (loss) before income tax	**21,296**	(2,452)
Write-down of equipment (notes 11 and 28)	**655**	-
Income tax expense (note 25)	**-**	-
Income (loss) and total comprehensive income (loss) for the period	**20,641**	(2,452)
Earnings (loss) per share:		
Basic earnings (loss) per common share (note 29)	**0.09**	(0.01)
Diluted earnings (loss) per common share (note 29)	**0.09**	(0.01)
Basic weighted average number of shares outstanding (000's) (note 29)	**217,775**	197,959
Diluted weighted average number of shares outstanding (000's) (note 29)	**218,084**	197,959

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

CONSOLIDATED STATEMENTS OF CASH FLOWS

(prepared in accordance with IFRS, expressed in thousands of Canadian dollars)

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Cash flows from (used in) operating activities		
Profit (loss) before tax	**$ 20,641**	$ (2,452)
Adjustment for items not affecting cash:		
Accretion on convertible loan	**67**	85
Accrued interest and government royalties	**1,161**	1,583
Depreciation	**3,012**	3,494
Deferred tooling revenue amortization and reclassification to revenue	**(11,576)**	(2,421)
Development cost amortization and write-off	**3,893**	978
Fair value of warrants amortization	**132**	88
Loss on repayment of debt	**397**	-
Preferred share dividends accrued	**756**	756
Provision for loss-making contracts	**(189)**	(689)
Provision for obsolete inventory	**(67)**	(226)
Stock based compensation	**115**	145
Write-down of equipment	**655**	-
Other items	**(122)**	(205)
	18,875	1,136
Changes in non-cash working capital		
Accounts receivable	**4,908**	(414)
Inventories	**3,102**	(3,617)
Prepayments and other assets	**(244)**	413
Other receivable	**(27,391)**	-
Accounts payable and accrued liabilities	**(2,853)**	1,558
Net cash from (used in) operating activities	**(3,603)**	(924)
Cash flows from (used in) investing activities		
Purchase of equipment	**(557)**	(1,224)
Payments relating to development costs and tooling	**(1,071)**	(1,337)
Net cash from (used in) investing activities	**(1,628)**	(2,561)
Cash flows from financing activities		
Increase (decrease) in bank indebtedness	**2,122**	(8,158)
Payment of interest	**(1,144)**	(1,128)
Proceeds from issuance of common shares	**973**	-
Proceeds from customer funding of program introduction	**9,712**	11,412
Proceeds from current and long-term debt	**-**	6,000
Repayment of current and long-term debt	**(6,882)**	(863)
Repayment of government royalties	**(731)**	-
Net cash from financing activities	**4,050**	7,263
Net increase (decrease) in cash	**(1,181)**	3,778
Cash - Beginning of year	**3,778**	-
Cash - End of year	**2,597**	3,778

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

CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(prepared in accordance with IFRS, expressed in thousands of Canadian dollars, except number of shares)

	Share capital		Equity component of convertible loan	Contributed surplus	Deficit	Total equity
	Shares	**Amount**				
Balance December 31, 2010	195,505,323	$ 72,927	$ 453	$ 2,662	$ (73,564)	$ 2,478
Issue of common shares (note 18i)	6,488,790	324	-	-	-	324
Stock based compensation expense (note 20)	-	-	-	145	-	145
Fair value of warrants issued (note 16e)	-	-	-	617	-	617
Loss for the period	-	-	-	-	(2,452)	(2,452)
Balance December 31, 2011	201,994,113	73,251	453	3,424	(76,016)	1,112
Balance December 31, 2011	201,994,113	73,251	453	3,424	(76,016)	1,112
Issue of common shares (notes 18b, c, d, e, f, g and h)	52,903,959	2,966	-	-	-	2,966
Loan conversion (note 16d)	-	206	(453)	-	-	(247)
Stock-based compensation expense (note 20)	-	-	-	115	-	115
Income for the period	-	-	-	-	20,641	20,641
Balance December 31, 2012	**254,898,072**	**76,423**	**-**	**3,539**	**(55,375)**	**24,587**

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

1. Nature of operations

Avcorp Industries Inc. (the "Company") is a Canadian-based manufacturer within the aerospace industry, and a single-source supplier for engineering design, manufacture and assembly of subassemblies and complete major structures for aircraft manufacturers.

We operate from two locations in Canada. Comtek Advanced Structures Ltd., a wholly owned subsidiary, is located in Ontario and is dedicated to composites manufacturing and repairs. Avcorp Industries Inc. is located in British Columbia and is dedicated to light weight metal manufacturing and assembly.

The Company's governing corporate statute is the Canada Business Corporations Act (the "CBCA").

The consolidated financial statements of the Company for the year ended December 31, 2012 were authorized for issue in accordance with a resolution of its Board of Directors on March 25, 2013.

2. Basis of preparation and measurement

The consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB).

The consolidated financial statements have been prepared on a historical cost basis, except for derivative financial instruments that have been measured at fair value. The consolidated financial statements are presented in Canadian dollars and all values are rounded to the nearest thousand (000), except when otherwise indicated.

3. Summary of significant accounting policies

The significant accounting policies used in the preparation of these consolidated financial statements are described below. These policies have been consistently applied to all periods presented, unless otherwise stated.

Basis of consolidation

The financial statements of the Company consolidate the accounts of Avcorp Industries Inc. and its subsidiary Comtek Advanced Structures Ltd. ("Comtek"). All significant intercompany transactions, balances and unrealized gains and losses from intercompany transactions are eliminated on consolidation.

Subsidiaries are those entities which the Company controls by having the power to govern the financial and operating policies. The existence and effect of potential voting rights that are currently exercisable or convertible are considered when assessing whether Avcorp Industries Inc. controls another entity. Subsidiaries are fully consolidated from the date on which control is obtained by the Company and are de-consolidated from the date that control ceases.

Foreign currency translation

- Functional and presentation currency: Foreign currency items included in the financial statements of each consolidated entity in the Avcorp Industries Inc. group are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency. The functional currency of the Company's subsidiary, Comtek, is also determined to be Canadian dollars.
- Transactions and balances: Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Generally, foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at period-end exchange rates of monetary assets and liabilities denominated in currencies other than an operation's functional currency are recognized in the statement of income.

Financial instruments

Financial assets and liabilities are recognized when the Company becomes a party to the contractual provisions of the instrument. Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

Financial assets and liabilities are offset and the net amount reported in the consolidated statements of financial position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis, or realize the asset and settle the liability simultaneously.

At initial recognition, the Company classifies its financial instruments in the following categories depending on the purpose for which the instruments were acquired:

- Financial assets and liabilities at fair value through profit or loss: The Company's financial assets and liabilities included in other assets are inflation derivative assets arising from the Company's sales contracts having price adjustment clauses within their terms. A financial asset or liability is classified in this category if acquired principally for the purpose of selling or repurchasing in the short-term.

  Financial instruments in this category are recognized initially and subsequently at fair value. Transaction costs are expensed in the statement of income. Gains and losses arising from changes in fair value are presented in the statement of income within other gains and losses in the period in which they arise. Financial assets and liabilities at fair value through profit or loss are classified as current except for the portion expected to be realized or paid beyond twelve months of the consolidated statements of financial position date, which is classified as non-current.

- Derivative financial instruments: The Company uses derivative financial instruments to reduce its exposure to price risk associated with its revenues, and costs of certain procured items. All derivatives have been classified on the consolidated statements of financial position balance sheet within prepayments and other assets, or other liabilities and are classified as current or non-current based on the contractual terms specific to the instrument. Gains and losses on re-measurement are included in other gains and losses. The Company does not have any derivative financial instruments as at December 31, 2012.

- Loans and receivables: Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. The Company's loans and receivables are comprised of trade receivables and cash and cash equivalents, and are included in current assets due to their short-term nature. Loans and receivables are initially recognized at the amount expected to be received less, when material, a discount to reduce the loans and receivables to fair value. Subsequently, loans and receivables are measured at amortized cost using the effective interest method less a provision for impairment.

  The Company transfers trade receivables under certain bank-sponsored revolving securitization programs. Because the Company retains substantially all the risks and rewards of ownership of the factored receivables, it continues to recognize the full carrying amount of these receivables and accounts for these transactions as collateralized borrowings. The Company does not have any bank-sponsored revolving securitization programs as at December 31, 2012.

- Financial liabilities at amortized cost: Financial liabilities at amortized cost include trade payables, bank debt and long-term debt. Trade payables are initially recognized at the amount required to be paid less, when material, a discount to reduce the payables to fair value. Bank debt and long-term debt are recognized initially at fair value, net of any transaction costs incurred, and subsequently at amortized cost using the effective interest method.

  Financial liabilities at amortized cost are classified as current liabilities if payment is due within twelve months. Otherwise, they are presented as non-current liabilities.

Impairment of financial assets

At each reporting date, the Company assesses whether there is objective evidence that a financial asset is impaired. If such evidence exists, the Company recognizes an impairment loss, as follows:

- Financial assets carried at amortized cost: The loss is the difference between the amortized cost of the loan or receivable and the present value of the estimated future cash flows, discounted using the instrument's original effective interest rate. The carrying amount of the asset is reduced by this amount either directly or indirectly through the use of an allowance account.

Impairment losses on financial assets carried at amortized cost are reversed in subsequent periods if the amount of the loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized.

Impairment of non-financial assets

Property, plant and equipment are tested for impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. For the purpose of measuring recoverable amounts, assets are grouped at the lowest levels for which there are separately identifiable cash in-flows (cash-generating units or "CGU"). The recoverable amount is the higher of an asset's fair value less costs to sell and value in use (being the present value of the expected future cash flows of the relevant asset or CGU). An impairment loss is recognized for the amount by which the asset's carrying amount exceeds its recoverable amount.

Inventories

Inventories are stated at the lower of cost and net realizable value. Cost is determined using the first-in, first-out ("FIFO") method. The cost of finished goods and work-in-progress comprises raw materials, direct labour, other direct costs and related production overheads (based on normal operating capacity) including applicable depreciation on property, plant and equipment and amortization of intangible assets. Net realizable value is the estimated selling price less applicable selling expenses.

Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated depreciation and accumulated impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset. Subsequent costs are included in the asset's carrying amount or recognized as a separate asset, as appropriate, only when it is probable that future economic benefits associated with the item will flow to the Company and the cost can be measured reliably. The carrying amount of a replaced asset is derecognized when replaced. Repairs and maintenance costs are charged to the statement of income during the period in which they are incurred.

An estimation is made of the useful life of equipment. Useful life is measured in terms of years or units-of-production, and depreciated on a straight line basis.

Computer hardware and software	2 - 10 years
Machinery and equipment	5 - 15 years
Leasehold improvements	end of lease, 2018

The Company allocates the amount initially recognized in respect of an item of property, plant and equipment to its significant parts and depreciates separately each such part. Residual values, method of depreciation and useful lives of the assets are reviewed annually and adjusted if appropriate.

Gains and losses on disposals of property, plant and equipment are determined by comparing the proceeds with the carrying amount of the asset and are included as part of other gains and losses in the consolidated statement of income.

Employee benefits

- Post-employment benefit obligations: Employees of companies included in these consolidated financial statements have entitlements under Company pension plans which are defined contribution pension plans.

  The cost of defined contribution pension plans is charged to expense as the contributions become payable.

- Stock based compensation: The Company grants stock options to certain employees. Stock options vest over three years and all expire five years after grant date. Each tranche in an award is considered a separate award with its own vesting period and grant date fair value. Fair value of each tranche is measured at the date of grant using the Black-Scholes option pricing model.

  Compensation expense is recognized over the tranche's vesting period based on the number of awards expected to vest, by increasing contributed surplus. The number of awards expected to vest is reviewed at least quarterly, with any impact being recognized immediately.

- Termination benefits: The Company recognizes termination benefits when it is demonstrably committed to either terminating the employment of current employees according to a detailed formal plan without possibility of withdrawal, or providing benefits as a result of an offer made to encourage voluntary termination. Benefits falling due more than twelve months after the end of the reporting period are discounted to their present value.

Provisions

Provisions for warranties, where applicable, are recognized in other liabilities when the Company has a present legal or constructive obligation as a result of past events, it is more likely than not that an outflow of resources will be required to settle the obligation, and the amount can be reliably estimated. Provisions are measured at management's best estimate of the expenditure required to settle the obligation at the end of the reporting period, and are discounted to present value where the effect is material. The Company performs evaluations to identify onerous contracts and, where applicable, records provisions for such contracts.

Revenue

Revenue is recognized when it is probable that the economic benefits will flow to the Company and delivery has occurred, the sales price is fixed or determinable, and collectability is reasonably assured. These criteria are generally met at the time the product is shipped and delivered to the customer and, depending on the delivery conditions, title and risk have passed to the customer and acceptance of the product, when contractually required, has been obtained.

Revenue is measured based on the price specified in the sales contract, net of discounts.

Cost of sales

Cost of sales includes the cost of production, including materials, direct labour, overhead expenses as well as applicable depreciation and amortization.

Income tax

a) Current income tax

   Current income tax assets and liabilities for the current period are measured at the amount expected to be recovered from or paid to the taxation authorities. The tax rates and tax laws used to compute the amount are those that are enacted or substantively enacted, at the reporting date in the countries where the Company operates and generates taxable income.

   Current income tax relating to items recognized directly in equity is recognized in equity and not in the income statement. Management periodically evaluates positions taken in the tax returns with respect to situations in which applicable tax regulations are subject to interpretation and establishes provisions where appropriate.

b) Deferred tax

   Deferred tax is provided using the liability method on deductible temporary differences between the tax bases of assets and liabilities and their carrying amounts for financial reporting purposes at the reporting date.

Deferred tax liabilities are recognized for all taxable temporary differences, except:

- When the deferred tax liability arises from the initial recognition of goodwill or an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss
- In respect of taxable temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future

Deferred tax assets are recognized for all deductible temporary differences, the carry forward of unused tax credits and any unused tax losses. Deferred tax assets are recognized to the extent that it is probable that taxable profit will be available against which the deductible temporary differences and the carry forward of unused tax credits and unused tax losses can be utilized, except:

- When the deferred tax asset relating to the deductible temporary difference arises from the initial recognition of an asset or liability in a transaction that is not a business combination and, at the time of the transaction, affects neither the accounting profit nor taxable profit or loss
- In respect of deductible temporary differences associated with investments in subsidiaries, associates and interests in joint ventures, deferred tax assets are recognized only to the extent that it is probable that the temporary differences will reverse in the foreseeable future and taxable profit will be available against which the temporary differences can be utilized

The carrying amount of deferred tax assets is reviewed at each reporting date and reduced to the extent that it is no longer probable that sufficient taxable profit will be available to allow all or part of the deferred tax asset to be utilized. Unrecognized deferred tax assets are reassessed at each reporting date and are recognized to the extent that it has become probable that future taxable profits will allow the deferred tax asset to be recovered.

Deferred tax assets and liabilities are measured at the tax rates that are expected to apply in the year when the asset is realized or the liability is settled, based on tax rates (and tax laws) that have been enacted or substantively enacted at the reporting date.

Deferred tax relating to items recognized outside profit or loss is recognized outside profit or loss. Deferred tax items are recognized in correlation to the underlying transaction either in other comprehensive income or directly in equity.

Deferred tax assets and deferred tax liabilities are offset if a legally enforceable right exists to set off current tax assets against current income tax liabilities and the deferred taxes relate to the same taxable entity and the same taxation authority.

Tax benefits acquired as part of a business combination, but not satisfying the criteria for separate recognition at that date, are recognized subsequently if new information about facts and circumstances change. The adjustment is either treated as a reduction to goodwill (as long as it does not exceed goodwill) if it was incurred during the measurement period or recognized in profit or loss.

Share capital

Common shares are classified as equity. Incremental costs directly attributable to the issuance of shares are recognized as a deduction from equity.

Dividends

Dividends on common and preferred shares are recognized in the Company’s consolidated financial statements in the period in which the dividends are approved by the Board of Directors of the Company.

Earnings per share

Basic earnings per share (“EPS”) is calculated by dividing the net income (loss) for the period by the weighted average number of common shares outstanding during the period.

Diluted EPS is calculated by adjusting the weighted average number of common shares outstanding for dilutive instruments. The number of shares included with respect to options, warrants and similar instruments is computed using the treasury stock method. The Company’s potentially dilutive common shares comprise stock options granted to employees, warrants and convertible loans.

Research and development costs

Research costs are expensed as incurred. Development costs, which are currently all tooling and new program introduction costs incurred on long-term programs that meet the criteria for deferral, are capitalized and amortized over the number of shipsets management believes is a reasonable estimate of units to be sold for the program.

Government assistance

Government assistance towards research and development expenditures is received from Technology Partnerships Canada. Assistance is repayable by way of royalties only if revenues are generated from specified product sales.

The Company credits government assistance directly to the costs and expenses of the related programs for which the assistance was provided.

Convertible loans and debentures

Upon issuance, convertible debentures and loans are classified into their equity and liability components based on the fair value of debt element, with the residual of the gross proceeds allocated to equity. The liability components on convertible debentures and loans are accreted up to their principal value by way of a charge to earnings over the term of the debt, using the effective interest rate method. Transaction costs are deducted from the value of the loan and accreted over the loan term.

Leases

Leases are classified as finance or operating leases. A lease that transfers substantially all the benefits and risks incident to the ownership of property is classified as a finance lease. All other leases are accounted for as operating leases whereby lease payments are expensed on a straight-line basis over the term of the lease. Gains and losses arising on sale and leaseback transactions, when the leaseback is classified as a capital lease, are deferred and amortized in proportion to the amortization of the leased asset. Lease inducements received are recorded as a deferred credit and amortized as a reduction of lease expense over the term of the lease.

Accounting standards issued but not yet applied

The following is a brief summary of the new standards:

IFRS 9 – Financial Instruments

IFRS 9 was issued in November 2009. It addresses classification and measurement of financial assets and replaces the multiple category and measurement models in IAS 39 for debt instruments with a new mixed measurement model having only two categories: amortized cost and fair value through profit or loss. IFRS 9 also replaces the models for measuring equity instruments and such instruments are either recognized at fair value through profit or loss or at fair value through other comprehensive income. Where such equity instruments are measured at fair value through other comprehensive income, dividends, to the extent not clearly representing a return of investment, are recognized in profit or loss; however, other gains and losses (including impairments) associated with such instruments remain in accumulated comprehensive income indefinitely. This standard is required to be applied for accounting periods beginning on or after January 1, 2015, with earlier adoption permitted. The Company has not yet assessed the impact of the standard or determined whether it will adopt the standard early.

IFRS 10 – Consolidation

IFRS 10 requires an entity to consolidate an investee when it is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Under existing IFRS, consolidation is required when an entity has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. IFRS 10 replaces SIC-12 *Consolidation – Special Purpose Entities* and parts of IAS 27, *Consolidated and Separate Financial Statements*.

IFRS 11 – Joint Arrangements

IFRS 11 requires a venturer to classify its interest in a joint arrangement as a joint venture or joint operation. Joint ventures will be accounted for using the equity method of accounting whereas for a joint operation the venturer will recognize its share of the assets, liabilities, revenue and expenses of the joint operation. Under existing IFRS, entities have the choice to proportionately consolidate or equity account for interests in joint ventures. IFRS 11 supersedes IAS 31, *Interests in Joint Ventures,* and SIC-13, *Jointly Controlled Entities-Non-monetary Contributions by Venturers.*

IFRS 12 – Disclosure of Interests in Other Entities

IFRS 12 establishes disclosure requirements for interests in other entities, such as joint arrangements, associates, special purpose vehicles and off-balance sheet vehicles. The standard carries forward existing disclosures and also introduces significant additional disclosure requirements that address the nature of, and risks associated with, an entity's interests in other entities.

IFRS 13 – Fair Value Measurement

IFRS 13 is a comprehensive standard for fair value measurement and disclosure requirements for use across IFRS standards. The new standard clarifies that fair value is the price that would be received to sell an asset, or paid to transfer a liability in an orderly transaction between market participants, at the measurement date. It also establishes disclosures about fair value measurement. Under existing IFRS, guidance on measuring and disclosing fair value is dispersed among the specific standards requiring fair value measurements and in many cases does not reflect a clear measurement basis or consistent disclosures.

IFRS 10, 11, 12 and 13 are effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. Management does not expect that these accounting standards issued but not yet applied will have a material impact on the Company's consolidated financial statements.

Amendments to Other Standards

In addition, there have been amendments to existing standards, including IAS 27, *Separate Financial Statements* (IAS 27), and IAS 28, *Investments in Associates* and *Joint Ventures* (IAS 28). IAS 27 addresses accounting for subsidiaries, jointly controlled entities and associates in non-consolidated financial statements. IAS 28 has been amended to include joint ventures in its scope and to address the changes in IFRS 10-13.

The standard setting bodies that determine IFRS have significant ongoing projects that could impact the IFRS accounting policies selected. The Company has processes in effect to ensure that potential IFRS accounting policy changes are monitored and evaluated. The impact of any new IFRS and IFRIC Interpretations will be evaluated as they are drafted and published.

4. Critical accounting estimates and judgements

The preparation of financial statements in conformity with IFRS requires management to make estimates and judgments that affect the amounts which are reported in the consolidated financial statements during the reporting period. Estimates and other judgments are evaluated at each reporting date and are based on management's experience and other factors, including expectations about future events that are believed to be reasonable under the circumstances.

- Management assesses the Company's ability to continue as a going concern at each reporting date, using all quantitative and qualitative information available. This assessment, by its nature, relies on estimates of future cash flows and other future events, whose subsequent changes would materially impact the validity of such an assessment.
- Carrying value of long-lived assets: The Company holds property, plant and equipment, (note 11) on the consolidated statements of financial position amounting to $9,633,000 (December 31, 2011: $12,523,000). Reduction in market demand during 2009 for business jet aircraft has resulted in negative operating cash flows during the subsequent years. The recoverability of these assets is dependent on the ability of the company to generate sufficient cash flow from operations over the remaining useful life of the assets, which is contingent on, amongst other factors, the ability of the Company to replace known program losses with new programs as well as ramping up scheduled production for new defence contracts. The recoverability of the carrying value of these assets is, in part, dependent on the estimates used in determining the expected period of future benefits over which to amortize. In addition, such recoverability is dependent on delivering to the scheduled production ramp-up for new defence programs, as well as dependent on market conditions including demand for such aircraft for which the Company provides its products.
- Recoverability of deferred tooling costs: The ability to defer tooling costs is dependent on the future recoverability of the amounts from cash flows generated by the related commercial operations as well as contractually required payments by customers. If operations perform below anticipated recoverable levels, the portion of deferred tooling costs that cannot be recovered is expensed immediately when known. At December 31, 2012, $2,718,000 (December 31, 2011: $5,540,000) in unamortized deferred tooling costs (note 10), which are expected to be recoverable from the related future cash flows of operations resulting from continued customer orders or recovery of cash from customers for deferred amounts, are presented as Development costs in the consolidated statements of financial position. Deferred tooling costs of $587,000 (December 31, 2011: $3,007,000) are not supported by customer advances.
- On a periodic basis the Company provides for its anticipated losses under existing contractual commitments to its customers by comparing its anticipated future costs of production to its contracted future revenues. The December 31, 2012 provision for anticipated losses was $Nil (December 31, 2011: $189,000). The decrease in this provision from December 31, 2011 was primarily as a result of the curtailment of a loss-making program, improvements in certain other program gross margins, as well as a reduction in associated anticipated number of aircraft components to be delivered.
- On a periodic basis the Company reviews its plant capacity and estimates the portion of its under-utilized overhead expenditures. The Company has expensed $4,660,000 of overhead costs during the current year (December 31, 2011: $4,149,000) in respect of unutilized plant capacity.
- Warranty provisions are provided for when an actual deficiency is identified, and through working with the customer it is estimated based on the expected cost per unit over the number of units affected. During previous years, the Company provisioned for $85,000 of expected warranty expenditures relating to a manufacturing deficiency. All rectifications have not been completed by the date of this report, and $85,000 remains provisioned for expected future expenditures.
- Deferred program revenues are recognized as revenue straight-line on a units-of-production basis over the expected life of the program; where expected life is an estimate based on customer and industry data.
- Other receivable is based on a binding arbitration award under which a quantum of damages was assessed and a period for payment was established.

5. Expenses by nature

The consolidated statement of income presents expenses by function. Accordingly, amortization and depreciation is no longer presented as a separate line on the statement, but is included within cost of sales to the extent that it relates to manufacturing machinery and equipment, as well as leasehold improvements.

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

Expenses by nature:

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Raw materials, purchased parts and consumables	**$ 37,739**	$ 39,198
Salary, wages and benefits	**35,318**	33,813
Depreciation and amortization	**6,278**	3,876
Legal and audit fees	**3,137**	1,225
Rent	**2,363**	2,336
Contract services and consulting	**1,791**	1,564
Utilities	**1,021**	996
Transportation	**739**	917
Travel costs	**652**	504
Office equipment rental/maintenance	**642**	592
Insurance	**445**	448
Royalties	**203**	395
Other expenses and conversion of costs into inventory	**2,398**	516
	92,726	86,380

6. Capital Risk Management

The Company's objectives when managing capital are to safeguard its ability to continue as a going concern and to provide an adequate return to shareholders, while satisfying other stakeholders.

The Company includes long-term debt, preferred shares and capital stock in its definition of capital, as shown in the Company's consolidated statements of financial position.

The Company's primary objective in its management of capital is to ensure that it has sufficient financial resources to fund ongoing operations and new program investment. In order to secure this capital the Company may attempt to raise funds via issuance of debt and equity, or by securing strategic partners (notes 16 and 18). The Company is subject to one capital restriction relating to redemption of preferred shares (note 19).

7. Financial Risk Management

The Company is exposed to certain financial risks including currency risk, credit risk, liquidity risk, interest rate risk and price risk.

a) Currency Risk

The Company sells a significant proportion of its products in US dollars at prices which are often established well in advance of manufacture and shipment dates. In addition, the Company purchases a significant proportion of its raw materials in US dollars at prices that are usually established at the order date. All of the Company's operations are based in Canada. As a result of this, the Company is exposed to currency risk to the extent that fluctuations in exchange rates are experienced. The amount of foreign exchange loss recorded in 2012 was $193,000 as compared to a $333,000 gain for the year ended December 31, 2011.

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

The Company had the following US dollar denominated balances:

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Bank cash position	**$ 2,197**	$ 4,598
Accounts receivable	**2,934**	6,041
Accounts payable net of prepayments	**1,329**	2,664
Long-term debt	**-**	713

With other variables unchanged, each $0.10 strengthening (weakening) of the US dollar against the Canadian dollar would result in an increase (decrease) of approximately $380,000 in net earnings for the year ended December 31, 2012 (December 31, 2011: $726,000 increase (decrease) in net earnings) as a result of holding a US dollar net asset position.

b) Credit Risk

Credit risk is the risk of a financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligation. The Company manages credit risk for trade and other receivables through a financial review of the credit worthiness of the prospective customer along with credit monitoring activities. The majority of the Company's trade receivables reside with Boeing Commercial Airplane Group (Boeing), Boeing Defense, Space & Security (BDS), Bombardier Aerospace (Bombardier), BAE Systems (Operations) Limited (BAE) and Cessna Aircraft Company (Cessna). During 2012 and 2011, there were no trade receivables written off by the Company in respect of these customers. The maximum exposure to credit risk is represented by the amount of accounts receivable in the consolidated statements of financial position.

As at the consolidated statements of financial position date 73.1% (December 31, 2011: 81.7%) of the Company's trade accounts receivable are attributable to these customers.

c) Liquidity Risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company seeks to manage liquidity risk through the management of its capital structure and financial leverage.

The Company's governing corporate statute is the Canada Business Corporations Act (the "CBCA"). Under the CBCA, the Company may not purchase or otherwise acquire its own shares, including redeeming the preferred shares, if there are reasonable grounds for believing that the Company would after the purchase be unable to pay its liabilities as they become due. The Company's board has determined that honouring any redemption request for preferred shares, regardless of the number of shares involved, would result in the Company being unable to pay its liabilities as they become due.

While the Company currently is able to meet its existing obligation, it is reliant on certain credit and loan facilities for the normal, ongoing operation of its business. Those operating facilities currently provide that it is an event of default if the Company redeems any of its preferred shares. The inability of the Company to access its customary operating facilities would impair the proper operation of the Company's business and prohibit it from meeting, in the normal course, its liabilities as they become due. Accordingly, at this time the Company is prohibited from completing any redemption of preferred shares.

Accounts payable and accrued liabilities are all due within the next twelve months.

The Company's operating line of credit is due on demand (note 12). Long-term debt repayments are as outlined in note 16. Preferred shares are redeemable as outlined in note 19.

The table below categorizes the Company's non-derivative financial liabilities into relevant maturity periods based on the remaining period from the consolidated statements of financial position date to the contractual maturity date. The amounts disclosed in the table are the contractual undiscounted cash flows.

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

	December 31, 2012			
	Less than 3 months	**3 months to 1 year**	**2 – 5 years**	**Over 5 years**
Bank indebtedness	$ 2,122	$ -	$ -	$ -
Long-term debt	72	620	4,300	-
Preferred shares	10,646	-	-	-
Trade payables	3,954	-	-	-

	December 31, 2011			
	Less than 3 months	**3 months to 1 year**	**2 – 5 years**	**Over 5 years**
Bank indebtedness	$ -	$ -	$ -	$ -
Long-term debt	218	1,287	12,027	-
Preferred shares	9,890	-	-	-
Trade payables	6,515	-	-	-

d) Interest Rate Risk

The Company is exposed to interest rate risk on the utilized portion of its operating line of credit at rates of bank prime plus 0.5%. The maximum operating line of credit availability is $12,000,000 (note 12) of which $2,122,000 is utilized as at December 31, 2012 (December 31, 2011: $Nil). The Company lowers interest rate costs by managing utilization of the operating lines of credit to the lowest amount practical. For the year ended December 31, 2012, with other variables unchanged, a 1% change in the bank prime interest rate would have a $21,000 (December 31, 2011: $Nil) impact on net earnings and cash flow.

The Company primarily finances the purchase of long-lived assets at fixed interest rates.

e) Price Risk

Certain of the Company's contracts contain derivative financial instruments to reduce exposure to price risk associated with its revenues and costs of certain procured items.

Sales Contracts

A number of the Company's sales contracts have a price adjustment clause where the final sales price is determined by certain indices in a period prior to the date of sale. As a result, the final sales price will change as these underlying indices change. This price adjustment clause is an embedded derivative that is recorded at fair value, with changes in fair value recorded in other income or expenses until the date of sale. As at December 31, 2012, the Company has $12,040,000 (December 31, 2011: $27,251,000) of firmly committed orders that include price adjustment clauses of this nature. A $5,000 gain has been recorded as a derivative gain for the year ended December 31, 2012 as compared to a $14,000 gain for the year ended December 31, 2011 as a result of the change in the fair value of the underlying embedded derivatives.

Purchase Contracts

The Company's purchase contracts do not have a price adjustment clause where the final purchase price is determined by certain indices in a period prior to the date of purchase.

Included in prepayments and other assets is $27,000 of inflation derivatives assets arising from the Company's sales contracts having price adjustment clauses within their terms (December 31, 2011: $33,000).

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

f) Financial Assets and Liabilities by Category

As at December 31, 2012 and 2011, the Company's financial assets and liabilities are categorized as follows:

				December 31, 2012
	Loans and receivables	**Held at fair value**	**Financial assets and liabilities at amortized cost**	**Total**
Financial Assets				
Accounts receivable	$ 7,944	$ -	$ -	$ 7,944
Commodity contracts	-	27	-	27
Other receivable	27,391	-	-	27,391
Financial Liabilities				
Bank indebtedness	-	-	2,122	2,122
Accounts payable and accrued liabilities	-	-	7,859	7,859
Long-term debt	-	-	4,992	4,992
Preferred shares	-	-	10,646	10,646

				December 31, 2011
	Loans and receivables	**Held at fair value**	**Financial assets and liabilities at amortized cost**	**Total**
Financial Assets				
Accounts receivable	$ 12,160	$ -	$ -	$ 12,160
Commodity contracts	-	33	-	33
Financial Liabilities				
Accounts payable and accrued liabilities	-	-	10,694	10,694
Long-term debt	-	-	13,532	13,532
Preferred shares	-	-	9,890	9,890

The Company's Commodity Contracts have been evaluated to have a Level 2 Fair Value hierarchy.

The Company uses the following hierarchy for determining and disclosing the fair value of financial instruments by valuation technique:

- Level 1: quoted (unadjusted) prices in active markets for identical assets or liabilities;
- Level 2: other techniques for which all inputs that have a significant effect on the recorded fair value are observable, either directly or indirectly; and
- Level 3: techniques that use inputs that have a significant effect on the recorded fair value that are not based on observable market data.

g) Fair values

The fair values of the Company's accounts receivable, accounts payable and accrued liabilities and preferred shares are estimated to approximate their carrying values due to their immediate or short-term maturity. The Company's long-term debt is primarily held with Export Development Canada ("EDC") (note 16a), which is a governmental body, and management believes that any future debt would come from related parties. The effective interest rate of 5% for the EDC debt is thought to approximate the rate that the Company could obtain if further debt was to be obtained from this source. An increase of 1% in the EDC debt, representing a worsening of the credit position of the company in respect of that party, would result in a change in the value of the loan by $81,000.

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

8. Accounts Receivable

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Trade receivables	**$ 6,926**	$ 11,249
Input tax credits	**940**	689
Other receivables	**78**	222
	7,944	12,160

The carrying amounts of the Company's trade and other receivables are denominated in the following currencies:

FOR THE YEAR ENDED DECEMBER 31	2012	2011
US dollar	**USD $ 2,934**	USD $ 6,041
Canadian dollar	**5,026**	6,017

9. Inventories

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Raw materials	**$ 7,418**	$ 8,571
Work in progress	**8,478**	10,293
Finished products	**676**	554
	16,572	19,418

The amount of inventory expensed in cost of sales during the year ended December 31, 2012 amounted to $68,979,000 (December 31, 2011: $68,784,000). The carrying value of inventory pledged as security as at December 31, 2012 is $16,572,000 (December 31, 2011: $19,418,000).

On a periodic basis the Company provides for its anticipated losses under existing contractual commitments to its customers by comparing its anticipated future costs of production to its contracted future revenues. The December 31, 2012 provision for anticipated losses was $Nil (December 31, 2011: $189,000). Work in progress inventory noted in the above table has been presented net of these provisions for anticipated losses. Certain program inventories have been funded by a customer, whereby the associated deferred program revenues will be recorded as revenue upon delivery of units of production.

The transition of production work back to Cessna was completed in 2012. Accordingly, $983,000 of remaining Cessna program inventories were written off (note 28).

10. Development Costs

Development costs represent hard and soft tooling, and prototype design costs incurred for various customer programs.

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Opening balance	**$ 5,540**	$ 5,181
Additions	**1,071**	1,337
Realized, amortization and write-off (note 28)	**(3,893)**	(978)
	2,718	5,540

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Cost	$ 3,669	$ 6,619
Accumulated amortization	(951)	(1,079)
Net book amount	2,718	5,540

The transition of production work back to Cessna was completed in 2012. Accordingly, $2,034,000 of Cessna program related Development Costs were written off (note 28).

11. Property, Plant and Equipment

	Machinery and equipment	Computer hardware and software	Leasehold improvements	Total
Year ended December 31, 2011				
Opening net book amount	$ 12,403	$ 1,814	$ 577	$ 14,794
Additions	988	188	48	1,224
Disposals – cost	(1,045)	(380)	(248)	(1,673)
Disposals – accumulated depreciation	1,044	380	248	1,672
Depreciation charge	(2,818)	(599)	(77)	(3,494)
Closing net book amount	10,572	1,403	548	12,523
At December 31, 2011				
Cost	36,187	8,034	881	45,102
Accumulated depreciation	(25,615)	(6,631)	(333)	(32,579)
Net book amount	10,572	1,403	548	12,523
Period ended December 31, 2012				
Opening net book amount	10,572	1,403	548	12,523
Additions	160	584	33	777
Disposals – cost	(7,349)	(1,871)	-	(9,220)
Disposals – accumulated depreciation	6,715	1,850	-	8,565
Depreciation charge	(2,480)	(447)	(85)	(3,012)
Closing net book amount	7,618	1,519	496	9,633
At December 31, 2012				
Cost	28,998	6,747	914	36,659
Accumulated depreciation	(21,380)	(5,228)	(418)	(27,026)
Net book amount	7,618	1,519	496	9,633

Included in computer hardware and software are assets held under finance leases at a cost of $261,000 (December 31, 2011: $149,000) having accumulated depreciation of $57,000 (December 31, 2011: $149,000).

Included in machinery and equipment are assets held under finance leases at a cost of $55,000 (December 31, 2011: $4,095,000) having accumulated depreciation of $43,000 (December 31, 2011: $1,042,000).

Included in leasehold improvements are assets held under finance leases at a cost of $Nil (December 31, 2011: $52,000) having accumulated depreciation of $Nil (December 31, 2011: $21,000).

During 2012 the value of certain machinery, equipment, tooling, computer hardware and software was written down by $655,000 (December 31, 2011: $Nil). The equipment which was no longer in use had a cost of $9,220,000, and an accumulated depreciation of $8,565,000; resulting in a $655,000 charge against income (note 28). A portion of this write-down was specifically related to the Cessna production contract termination. The transition of production work back to Cessna was completed in 2012. Accordingly, Cessna program related equipment was written off having a cost of $6,643,000 and an accumulated depreciation of $6,179,000; resulting in a $464,000 charge against income (note 28).

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

The Company does not have any commitments at year-end to purchase property, plant and equipment in 2013.

12. Bank Indebtedness

On September 27, 2012 the Company entered into a loan agreement with a Canadian chartered bank for a $12 million principal amount secured debt facility. The debt facility has a three-year term and bears interest at a rate equal to the bank's prime rate plus 0.5%.

The debt facility is secured by a charge and specific registration over all of the assets of the Company.

As a condition of obtaining this operating line of credit, the following terms were established:

- Company shall maintain a consolidated fixed charge coverage ratio of not less than 1:1, calculated on a rolling twelve month basis and tested as of the end of each fiscal month;
- Company shall maintain excess availability on its operating line of credit in an amount no less than a cure amount providing for any shortfall in the fixed charge coverage ratio; and
- the cure amount can only be added to the numerator two times in the 2014 fiscal year and thereafter.

As at December 31, 2012 the Company had drawn $2,122,000 on this debt facility offset by $2,597,000 cash, providing a net cash position of $475,000.

13. Accounts Payable and Accrued Liabilities

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Trade payables	**$ 3,954**	$ 6,515
Payroll-related liabilities	**3,154**	2,787
Other	**751**	1,392
	7,859	10,694

14. Deferred Program Revenues

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Opening balance	**$ 18,671**	$ 6,804
Additions	**15,015**	16,838
Realized	**(16,172)**	(4,971)
	17,514	18,671

The Company sold tooling on certain aircraft programs to customers. The customers are allowing the Company to use the tooling for production of aircraft components for the life of those programs. Accordingly, as the Company will receive the full benefit of the use of the tooling, the sale amount is deferred and will be amortized to income, straight-line on a units-of-production basis over the expected life of the program. Additionally, customers have funded the non-recurring costs incurred during the introduction of new production programs. These costs are deferred as development costs and will be amortized to income, straight-line on a units-of-production basis over the expected life of the programs, in conjunction with the associated deferred revenue upon commencement of production.

Certain program inventories have been funded by a customer, whereby the associated deferred program revenues will be recorded as revenue upon delivery of units of production.

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

15. Deferred Gain, Lease Inducement and Prepaid Rent

On July 17, 2003, the Company sold its land and building for gross proceeds of $16,000,000, representing $14,500,000 received in cash for the property and $1,500,000 as a lease inducement credit. Concurrently, the Company entered into a 15-year leaseback agreement with the purchaser of the property. A $712,000 gain arising on disposal of property in 2003 was recorded as a deferred gain and is being amortized to income over the life of the lease. The unamortized balance of the gain is $263,000 as at December 31, 2012 (December 31, 2011: $311,000). The amount of prepaid rent the Company has as at December 31, 2012 is $146,000 (December 31, 2011: $146,000).

Concurrent with the sale and leaseback transaction recorded in 2003, the Company recorded a lease inducement credit of $1,500,000. The lease inducement credit is being amortized against rental expense over the term of the lease. It has an unamortized balance of $567,000 as at December 31, 2012 (December 31, 2011: $666,000).

16. Long-Term Debt

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Convertible debenture (a)	**$ 4,392**	$ 4,447
Finance leases (b)	**208**	888
Accrued government royalties (c)	**392**	1,088
Convertible loan (d)	**-**	1,638
Term loan (e)	**-**	5,471
	4,992	13,532
Less: Current portion	**(692)**	(1,505)
	4,300	12,027

a) Export Development Canada Convertible Debenture

The Company entered into a First Amendment Waiver and Consent Agreement dated June 27, 2011 with Export Development Canada (EDC). Pursuant to this amendment, the terms of the debenture dated December 31, 2009 have been amended such that the debenture now has a maturity date of March 31, 2016. Under the terms of the agreement, the Company will commence $150,000 quarterly principal repayments on July 1, 2013. Principal repayments are due on the first business day of each quarter.

The principal outstanding debenture amount of $4,338,000 is convertible at the option of the holder into 21,688,720 shares at a conversion price of $0.20. The Company can require conversion of the full amount of the debenture in the event that the weighted average trading price of the Company's shares on the Toronto Stock Exchange is greater than 125% of the conversion price for 20 consecutive days and such weighted average trading price exceeds $4.00.

The debenture bears interest at 5.0% per annum and is unsecured.

Beginning July 1, 2011 until June 30, 2012, the interest due on the EDC debenture shall be payable in cash or common shares of the Company, at the election of the Company, at the five day volume weighted average trading price of the Company's common shares calculated retroactively from the final day of the fiscal quarter. All interest thereafter is payable in cash.

Interest accrued and payable as at December 31, 2012 amounted to $54,000 (December 31, 2011: $109,000).

b) Finance Leases

There are various equipment leases that have a weighted average interest rate of 8.12% per annum. The leases are secured by way of a charge against specific assets. The leases are repayable in equal installments over periods up to 60 months.

c) Accrued Government Royalties

Royalties of $392,000 (December 31, 2011: $1,088,000) applicable on certain contracts are payable to Industrial Technologies Office. On February 5, 2010, the Company signed an amended agreement with Industrial Technologies Office deferring commencement of royalty repayments to April 30, 2012 and subsequent years.

d) Convertible Loan

On September 27, 2012 the Company converted into common shares (note 18g) the principal portion of the convertible loan, which had the following terms and conditions:

On April 16, 2010, the Company completed a secured subordinated convertible loan with a principal amount of $1,771,000 which was convertible into common shares.

The secured subordinated convertible loan was provided by Panta Canada B.V., a related party. The loan, which was evidenced by a promissory note, had a five year term with an interest rate of 6% per year; it was secured by a security interest in all of the Company's present and after-acquired personal property and a floating charge on land which ranked subordinate to all liens, charges and security interests disclosed. The $1,771,000 principal amount was converted into common shares at a conversion price of $0.07 per common share. The $259,000 accumulated interest, which was not convertible, was paid concurrently with the principal conversion.

The loan was classified into its debt and equity components using the credit adjusted rate. The carrying amount of the financial liability was first determined by discounting the stream of future principal and interest payments at the rate of interest (12.0%) as specified within the convertible loan agreement under circumstances which would have taken effect where the convertibility feature had not been approved by a vote of the common shareholders. The equity component equaled the amount determined by deducting from the carrying amount of the compound instrument the amount of the debt component. For accounting purposes, the debt component was assigned a value of $1,318,000 and the conversion rights were assigned a value of $453,000. The convertible loan, net of accreted interest as at the date of conversion amounting to $247,000, has been reclassified into equity.

e) Term Loan

On September 27, 2012 the Company repaid in full the term loan and accrued interest having the following terms and conditions:

On May 24, 2011, the Company completed a secured subordinated term loan with a principal amount of $6,000,000. The Company received full funding from the loan on July 8, 2011.

The secured subordinated term loan was provided by Panta III B.V., a related party. The loan, which was evidenced by a promissory note, had a five year term; was secured by a security interest in all of the Company's present and after-acquired personal property and a floating charge on land which ranked subordinate to all liens, charges and security interests disclosed. Interest was calculated, compounded, and paid monthly. Prepayments in whole or in part of the loan were permitted at any time without penalty. As per the requirements of the Toronto Stock Exchange, exercise of the conversion right of the loan into 85,714,286 common shares at a conversion price of $0.07 per common share was subject to disinterested shareholder approval, which approval was sought at the 2011 annual meeting of shareholders on June 16, 2011. As the conversion feature of the loan was not approved by the Company's shareholders at its Annual Meeting, the interest rate under the loan became 15% per annum.

As partial consideration for the loan, the Company issued to Panta III B.V., 19,550,532 common share purchase warrants, each warrant exercisable on or before January 1, 2015 with respect to one common share at an exercise price of $0.0713 per common share. The fair value of the warrants issued has been treated as a $617,000 transaction cost and has been accreted over the loan term. The unamortized portion of the fair value of the warrants has been recorded as a $397,000 charge against income as at the September 27, 2012 loan repayment date.

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

17. Obligations and Commitments Under Finance and Operating Leases

The Company has committed to payments under certain capital and operating leases relating to manufacturing machinery and equipment, and building lease costs. Future minimum lease payments required in each of the next five fiscal years and thereafter are:

FOR THE YEAR ENDED DECEMBER 31		**2012**		2011
	Operating	**Finance**	Operating	Finance
2012	**$ -**	**$ -**	$ 2,558	$ 699
2013	**2,504**	**97**	2,553	228
2014	**2,497**	**75**	2,546	-
2015	**2,398**	**67**	2,447	-
2016	**2,412**	**-**	2,461	-
2017	**2,412**	**-**	2,461	-
Thereafter	**1,774**		1,799	-
Total future minimum lease payments	**13,997**	**239**	16,825	927
Less: Imputed interest	**n/a**	**(31)**	n/a	(39)
Balance of obligation under finance leases included in long-term debt (note 16b)	**-**	**208**	-	888

For the year ended December 31, 2012, an amount of $2,507,000 representing payments under operating leases was expensed (December 31, 2011: $2,466,000).

As at December 31, 2012 the Company had $14,883,000 of committed contractual operational purchase order obligations outstanding (December 31, 2011: $16,732,000).

18. Capital Stock

Authorized

The Company is authorized to issue an unlimited number of common shares as well as an unlimited number of first preferred and second preferred shares, issuable in series, the terms of which are determined by the directors at the time of creation of each series.

Common shares issued or reserved:

	Number of shares	**Amount**
December 31, 2010	195,505,323	72,927
Share issue (i)		
Non-cash	6,488,790	324
December 31, 2011	201,994,113	73,251
Share issue (h)		
Cash	23,172,552	973
Non-cash (b, c, d, e, f, g)	29,731,407	1,993
December 31, 2012	254,898,072	76,217

a) The Company has reserved a total of 21,688,720 common shares for issuance, the maximum number that may be exercised under the terms of the convertible debenture due on March 31, 2016 (note 16a).

b) On January 10, 2012, the Company completed a private placement of 1,173,126 common shares in consideration of $55,000 interest accrued for the period from July 1, 2011 to September 30, 2011 on the Export Development Canada convertible debenture (note 16a).

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

c) On February 6, 2012, the Company completed a private placement of 1,150,395 common shares in consideration of $55,000 interest accrued for the period from October 1, 2011 to December 31, 2011 on the Export Development Canada convertible debenture (note 16a).

d) On April 4, 2012, the Company completed a private placement of 107,575 common shares in consideration of a $4,000 payment to the former principal shareholders of Comtek Advanced Structures Ltd., under the terms of a Share Purchase Agreement.

e) On April 20, 2012, the Company completed a private placement of 1,008,142 common shares in consideration of $54,000 interest accrued for the period from January 1, 2012 to March 31, 2012 on the Export Development Canada convertible debenture (note 16a).

f) On September 21, 2012, the Company completed a private placement of 992,169 common shares in consideration of $54,000 interest accrued for the period from April 1, 2012 to June 30, 2012 on the Export Development Canada convertible debenture (note 16a).

g) On September 27, 2012, the Company issued 25,300,000 common shares at $0.07 per share for a book value of $1,771,000, pursuant to the terms of a loan agreement entered into between the Company and Panta Canada B.V. on April 16, 2010 (note 16d).

h) On September 28, 2012, the Company completed a private placement of 23,172,552 common shares at $0.042 per share for gross proceeds of approximately $973,000. The subscriber in the private placement was Panta Canada B.V.

i) On August 15, 2011, the Company completed a private placement of 6,488,790 common shares in consideration of $324,000 interest accrued to June 30, 2011 on the Export Development Canada convertible debenture (note 16a).

j) The Company's incentive stock option plan is administered by the Board of Directors. At the 2010 Annual General Meeting, a Resolution was passed changing the Corporation's 2007 share option plan, from a fixed plan wherein 3,166,667 common shares are reserved for issuance, to a rolling share option plan wherein 10% of the issued and outstanding common shares at the time an option is granted be reserved for issuance.

A summary of the Company's stock options issued as of December 31, 2012 and December 31, 2011, and changes during the periods ending on those dates, are presented below.

FOR THE YEAR ENDED DECEMBER 31		**2012**		2011
	Options	**Weighted average exercise price**	Options	Weighted average Exercise price
Outstanding - Beginning of year	**8,035,500**	**$ 0.05**	8,766,000	$ 0.05
Granted	**3,230,500**	**0.05**	-	-
Forfeited	**-**	**-**	730,500	0.05
Exercised	**-**	**-**	-	-
Outstanding - End of year	**11,266,000**	**0.05**	8,035,500	0.05

The following table summarizes stock options outstanding and exercisable as at December 31, 2012:

	Number	**Weighted average remaining contractual life (years)**	**Weighted average exercise price**
$0.05 - $0.06	11,266,000	2.97	$ 0.05

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

k) The Company's contributed surplus is comprised as follows:

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Beginning of year	**$ 3,424**	$ 2,662
Stock-based compensation expense	**115**	145
Fair value of warrants	**-**	617
End of year	**3,539**	3,424

l) During 2011 19,550,532 warrants were issued having a fair value of $617,000 (note 16e). Each warrant is exercisable on or before January 1, 2015 with respect to one common share at an exercise price of $0.0713 per common share.

19. Preferred Shares

On July 10, 2006, the Company issued 1,200,000 preferred shares at an issue price of $10.00 per preferred share. Gross proceeds from the 2006 issuance of preferred shares amounted to $12,000,000. The costs of issuing the preferred shares during 2006 amounted to $546,000 and were deducted from the gross proceeds.

The preferred shares provide for a 9.25% per annum dividend, payable quarterly in cash on the last day of March, June, September and December. Dividend payments have been deferred since January 2009. Unpaid dividends as at December 31, 2012 amounted to $3,024,000 (December 31, 2011: $2,268,000).

Each preferred share is convertible at any time, without the payment of additional consideration, at the option of the holder into 3.64 common shares, at a conversion price of $2.75 per common share.

The conversion price will be subject to adjustment in certain circumstances pursuant to customary anti-dilution provisions.

At any time after June 30, 2011, the preferred shares will be redeemable in whole or in part at the option of the holder at the issue price plus all accrued and unpaid dividends thereon calculated to the date of redemption if:

- at any time after that date the current market price on the fifth day prior to such date is less than $2.75; or
- there is a change in control of the Company involving the acquisition of voting control or direction over 66-2/3% or more of the common shares.

The Company's governing corporate statute is the Canada Business Corporations Act (the "CBCA"). Under the CBCA, the Company may not purchase or otherwise acquire its own shares, including redeeming the preferred shares, if there are reasonable grounds for believing that the Company would after the purchase be unable to pay its liabilities as they become due. The Company's board has determined that honouring any redemption request for preferred shares, regardless of the number of shares involved, would result in the Company being unable to pay its liabilities as they become due.

While the Company currently is able to meet its existing obligation, it is reliant on certain credit and loan facilities for the normal, ongoing operation of its business. Those operating facilities currently provide that it is an event of default if the Company redeems any of its preferred shares. The inability of the Company to access its customary operating facilities would impair the proper operation of the Company's business and prohibit it from meeting, in the normal course, its liabilities as they become due. Accordingly, at this time the Company is prohibited from completing any redemption of preferred shares.

Prior to December 31, 2008, holders of preferred shares converted 383,200 preferred shares resulting in 816,800 preferred shares remaining having a $8,168,000 gross book value, which net of issuance $546,000 costs results in a $7,622,000 net book value.

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

20. Stock based Compensation

The Company records compensation expense for the fair value of the stock options granted under its incentive stock option plan using the Black-Scholes option-pricing model. This model determines the fair value of stock options granted and amortizes it to earnings over the vesting period.

The fair value of 3,230,500 options granted during the year ended December 31, 2012 was $100,000 (December 31, 2011: $Nil).

The assumptions used in the valuation of stock options were as follows:

	2,500,000 Options	**730,500 Options**
Risk-free rate (%)	1.30	1.57
Dividend yield (%)	0	0
Expected Lives (years)	3.5	3.8
Volatility (%)	86.09	84.62

The amount of stock-based compensation expense, for options granted in current and prior periods, amortized to earnings during the year ended December 31, 2012 was $115,000 (2011: $145,000).

The Black-Scholes option-pricing model used by the Company to calculate option values was developed to estimate the fair value of freely tradeable, fully transferable options without vesting restrictions, which significantly differ from the Company's stock option awards. Changes in the subjective input assumptions can materially affect the fair value estimate, and therefore, the existing models do not necessarily provide a reliable, single measure of the fair value of options granted by the Company.

21. Defined Contribution Plan

The total cost recognized and paid for the Company's defined contribution plan is as follows.

FOR THE YEAR ENDED DECEMBER 31	**2012**	2011
Defined contribution plan	**$ 1,447**	$ 1,411

The Company's contribution to the plan is calculated on a percentage of employee wages. The range of percentages is 1.5% to 9.5%. The plan is available to all employees.

22. Finance Costs

FOR THE YEAR ENDED DECEMBER 31	**2012**	2011
Interest on capital leases	**$ 37**	$ 95
Interest on other long-term debt	**306**	348
Interest on short-term debt	**71**	473
Interest on related party debt	**747**	578
Preferred share dividends accrued	**756**	756
Accretion of equity component of convertible loan	**67**	85
Accretion of fair value of warrants	**132**	88
Net interest expense	**2,116**	2,423

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

23. Supplementary Cash Flow Information

Non-cash financing and investing activities are as follows:

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Debt and interest paid using common shares	**$ 1,993**	$ 324
Equipment acquired under capital lease	**220**	-
Fair value of warrants issued	**-**	617
Equity component of convertible loan	**247**	-
Uncollected deferred revenue	**706**	2,876

24. Warranty Provisions

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Opening balance	**$ 85**	$ 167
Charge/(credit) to the statement of income:		
Additions	**-**	-
Increases(decreases) to existing provisions	**-**	(54)
Accretion	**-**	-
Used during year	**-**	(28)
	85	85

During 2010, the Company provided for $428,000 of expected warranty expenditures relating to a manufacturing deficiency. All rectifications have not been completed by the date of this report, and $85,000 remains provisioned for expected future expenditures.

25. Income Tax

A reconciliation of income tax at statutory rates to actual income taxes is as follows:

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Statutory tax rate	**25.0%**	26.5%
Income tax (recovery) at the statutory income tax rate	**$ 5,161**	$ (650)
Adjustment of provision to tax return	**624**	121
Difference between current and future tax rates	**-**	48
Change in unrecognized deferred tax assets	**138**	178
Benefit of losses not previously recognized	**(6,286)**	-
Non-deductible preferred share dividends	**188**	200
Other	**175**	103
Tax expense	**-**	-

The provision for income tax expense (recovery) is based on the combined federal and provincial annual income tax rate expected for the full financial year of 25.0%. The tax rate has decreased by 0.5% from December 31, 2011 due to a federal corporate tax rate reduction.

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

Deferred tax assets are recognized for deductible temporary differences, unused tax losses, and unused tax credits to the extent that the realization of the related tax benefit through future taxable profits is probable. The Company did not recognize deferred income tax assets of $14,823,000 (2011: $20,551,000) in respect of losses amounting to $21,310,000 (2011: $45,150,000) which expire beginning in 2013 through 2032, unclaimed research and development costs of $10,421,000 (2011: $10,319,000) with no expiry, and investment tax credits of $3,057,000 (2011: $3,057,000) which expire beginning in 2017 through 2030, and deductible temporary differences of $18,221,000 (2011: $17,564,000).

26. Related Party Transactions

a) During the current year a performance guarantee was provided by a certain shareholder and director on production contracts with a certain customer. Fees paid to a certain shareholder and director during the year ended December 31, 2012 amounted to $38,000 (December 31, 2011: $Nil). Fees payable to a certain shareholder and director as at December 31, 2012 are $17,000 (December 31, 2011: $Nil). These fees are included in the statements of income and comprehensive income as cost of sales and amount to $55,000 for the year ended December 31, 2012 (December 31, 2011: $Nil).

b) During the year ended December 31, 2012, consulting services were provided by certain directors. Fees paid to certain directors, or companies with which they have beneficial ownership, during the year ended December 31, 2012 amounted to $62,000 (December 31, 2011: $80,000). Fees payable to certain directors or Companies with which they have beneficial ownership, as at December 31, 2012 are $14,000 (December 31, 2011: $Nil). These fees are included in the statements of income and comprehensive income as administrative and general expenses and amount to $76,000 for the year ended December 31, 2012 (December 31, 2011: $78,000).

c) Key management compensation

Key management includes Executive Officers for all operating facilities. The compensation paid or payable to key management for employee services is shown below.

FOR THE YEAR ENDED DECEMBER 31	**2012**	2011
Salaries and other short-term employee benefits	**$ 751**	$ 642
Contributions to defined contribution plan	**39**	34
Option-based awards	**12**	26
	802	702

d) Loans to related parties

The balance of loans receivable from key management as at December 31, 2012 is $15,000 (December 31, 2011: $15,000).

Other related-party transactions are disclosed elsewhere in these consolidated financial statements (notes 16d, 16e, 18g and 18h).

These transactions were conducted in the normal course of business and were accounted for at the exchange amount.

27. Economic Dependence and Segmented Information

a) Sales to four major customers for the year ended December 31, 2012, which comprise several programs and contracts, accounted for approximately 85.0% (December 31, 2011: 85.4%) of sales.

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

FOR THE YEAR ENDED DECEMBER 31	2012		2011	
	Revenue	**% of Total**	Revenue	% of Total
BAE Systems	**$ 15,193**	**17.0**	$ 3,666	4.2
Boeing	**29,961**	**33.6**	26,887	31.3
Bombardier	**16,784**	**18.8**	17,062	19.8
Cessna	**14,055**	**15.7**	25,883	30.1
Other	**13,344**	**14.9**	12,520	14.6
Total	**89,337**	**100.0**	86,018	100.0

b) The Company operates in one industry that involves the manufacture and sale of aerospace products. All of the Company's operations and assets are in Canada. The Company operates from two locations in Canada.

Comtek Advanced Structures Ltd. a wholly owned subsidiary is located in Ontario and is dedicated to composites manufacturing. Avcorp Industries Inc. is located in British Columbia and is dedicated to light weight metal manufacturing and assembly. Revenues, incomes (loss) and total assets are distributed by operating segment as noted in the tables below.

FOR THE YEAR ENDED DECEMBER 31	2012		2011	
	Revenue	**% of Total**	Revenue	% of Total
Avcorp Industries Inc.	**$ 75,543**	**84.6**	$ 74,236	86.3
Comtek Advanced Structures Ltd.	**13,794**	**15.4**	11,782	13.7
Total	**89,337**	**100.0**	86,018	100.0

FOR THE YEAR ENDED DECEMBER 31	2012		2011	
	Income (loss)	**% of Total**	Income (loss)	% of Total
Avcorp Industries Inc.	**$ 20,826**	**100.0**	$ (2,004)	81.7
Comtek Advanced Structures Ltd.	**(185)**	**(0.00)**	(448)	18.3
Total	**20,641**	**100.0**	(2,452)	100.0

FOR THE YEAR ENDED DECEMBER 31	2012		2011	
	Total Assets	**% of Total**	Total Assets	% of Total
Avcorp Industries Inc.	**$ 64,110**	**93.4**	$ 51,247	93.2
Comtek Advanced Structures Ltd.	**4,525**	**6.6**	3,714	6.8
Total	**68,635**	**100.0**	54,961	100.0

28. Other Operating Income

On November 16, 2012, the Company received the determination of an appointed arbitration panel constituted to adjudicate outstanding issues relating to cost reimbursements and compensation payable to the Company in connection with the transition of Cessna production work back to Cessna and other suppliers. The transition of Cessna production work was first announced by the Company on December 17, 2010 and immediately following notification by Cessna, the Company had attempted to negotiate compensation payments as contemplated by the Cessna Strategic Alliance Agreement ("SAA"). Only when negotiations and mediation were unsuccessful did the Company refer the matter to binding arbitration.

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

The binding arbitration award, delivered to the Company on November 16, 2012, determined that: the SAA was an exclusive agreement between Cessna and Avcorp; Cessna could not unilaterally transition production work from Avcorp; Avcorp had fulfilled the requirements of the SAA; and, Avcorp suffered damages as a result of Cessna transitioning production work from Avcorp. In addition, all counterclaims that were advanced by Cessna were denied. The quantum of damages was assessed by the arbitration panel at $27,391,000, which amount was payable to Avcorp within thirty days of the arbitration award. Accordingly, the Company has recorded the amount owed to it as an Other receivable.

On November 26, 2012 Cessna filed a complaint in the United States District Court For The District Of Kansas seeking to vacate the award as a manifest disregard for the law and in violation of public policy.

On December 21, 2012 Avcorp filed a memorandum in support of a motion to confirm final arbitration award, and dismiss the complaint in the United States District Court For The District Of Kansas.

It is Management's opinion that the US court will not re-hear the case nor pass judgement on the merits of the arbitration panel's binding final decision. The court's review will consider:

1. Whether the award was procured by corruption, fraud, or undue means;
2. Whether there was evident partiality or corruption in the arbitrators;
3. Whether the arbitrators were guilty of misconduct in refusing to postpone the hearing, upon sufficient cause shown, or in refusing to hear evidence and material to the controversy; or of any misbehavior by which the rights of any party have been prejudiced; or
4. Whether the arbitrators have exceeded their powers, or so imperfectly executed them that a mutual, final, and definite award upon the subject matter submitted was not made.

The amounts disclosed in the table represent the binding award net of the associated costs.

FOR THE YEAR ENDED DECEMBER 31	2012
Other operating income	$ 27,391
Revenue:	
Sale of tools	(120)
Cost of sales:	
Inventories	983
Development costs	2,034
Supplier tooling charge	46
	3,063
Administrative and general expenses:	
Legal and arbitration expenses	2,231
Severance expenses	205
	2,436
Write-down of equipment	464
Net arbitration award	21,548

(prepared in accordance with IFRS, all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)

29. Earnings per share

Basic earnings per share amounts are calculated by dividing the net income (loss) for the year attributable to common equity holders of the parent by the weighted average number of common shares outstanding during the year.

Diluted earnings per share amounts are calculated by dividing the net profit attributable to common equity holders of the parent (after adjusting for dividends on the convertible preferred shares and interest on the convertible debenture) by the weighted average number of common shares outstanding during the year plus the weighted average number of common shares that would be issued on conversion of all the dilutive potential common shares into common shares. During 2012 dividends on the convertible preferred shares and interest on the convertible debenture are anti-dilutive, and therefore are not included in the calculation of diluted earnings.

The following reflects the share data used in the basic and diluted earnings per share computations:

FOR THE YEAR ENDED DECEMBER 31	2012	2011
Weighted average number of common shares for basic earnings per share[1]	**217,775**	197,959
Effect of dilution:		
Share options	**309**	-
Weighted average number of ordinary shares adjusted for the effect of dilution[1]	**218,084**	197,959

[1]The weighted average number of shares take into account the weighted average effect of changes in treasury share transactions during the year.

There have been no other transactions involving common shares or potential common shares between the reporting date and the date of authorization of these consolidated financial statements.

AVCORP INDUSTRIES INC.

BOARD OF DIRECTORS AND OFFICERS

David Levi [(1)(2)(3)]
CHAIRMAN OF THE BOARD
President and CEO
GrowthWorks Capital Ltd.
Vancouver, British Columbia

Jaap Rosen Jacobson [(2)]
DIRECTOR
President
Panta Holdings B.V.
Mijdrecht, The Netherlands

Eric Kohn *TD* [(1*)(2*)]
DIRECTOR
Managing Partner
Barons Financial Services SA
Geneva, Switzerland

Ray Castelli [(1)]
DIRECTOR
Chief Executive Officer
Weatherhaven
West Vancouver, BC

Kees de Koning [(3)]
DIRECTOR
Nootdorp, The Netherlands

Elizabeth Otis [(3*)]
DIRECTOR
Seattle, Washington, USA

Mark van Rooij [(3)]
DIRECTOR
President and Chief Executive Officer
White Rock, British Columbia

(1) Member of the Audit and Corporate Governance Committee
(2) Member of the Compensation and Nominating Committee
(3) Member of the Executive Committee

* Designates the Committee Chair

MANAGEMENT

Edward M. Merlo
CORPORATE SECRETARY
Vice President, Finance
Richmond, British Columbia

Larry Glenesk
Vice President, Business Development, Defense
White Rock, British Columbia

Amandeep Kaler
Vice President, Operations
Surrey, British Columbia

Ken McQueen
Vice President, Organization Development
New Westminster, British Columbia

Josie Monterosso
Vice President, Supply Chain
White Rock, British Columbia

Jeff Schoenfeld
Vice President, Engineering and Development
Vancouver, British Columbia

Paul Wiggum
Vice President, Sales & Marketing
White Rock, British Columbia

DIRECTORY

Legal Counsel

McMillan LLP
Barristers & Solicitors
Vancouver, British Columbia

Auditors

Ernst & Young LLP
Chartered Accountants
Vancouver, British Columbia

Shares Listed

Toronto Stock Exchange
Symbol AVP

Registrar and Transfer Agent

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Vancouver, British Columbia

Bank

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