AVCORP

first quarter report 2010

ABOUT AVCORP INDUSTRIES INC. Avcorp designs and builds major airframe structures for some of the world's leading aircraft companies, including Boeing, Bombardier, and Cessna. With more than 50 years of experience, 507 skilled employees and 354,000 square feet of facilities, 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. 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 May 12, 2010, and should be read in conjunction with the Company's unaudited interim consolidated financial statements and notes thereto for the three month period ended March 31, 2010 and with the audited financial statements and notes thereto for the year ended December 31, 2009.

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. One dedicated to composites, Comtek Advanced Structures Ltd. a wholly owned subsidiary located in Ontario, and the other dedicated to light weight metal manufacturing, Avcorp Industries Inc. located in British Columbia.

Avcorp is in compliance with Industry Standard Quality requirements.

Financial Overview

Quarterly Results

The following table provides selected unaudited quarterly financial information for the eight most recent fiscal quarters to March 31, 2010.

QUARTERLY RESULTS
unaudited, prepared in accordance with Canadian GAAP, expressed in thousands of Canadian dollars except per share amounts

	2010	2009				2008		
For the three months ended	Mar 31	Dec 31	Sep 30	Jun 30	Mar 31	Dec 31	Sep 30	Jun 30
Revenue	$ 17,376	$ 16,641	$ 14,302	$ 16,172	$ 22,087	$ 34,434	$ 30,894	$ 32,389
Income (loss) from operations	(2,073)	(1,936)	(2,128)	552	(1,989)	(1,561)	1,004	859
EBITDA[1,2]	(1,084)	(1,377)	(1,103)	1,530	(1,550)	1,141	1,676	2,218
Net income (loss)	(2,330)	(2,718)	(2,585)	65	(3,172)	(1,972)	(220)	364
EBITDA per share[1,2]								
Basic	(0.01)	(0.01)	(0.02)	0.05	(0.05)	0.04	0.05	0.07
Diluted	(0.01)	(0.01)	(0.02)	0.05	(0.05)	0.04	0.05	0.07
Net income (loss) per share								
Basic	(0.01)	(0.02)	(0.06)	0.00	(0.10)	(0.06)	(0.01)	0.01
Diluted	(0.01)	(0.02)	(0.06)	0.00	(0.10)	(0.06)	(0.01)	0.01
Long-term debt	2,380[3]	1,811[3]	2,034[3]	2,387[3]	2,843[3]	2,872[3]	7,192	7,424

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

Three Months Ended March 31, 2010 and 2009 Results Overview

During the quarter ended March 31, 2010, the Company recorded a loss from operations of $2,073,000 on $17,376,000 revenue, as compared to a $1,989,000 loss from operations on $22,087,000 revenue for the same quarter of the preceding year; and a net loss for the current quarter of $2,330,000 as compared to a net loss of $3,172,000 for the quarter ended March 31, 2009.

Continued reduced customer demand has resulted in idle plant capacity. The Company has expensed $1,333,000 of overhead costs during the current quarter (March 31, 2009: $Nil) which under normal production levels would have been inventoried, then expensed at a later time when the product is sold.

The Company has increased its provision for loss making contracts by $105,000 during the current quarter, primarily as a result of the adverse impact the strengthening of the Canadian dollar relative to the US dollar has had on US dollar denominated sales.

During the current quarter 2010 the Company provisioned for $417,000 of expected warranty expenditures relating to a manufacturing deficiency arising within its supply chain. This provision is in addition to the $1,647,000 balance of warranty expenditures previously provided for to December 31, 2009.

The Company has established specific program restart projects in an effort to mitigate program start-up inefficiencies. These actions include process flow improvements such as jig modifications, upgrade of manufacturing assembly planning documents, as well as balancing inventory throughout the supply chain. Costs amounting to $192,000 have been expensed within these program restart projects.

It should be noted that the current quarter loss includes a $42,000 foreign exchange gain (March 31, 2009: $1,044,000 foreign exchange loss) which occurred as a result of holding foreign-currency-denominated receivables, payables and debt.

Subsequent to the quarter, the Company filed a motion to introduce proceedings in the Superior Court of Quebec for compensation as a result of the termination of a procurement contract. The Company is seeking compensation in excess of $18,000,000 for unrecovered costs incurred in accordance with the termination for convenience provisions of a contract terminated by the customer in 2007. The Company and the customer have been in discussions regarding this claim however, no resolution was reached prior to the limitation period expiring. The customer has, as at the date of this report, rejected the Company's claim. As at the date of this report, no statement of defence has been filed and no court date has been set. During the quarter ended March 31, 2010 the Company incurred $151,000 of legal and consulting fees in the course of negotiating, analyzing and documenting the termination compensation.

The Company expects revenue growth in 2010 from full rate production of the Boeing Defense Space & Security CH47 helicopter and the Cessna Citation CJ4 business jet; both programs were in start-up phase for the Company in 2009. Additionally, the Company will experience moderate revenue growth during the second half of 2010 as a result of program re-starts and production rate increases.

Cash flows from operating activities during the current quarter utilized $1,016,000 of cash, as compared to utilizing $681,000 of cash during the quarter ended March 31, 2009. The Company has a working capital surplus of $1,761,000 as at March 31, 2010 (December 31, 2009: $820,000 surplus) and an accumulated deficit of $67,895,000 at March 31, 2010 (December 31, 2009: $65,379,000).

The Company has operating lines of credit with a Canadian chartered bank totalling $15,000,000 (March 31, 2009: $17,000,000). The facilities are due on demand. It should be noted that the credit available to the Company under its operating line of credit is equal to the amount determined by margin formula less $1,000,000.

On March 11, 2010, the Company entered into a Forbearance Agreement with the bank providing its operating lines of credit. The Forbearance Agreement ends on June 9, 2010. The Company is subject to a quarterly review within which the Bank determines if there has occurred an event of default. Provided no default has occurred, the Forbearance Agreement is extended for a recurring period of 90 days.

On March 1, 2010, the Company completed a private placement of 17,773,211 common shares at $0.055 per share for gross proceeds of approximately $978,000. Subscribers in the private placement were Panta Holdings B.V. (Panta), which subscribed for 15,995,890 common shares, and Working Opportunity Fund (EVCC) Ltd., which subscribed for 1,777,321 common shares. The common shares issued under the private placement are subject to a restriction on resale for a period of four months and one day from the date of issue, in accordance with applicable Canadian securities laws.

On April 16, 2010, the Company completed a secured subordinated convertible loan in a principal amount of $1,771,000, which, subject to shareholder approval, is convertible into a maximum of 29,516,666 common shares. Funding of the principal amount occurred on April 21, 2010.

The secured subordinated convertible loan was provided by Panta Holdings B.V. through a wholly-owned subsidiary. The loan, which is evidenced by a promissory note, has a five year term with an interest rate of 6% per year. The $1,771,000 principal amount is convertible into common shares at a conversion price of $0.06 per common share in the first two years of the loan, $0.07 per common share in the third and fourth years of the loan, and $0.08 per common share in the fifth year of the loan. Accumulated interest will not be convertible.

As per the requirements of the Toronto Stock Exchange, exercise of the conversion right of the loan is subject to disinterested shareholder approval, which approval is being sought at the 2010 annual meeting of shareholders to be held on May 18, 2010. If the

conversion right is not approved at the meeting, the interest rate on the loan will change from 6% per year to 12% per year, and the loan will become payable on demand.

Assuming full conversion of the loan into the maximum 29,516,666 common shares, Panta will hold 117,830,842 common shares, representing approximately 52.4% of Avcorp's outstanding shares.

The proceeds from the convertible loan will be used for working capital purposes, and to fund tooling and equipment.

The Company is currently working on the completion of obtaining additional debt and equity to provide working capital financing for anticipated revenue growth in 2010 and into 2011.

Going Concern

As at March 31, 2010, the Company was not in compliance with a financial covenant associated with its operating lines of credit. In addition, the Company is forecasting that it will be in default of one or more of its covenants in the next 12 months. In the absence of obtaining a waiver of such breach, the lender is entitled to demand immediate payment. The lender had agreed to forbear from demanding payment of the indebtedness and from taking steps to enforce the security, subject to the Company complying with terms and conditions of a Forbearance Agreement which ends on June 9, 2010.

Also, as at March 31, 2010, the Company was not in compliance with a financial covenant associated with the convertible debenture held by Export Development Canada. The Company has obtained a waiver from the debenture holder for this non-compliance; it has not obtained a waiver for anticipated future breaches. In the absence of obtaining a waiver of such future breaches, the lender would be entitled to demand payment. Accordingly, the convertible debenture is classified as current debt. The Company is required to maintain certain measures of working capital, debt to tangible net worth, and debt service coverage.

During June 2009, the Company's Board of Directors resolved to defer Preferred Share dividends until January 2011. The Company has not paid $942,000 of preferred share dividends which were accrued and payable as at March 31, 2010.

The consolidated financial statements of the Company have been prepared in accordance with Canadian generally accepted accounting principles (GAAP) applicable to a going concern, which contemplates the realization of assets and liquidation of liabilities during the normal course of operations. The conditions and risks noted above cast significant doubt on the validity of that assumption. The Company forecasts its financing requirements in the next 12 months to exceed the current availability of the operating line of credit. Accordingly, the Company has completed a private placement and rights offering, and will continue its efforts to obtain additional debt financing, renegotiate debt repayments, issue additional common shares, reduce operating expenses and maintain existing terms regarding customer collections in order to provide liquidity in excess of forecasted requirements. However, the success of these activities cannot be assured.

These consolidated financial statements do not reflect adjustments to the carrying value of assets and liabilities, the reported revenues and expenses, and balance sheet classifications used that would be necessary if the going concern assumption were not appropriate; such adjustments could be material.

Revenue

Revenue for the quarter ended March 31, 2010 was $17,376,000 as compared to $22,087,000 for the quarter ended March 31, 2009. Revenues from the Company's customers are as follows.

REVENUE DISTRIBUTION

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

For the quarter ended March 31	2010		2009	
	Revenue	% of Total	Revenue	% of Total
Boeing	$ 6,556	37.7	$ 4,221	19.1
Bombardier	5,041	29.0	5,677	25.7
Cessna	3,818	22.0	8,538	38.7
Other	1,961	11.3	3,651	16.5
Total	17,376	100.0	22,087	100.0

Shipments of large assemblies to Boeing Commercial Airplane Group (Boeing), specifically for the 737 commercial jet program increased by 25% during the first quarter 2010 relative to the same quarter in 2009. The lower 2009 shipments were due to a burn-off of inventories which had accumulated during Boeing's 2008 work stoppage. The primary source of revenue from Boeing is from the 737 aircraft. During the second quarter 2009 the Company commenced delivering components to Boeing Defense, Space & Security for the Chinook CH47 helicopter. The Company achieved full rates of production parts for this program during 2009, with the intent to deliver larger assembled structures in 2011. The Company continues to work towards obtaining additional new contracts supporting Boeing commercial jet programs.

Deliveries to Bombardier Aerospace (Bombardier) increased by 13% for the Challenger CL605, with a slight revenue decrease for the CL850 business jet program during the current quarter relative to the quarter ended March 31, 2009. The Company's primary source of revenues from Bombardier in 2010 will continue to be from components on the CL605 and CL850 business jets, and composite floor boards for the CRJ and Q400 aircraft programs.

Deliveries of major structures to Cessna were 33% lower during the first quarter 2010, relative to the first quarter 2009. The reduction in deliveries was precipitated by a reduction in aircraft deliveries by Cessna as well as a burn-off of inventories by this customer. The primary sources of revenue from Cessna are from deliveries of components for the Citation Sovereign business jet, the Citation CJ3 business jet and the Citation CJ4 business jet. A continuation of deliveries for components of these aircraft is expected to comprise the majority of revenues from Cessna for 2010. Citation CJ3 component deliveries are expected to increase slightly, while deliveries of Citation Sovereign components are expected to show moderate increases for the remainder of 2010 relative to the first quarter of this year. The first deliveries for the Citation CJ4 business jet components commenced during 2009 and have reached full rates of production in 2010.

Deliveries of Boeing 757 commercial jets wing adapter plugs for winglet retrofit to Aviation Partners Boeing have fallen by 75% relative to the quarter-ended March 31, 2009. This is as a result of decreased demand for these aircraft retrofits by airlines.

Revenues for Comtek Advanced Structures Ltd. (Comtek) decreased by approximately 45% during the first quarter 2010 relative to 2009. The reduction in revenue was primarily attributable to the cessation in deliveries of composite structures to a tier-one supplier for the Airbus 380, and reduced deliveries for composite floor boards.

Revenues have decreased by 17% during the current quarter relative to the same quarter in 2009 as a result of the impact the strengthening in the Canadian dollar relative to the US dollar has had on US dollar denominated sales.

Gross Profit

Gross profit (revenue less cost of sales) for the quarter ended March 31, 2010 was 9.0% of revenue as compared to 14.2% of revenue for the quarter ended March 31, 2009.

Gross profit has declined during the current quarter, relative to the same quarter in the preceding year, because reduced revenues resulting from reduced customer demand has had an adverse impact on the Company's cost structure.

Overhead costs incurred in support of operational capabilities, as well as quality and engineering systems expenditures, have become significant relative to the revenues the business is generating. Costs expensed as a result of idle plant capacity amounted to $1,333,000 during the quarter. This cost-revenue imbalance can be partially mitigated in 2010 by new program revenue growth, which should occur with full rate production for the Citation CJ4 business jet components and full year delivery of components to Boeing Defense, Space & Security for the CH47 helicopter. Costs expensed as a result of idle capacity have been reduced relative to the immediately preceding quarter.

The Company has increased its provision for loss making contracts by $105,000 during the current quarter, primarily due to the adverse impact on US dollar sales resulting from the strengthening of the Canadian dollar relative to the US dollar.

As the workforce has been reduced, the remaining employees are relatively senior in pay-grade and consequently the average wage and benefit rate the Company pays has increased. As the Canadian dollar has strengthened the cost of materials used in production have fallen for those materials purchased in US dollars.

A re-tooling of plant-floor processes as well as anticipated new program revenue growth will be the largest factors in reducing the Company's cost structure and contributing towards offsetting idle capacity costs.

Administration and General Expenses

As a percentage of revenue, administration and general expenses increased from 13.7% for the quarter ended March 31, 2009 to 15.7% for 2010, primarily as a result of reduced revenues in the first quarter 2010 relative to the same quarter in 2009. In absolute terms, the administrative and general expenses were reduced by $287,000 for the quarter ended March 31, 2010 relative to last year. The Company incurred legal and consulting fees in the course of negotiating, analyzing and documenting termination claim it is pursuing with a customer. These are one-time costs for which fees amounting to $151,000 were expensed during 2010.

Foreign Exchange Gain

The Company recorded a $42,000 foreign exchange gain during the first quarter 2010 (March 31, 2009: $1,044,000 loss) as a result of holding foreign-currency-denominated receivables, payables and debt.

Earnings Before Interest, Taxes, Depreciation & Amortization

Earnings before interest, taxes, depreciation and amortization (EBITDA) was a $1,084,000 loss for the quarter ended March 31, 2010 compared to a negative EBITDA of $1,550,000 for the quarter ended March 31, 2009.

EBITDA

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

For the quarter ended March 31	2010	2009
Income (loss) for the period	$ (2,330)	$ (3,172)
Interest expense and financing charges	257	529
Income tax expense	-	-
Depreciation	867	982
Amortization of development costs and intangible assets	122	111
	(1,084)	(1,550)

Interest and Financing Charges

Total interest and financing charges on both short- and long-term debt, some to related parties, for the quarter ended March 31, 2010 was $257,000 as compared to $529,000 for the same quarter in the previous year. The reduction in interest and financing charges for the first quarter 2010 is primarily as a result of having less debt than in the first quarter 2009, a reduction in royalty charges as a consequence of decreased revenues, and a reduction in interest rate for certain debt.

Income Taxes

The Company has not incurred a tax expense during the current quarter (March 31, 2009: $Nil).

Income

Loss for the quarter ended March 31, 2010 was $2,330,000 compared to $3,172,000 for the quarter ended March 31, 2009. A $42,000 foreign exchange gain was offset by the adverse impact of significantly reduced revenues and resultant gross margin deterioration, specifically a $1,333,000 charge against income for idle capacity; and charges amounting to $417,000 for expected warranty expenditures.

Liquidity and Capital Resources

The Company ended the current quarter with bank operating line utilization of $7,428,000 compared to $8,422,000 as at December 31, 2009. Unless secured by cash, the Company's operating lines of credit provide for a total utilization of $15,000,000. On closing of the October 7, 2009 rights offering the operating line of credit guarantee provided by the former Chairman of the Board and shareholder was reduced by $1,000,000 thereby having the effect of reducing the Company's operating line of credit to $14,000,000 subject to asset margining stipulations.

The Company forecasts its financing requirements for 2010 to exceed the current availability of the operating line of credit. Accordingly, the Company has completed a private placement during the quarter, and subsequent to the end of the quarter closed a secured subordinated convertible loan in the amount of $1,771,000. The Company expects to finance investment in the start-up of new military defence programs with milestone payments from customers. However, success of these activities cannot be assured.

Cash Flows from Operating Activities

Cash utilized by operating activities, before consideration of changes in non-cash items relating to operating activities, was $1,016,000 for the quarter ended March 31, 2010 compared to a utilization of $681,000 for the same quarter last year. This current quarter cash utilization occurred as a result of operating losses.

Non-cash operating assets and liabilities provided $1,463,000 of cash during the current quarter, compared to providing $1,447,000 during the same quarter in 2009. The 2010 balance arose primarily as a result of a consumption of inventories and growth in trade payables offset by a growth in accounts receivable, arising from the re-start of certain program deliveries. 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 quarter, the Company purchased capital assets totalling $189,000 as compared to $193,000 during the quarter ended March 31, 2009. The Company continues to minimize its capital expenditures in order to conserve cash, with only operation critical expenditures being made.

Additionally, the Company invested $238,000 during the current quarter (March 31, 2009: $1,193,000) in tooling and in improving the production efficiencies of various program lines. A significant portion of the 2009 first quarter expenditure was specifically invested in new product introduction for the Cessna Citation CJ4 business jet program and the Boeing Defense, Space & Security CH47 helicopter program. The Company commenced delivering tail assemblies and components for these programs in the second quarter 2009. Current quarter expenditures relate to investment in start-up costs for the Joint Strike Fighter F-35 military jet aircraft program with BAE Systems for which product deliveries will commence in 2011.

Cash Flows from Financing Activities

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

During the quarter ended March 31, 2010, the Company's operating line of credit utilization decreased by $994,000 (March 31, 2009: $886,000 increased utilization).

For the quarter ended March 31, 2010, proceeds from funding of program non-recurring expenditures amounted to $369,000 (March 31, 2009: $149,000).

Also, during the current quarter, the Company repaid $368,000 of current and long-term debt consisting of $278,000 in equipment financing and $90,000 in royalty repayments.

On March 1, 2010, the Company completed a private placement of 17,773,211 common shares at $0.055 per share for gross proceeds of approximately $978,000. Subscribers in the private placement are Panta Holdings B.V., which has subscribed for 15,995,890 common shares, and Working Opportunity Fund (EVCC) Ltd., which has subscribed for 1,777,321 common shares. The common shares issued under the private placement are subject to a restriction on resale for a period of four months and one day from the date of issue, in accordance with applicable Canadian securities laws.

On March 31, 2010, the ratio of the Company's current assets to current liabilities was 1.08:1 (December 31, 2009: 1.04:1), with the debt to equity ratio at 0.98:1 (December 31, 2009: 0.97:1).

Contractual Obligations

PAYMENTS DUE BY PERIOD

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

	Total	2010	2011 – 2013	2014 – 2015	Post 2015
Convertible debenture	$ 4,391	$ 4,391[3]	$ -	$ -	$ -
Capital lease obligation	2,395	629	1,766	-	-
Purchase obligation[1]	22,728	1,769	8,056	5,455	7,448
Other long-term obligations[2]	835	-	825	10	-
Total contractual obligations	30,349	6,789	10,647	5,465	7,448

1 Purchase obligations include payments for the Company's operating and property leases.
2 This amount represents obligations the Company has with Industrial Technologies Office.
3 The Company will not be obligated to pay any interest or principal until the debenture matures on March 31, 2011.
As at March 31, 2010, the Company was not in compliance with a financial covenant associated with the convertible debenture. The Company has obtained a waiver from the debt holder for this non-compliance; it has not obtained a waiver for anticipated future breaches. In the absence of obtaining a waiver of such future breach, the lender would be entitled to demand immediate payment. Accordingly, the convertible debenture is classified as current debt.

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

Subsequent to the end of the quarter, the former Chairman of the Board sold 177,850 Series A Preferred Shares owned by himself, and on behalf of his wife and family trust to Working Opportunity Fund (EVCC) Ltd.

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, issueable in series, the terms of which will be determined by the Company's directors at the time of creation of each series. There were 195,505,323 common shares issued and 1,141,512 reserved for issuance at March 31, 2010 pursuant to a convertible debenture. The book value of common shares issued and outstanding as at March 31, 2010 was $75,574,000.

As at May 12, 2010, there were 195,505,323 common shares, 816,800 preference shares, 450,000 warrants and no options issued and outstanding.

Convergence with International Financial Reporting Standards

In 2006, Canada's Accounting Standards Board ratified a strategic plan that will result in Canadian generally accepted accounting principles (Canadian "GAAP"), as used by public companies, being evolved and converged with International Financial Reporting Standards ("IFRS") over a transitional period which will be complete by 2011. On February 13, 2008, the Canadian Accounting Standards Board confirmed that publicly accountable entities will be required to prepare financial statements in accordance with IFRS for interim and annual financial statements for fiscal years beginning on or after January 1, 2011 with appropriate comparative data from the prior year. Under IFRS, there is significantly more disclosure required, specifically for quarterly reporting. Further, while IFRS uses a conceptual framework similar to Canadian GAAP, there are significant differences in accounting policies that will need to be addressed by management. As of the date of this report, the International Accounting Standards Board has projects underway that should result in new pronouncements; accordingly the Company is assessing the impact of the ultimate adoption of IFRS on the Company's consolidated financial statements. Management has prepared a diagnostic identifying key areas where IFRS transition may have an impact. During the next phase of transition a technical analysis will be conducted in order to identify potential financial impacts thereby providing the platform upon which decisions on accounting policy choices will be made. Management has reviewed its business systems and determined that they are capable of processing and recording the transitional period reporting requirements. As well, key employees have been trained in the new reporting standards, and a plan for adoption of IFRS is being developed.

Operations Overview

Delivery and Quality Performance

Deliveries and quality performance as at March 31, 2010 were at planned levels for Bombardier and Boeing programs. Within the supply chain for Cessna programs the Company experienced quality issues giving rise to warranty expenditures, for which the Company is currently implementing corrective and preventive measures.

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 extend from January 2007 to December 2011, Boeing Defense, Space and Security to December 31, 2012, and BAE systems to December 21, 2011 with the latter two agreements pending final approval by the customer and Company. The Bombardier and Cessna agreements extend for the life of the programs.

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 March 31, 2010, was $272 million, ($54 million of which pertains to 2010), compared to $276 million as at December 31, 2009. The changes in order backlog are as follows:

- $17 million decrease in order backlog resulting from revenues recorded during the quarter ended March 31, 2010;
- $19 million increase in order backlog primarily due to production rate increases of various existing programs; and
- $6 million decrease in order backlog resulting from changes 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

Vendor quality performance generally met targeted levels during the year, with the exception of a limited number of vendors which the Company is managing on a day-to-day basis and in some cases with on-site personnel. During the current quarter the Company provisioned for $417,000 of expected warranty expenditures relating to a manufacturing deficiency arising within its supply chain. The Company will continue to work closely with our supply chain to ensure a stable, uninterrupted delivery of compliant products and will make 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.

Working Capital Utilization

Total current assets less total current liabilities was in a surplus position of $1,761,000 at March 31, 2010 and a surplus of $820,000 at December 31, 2009. The change in position during the first quarter 2010 was primarily due to cash generated from the consumption of inventories as well as the reduction of bank indebtedness via equity financings, and re-negotiated debt terms from current to long-term.

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 continue to be made, and that those investments along with the expected continued financial support of shareholders and lenders will 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 March 31, 2010 was 507 (December 31, 2009: 473). Employees have appropriate qualifications and experience to perform their duties and the Company provides ongoing training and opportunities for employee growth. The reductions in plant labour force over the course of the preceding year, have resulted in a higher cost of labour due to the remaining senior employees earning a higher rate of wages and benefits.

Equipment, Systems, Technologies and Processes

A select number of internal projects are reaching their completion, within which production is being re-started with productivity at targeted levels.

Technology upgrades in high-speed machining have occurred in the past two years. These investments were made to mitigate supply chain delivery risk, provide machining capacity for new programs, and bring currently out-sourced work in-house, thereby reducing costs and capturing margin currently in supplier prices.

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:

- increases in material costs, primarily aluminum plate, titanium 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; and
- the trend to greater use of composite material in primary structures in each new generation of aircraft.

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.

Procured Materials and Parts

Delivery delays on raw materials, in particular aluminum plate and machined components, have been partially mitigated by continued efforts with dual sourcing. In addition, continuing efforts are being undertaken to utilize customer relationships to reduce or minimize the increase in cost of bought-in materials and parts as well as ensure delivery commitments.

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 indicates that the aerostructures markets for commercial aircraft and business jets will be stable through 2010 following the dramatic reduction of the business jet volumes in 2009. This research also indicates some recovery is expected for 2011. The market for defence aircraft is expected to continue to grow through 2010 and into 2011.
- Market indications such as recovery of air travel rates and reduced airline capacity could increase rates on the Boeing 737 and Airbus A320 in 2011.
- The production of the Boeing 757 wing adapter plug for winglet retrofits is expected to continue at its reduced rate.
- Bombardier Challenger 850 and the Challenger 605 business jet aircraft production remain flat into 2010. The rates for Bombardier's regional aircraft are expected to be at lower levels for 2010, due to generally reduced global air travel.
- Cessna Citation Sovereign and CJ3 business jet rates have decreased significantly for 2009, and it is expected that these levels will be remain for 2010. The introduction of the CJ4 is progressing as planned showing continuous growth into 2010.
- Offset opportunities created by Canadian Government procurement within military aerospace programs exists 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's collective agreement with its labour force, which was to expire on September 30, 2009, was extended to March 31, 2010 with no changes in terms. Management is currently negotiating the successor agreement.

The Company continues to focus on cost reductions for direct labour, material and overhead. 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.

Composite Materials

The December 31, 2007 acquisition of Comtek adds ongoing operations expertise in the design and competitive manufacture 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.

Outlook

Current strength of the Canadian dollar relative to the US dollar has caused the Company's current order backlog to decline during 2010. 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 2010, followed by Cessna and Bombardier.

The Company forecasts its 2010 revenue levels to be slightly increased over 2009 primarily as a result of full rate production for programs introduced during 2009 and re-start of programs which were dormant during 2009. With the exception of capital expenditures required for new programs, the Company's investment in new equipment will be maintained at 2009 levels. The Company has commenced rehiring a portion of its workforce to meet increased 2010 and 2011 customer delivery requirements.

The Company forecasts its financing requirements for 2010 to exceed the current availability of the operating line of credit. Accordingly, the Company has completed private placements, a rights offering, and obtained additional debt financing. However, success of these activities cannot be assured.

Transactions with Related Parties

During the year ended December 31, 2005, the Company entered into an agreement under which the former Chairman of the Board and shareholder in consideration of mutual agreements with a Canadian chartered bank under which the former Chairman of the Board and shareholder guarantees the indebtedness of the Company to the Bank limited to $2,000,000. As at October 7, 2009, the guarantee was reduced to $1,000,000. In connection with providing the limited guarantee on the operating line of credit, the Company will pay a fee of 20% on the remaining $1,000,000 limited guarantee calculated on a daily basis. Fees paid to the former Chairman of the Board and shareholder during the quarter ended March 31, 2010 amounted to $49,000 (March 31, 2009: $149,000). Fees payable to the former Chairman of the Board and shareholder as at March 31, 2010 are $Nil (March 31, 2009: $Nil). These fees are included in the Statements of Operations as interest expense and financing charges and amount to $49,000 for the quarter ended March 31, 2010 (March 31, 2009: $50,000).

On February 3, 2006, a performance guarantee was provided by certain shareholders and former directors on production contracts with a certain customer. Fees ranging to $20,000 per month were provided as consideration for the performance guarantee. Fees paid to the former Chairman of the Board and shareholder during the quarter ended March 31, 2010 amounted to $Nil (March 31, 2009: $120,000). Fees payable to the former Chairman of the Board and shareholder as at March 31, 2010 are $Nil (March 31, 2009: $Nil). These fees are included in the Statements of Operations as cost of sales and amount to $Nil for the quarter ended March 31, 2010 (March 31, 2009: $Nil).

During the quarter ended March 31, 2010, no consulting services were provided by certain directors. Fees paid to certain directors, or Companies with which they have beneficial ownership, during the quarter ended March 31, 2010 amounted to $Nil (March 31, 2009: $Nil). Fees payable to certain directors or Companies with which they have beneficial ownership, as at March 31, 2010 are $10,000 (March 31, 2009: $Nil). These fees are included in the Statements of Operations as administrative and general expenses and amount to $Nil for the quarter ended March 31, 2010 (March 31, 2009: $Nil).Other related-party transactions are disclosed within the discussion of cash flows from financing activities.

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

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

The preparation of the financial statements in conformity with generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities, and the reported revenues and expenses.

The critical accounting estimates the Company has made relate to the following:

- 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 March 31, 2010 provision for anticipated losses was $1,185,000 (December 31, 2009: $1,080,000). The increase in this provision from December 31, 2009 was primarily due to the adverse impact the strengthening of the Canadian dollar relative to the US dollar has had on US dollar denominated sales.

- Unamortized development and tooling costs, net of related government assistance, which reflect the Company's investment in new programs and manufacturing process development, are recorded at $4,123,000 (March 31, 2009: $3,923,000). These costs are to be amortized over the number of units which management believes is a conservative estimate of deliveries for the programs to the customer. Development costs will be written off proportionately to any anticipated reduction in expected unit deliveries to the customer. Current reductions in deliveries have not impacted amortizations over the expected life of these aircraft programs. Furthermore, the Company will write off any amounts of development costs which it estimates will not be recoverable from the recurring programs to which they relate. At this time, management estimates that all development costs are recoverable.

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

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

- An estimation is made of the useful life of intangible assets. Useful life is measured as a range between one and ten years.

- During 2007, the Company became aware of a requirement to rework previously delivered product. As at the date of this report, it is uncertain as to when the rectification will take place. In consideration of the nature of rework required, and the possible extent to which the defect effects delivered product, the Company accrued a $1,454,000 discounted charge within cost of sales in 2007. In the opinion of the Company, an equivalent claim against the manufacturer of a sub-component to the product can be made and is estimated to be recoverable. Accordingly, a $1,454,000 recovery was accrued within cost of sales. During 2009, the Company revised its discounted warranty provision to $1,647,000 and discounted warranty recovery to $1,637,000. During the quarter ended March 31, 2010, the Company provisioned an additional $417,000 of expected warranty expenditures relating to a manufacturing deficiency arising within its supply chain. The amounts recorded are based on management's best estimate of the amount of product affected and the timing of the rework, which is expected to occur over the next two to three year period.

Measurement Uncertainty:

The preparation of the accompanying financial statements required management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenue and expenses during the reporting periods. By their nature these estimates are subject to measurement uncertainty. The effect on the financial statements of changes in such estimates in future periods could be material and would be accounted for in the period the change occurs.

- Carrying value of long-lived assets - The Company holds property, plant and equipment, and intangible assets on the balance sheet amounting to $18,402,000 (December 31, 2009: $19,164,000). The recoverability of the carrying value of these assets is, in part, dependant on the estimates used in determining the expected period of future benefits over which to amortize. In addition, such recoverability is 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. If operations perform below anticipated recoverable levels, the portion of deferred tooling costs that cannot be recovered is expensed immediately when known. At March 31, 2010, $4,123,000 (December 31, 2009: $3,923,000) in unamortized deferred tooling costs, which are expected to be recoverable from the related future cash flows of such new operations, are presented as Development Costs in the balance sheet.

- In accordance with Canadian GAAP the carrying value of long-lived assets is tested for impairment. Circumstances such as the decline in the Company's share price, the significant reduction in customer orders, and the financial condition of the Company may exist and indicate that the carrying amount of long-lived assets may not be recoverable. The aforementioned circumstances existed for the Company as at March 31, 2010 indicating that an assessment for impairment was required. An impairment assessment was made which considered the undiscounted cash flows from forecasted customer orders. The result of the impairment assessment indicated that long-lived assets were recoverable from forecasted future cash flows.

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 3%. The maximum operating line of credit availability is $15,000,000. The Company lowers interest rate costs by managing utilization of the operating lines of credit to the lowest amount practical. For the quarter ended March 31, 2010, with other variables unchanged, a 1% change in the bank prime interest rate would have a $18,000 impact on net earnings or cash.

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 gain recorded in the first quarter 2010 was $42,000 (March 31, 2009: $1,044,000 loss).

As at the balance sheet date, the Company had the following US dollar denominated balances:

Accounts receivable	$ 3,584,000
Bank cash position	1,962,000
Accounts payable	1,507,000
Long-term debt	1,727,000

With other variables unchanged, each $0.10 strengthening (weakening) of the US dollar against the Canadian dollar would result in a (decrease) increase of approximately $231,000 in net earnings for the quarter ended March 31, 2010 as a result of holding a net asset US dollar 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) and Cessna Aircraft Company (Cessna). The maximum exposure to credit risk is represented by the amount of accounts receivable in the balance sheet.

As at the balance sheet date 76% (March 31, 2009: 60%) 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 March 31, 2010 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 quarter ended March 31, 2010, 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 Canadian generally accepted accounting principles (GAAP) 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 GAAP. 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 Chief Executive Officer

report of auditors

To the Shareholders of Avcorp Industries Inc.

Under National Instrument 51-102, Part 4, subsection 4.3(3)(a), if an auditor has not performed a review of the interim financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

The accompanying unaudited interim financial statements of the Company have been prepared by and are the responsibility of the Company's management.

The Company's independent auditor has not performed a review of these financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

Consolidated Balance Sheets

as at March 31, 2010 and December 31, 2009 (unaudited, in thousands of Canadian dollars)

	March 31, 2010	December 31, 2009
Assets		
Current assets		
Accounts receivable	$ 8,396	$ 6,689
Inventories (note 6)	14,306	15,497
Prepayments	1,126	1,092
Other assets (note 5e)	23	24
	23,851	23,302
Development costs (note 7)	4,123	3,923
Property, plant and equipment (note 8)	16,668	17,346
Warranty claim receivable (note 16)	1,637	1,637
Intangible assets (note 9)	1,734	1,818
	48,013	48,026
Liabilities		
Current liabilities		
Bank indebtedness (note 10)	7,428	8,422
Accounts payable and accrued liabilities	9,421	7,929
Current portion of long-term debt (note 11)	5,241	6,131
	22,090	22,482
Deferred gain	394	405
Lease inducement	838	863
Deferred tooling revenues	4,088	3,116
Long-term debt (note 11)	2,380	1,811
Warranty provision (note 16)	2,064	1,647
Future income tax liability	858	858
	32,712	31,182
Shareholders' Equity		
Capital stock (note 12)	72,927	71,954
Preferred shares	7,622	7,622
Contributed surplus	2,647	2,647
Deficit	(67,895)	(65,379)
	15,301	16,844
	48,013	48,026

Nature of operations and going concern (note 1)
Measurement uncertainty (note 3)
Subsequent events (note 19)

Approved by the Board of Directors

David Levi
Chairman

Eric Kohn
Committee Chair,
Audit & Corporate Governance Committee

Consolidated Statements of Operations and Comprehensive Loss

For the quarter ended March 31, 2010 and 2009
(unaudited, in thousands of Canadian dollars, except number of shares and per share amounts)

For the quarter ended March 31	2010	2009
Revenues	$ 17,376	$ 22,087
Cost of sales and expenses		
Cost of sales	15,808	18,947
Administrative and general expenses	2,732	3,019
Amortization and depreciation	951	1,066
Foreign exchange (gain) loss (note 5a)	(42)	1,044
	19,449	24,076
Loss from operations	(2,073)	(1,989)
Interest expense and financing charges (note 14)	(257)	(529)
Unrealized derivative loss (note 5e)	-	(654)
Loss and comprehensive loss for the period	(2,330)	(3,172)
Basic and diluted loss per common share	(0.01)	(0.10)
Basic and diluted weighted average number of shares outstanding (000's)	183,854	32,315

Consolidated Statements of Deficit

For the quarter ended March 31, 2010 and 2009
(unaudited, in thousands of Canadian dollars)

For the quarter ended March 31	2010	2009
Deficit – Beginning of period	$ (65,379)	$ (56,213)
Loss for the period	(2,330)	(3,172)
Preferred share dividends	(186)	(186)
Deficit – End of period	(67,895)	(59,571)

Consolidated Statements of Cash Flows
For the quarter ended March 31, 2010 and 2009
(unaudited, in thousands of Canadian dollars)

For the quarter ended March 31	2010	2009
Cash flows from operating activities		
Loss for the period	$ (2,330)	$ (3,172)
Items not affecting cash (note 15a)	1,314	2,491
	(1,016)	(681)
Change in non-cash items related to operating activities (note 15b)	1,463	1,447
	447	766
Cash flows from investing activities		
Purchase of property, plant and equipment	(189)	(193)
Payments relating to development costs and tooling	(238)	(1,193)
	(427)	(1,386)
Cash flows from financing activities		
(Decrease) increase in bank indebtedness	(994)	886
Proceeds from customer funding of program non-recurring expenditures	369	149
Repayment of current and long-term debt	(368)	(415)
Issue of common shares	977	-
Share issue expense	(4)	-
	(20)	620
Net change in cash and cash equivalents	-	-
Cash and cash equivalents - Beginning of period	-	-
Cash and cash equivalents - End of period	-	-
Interest paid	193	440

1 Nature of operations and going concern

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.

For the quarter ended March 31, 2010, the Company recorded a net loss of $2,330,000 on $17,376,000 revenue, as compared to a $3,172,000 net loss from $22,087,000 revenue for the quarter ended March 31, 2009. The Company has a working capital surplus of $1,761,000 as at March 31, 2010 (December 31, 2009: $820,000 surplus) and an accumulated deficit of $67,895,000 at March 31, 2010 (December 31, 2009: $65,379,000).

As at March 31, 2010, the Company was not in compliance with a financial covenant associated with its operating lines of credit. In addition, the Company is forecasting that it will be in default of one or more of its covenants in the next 12 months. In the absence of obtaining a waiver of such breach, the lender is entitled to demand immediate payment. The lender had agreed to forbear from demanding payment of the indebtedness and from taking steps to enforce the security, subject to the Company complying with terms and conditions of a Forbearance Agreement which ends on June 9, 2010 (note 10).

Also, as at March 31, 2010, the Company was not in compliance with a financial covenant associated with the convertible debenture held by Export Development Canada (note 11a). The Company has obtained a waiver from the debenture holder for this non-compliance; it has not obtained a waiver for anticipated future breaches. In the absence of obtaining a waiver of such future breaches, the lender would be entitled to demand payment. Accordingly, the convertible debenture is classified as current debt. The Company is required to maintain certain measures of working capital, debt to tangible net worth, and debt service coverage.

During June 2009, the Company's Board of Directors resolved to defer Preferred Share dividends until January 2011. The Company has not paid $942,000 of preferred share dividends which were accrued and payable as at March 31, 2010.

These consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles (GAAP) applicable to a going concern, which contemplates the realization of assets and liquidation of liabilities during the normal course of operations. The conditions and risks noted above cast significant doubt on the validity of that assumption. The Company forecasts its financing requirements in the next 12 months to exceed the current availability of the operating line of credit. Accordingly, the Company has completed a private placement and rights offering, and will continue its efforts to obtain additional debt financing, renegotiate debt repayments, issue additional common shares, reduce operating expenses and maintain existing terms regarding customer collections in order to provide liquidity in excess of forecasted requirements. However, the success of these activities cannot be assured.

These consolidated financial statements do not reflect adjustments to the carrying value of assets and liabilities, the reported revenues and expenses, and balance sheet classifications used that would be necessary if the going concern assumption were not appropriate; such adjustments could be material.

2 Significant Accounting Policies

These unaudited interim consolidated financial statements are prepared in accordance with accounting principles generally accepted in Canada (Canadian GAAP).

Certain information and note disclosures normally included in the annual consolidated financial statements prepared in accordance with Canadian GAAP have been condensed or excluded.

As a result, these unaudited interim consolidated financial statements do not contain all disclosures required to be included in the annual consolidated financial statements and should be read in conjunction with the most recent audited annual consolidated financial statements and notes thereto for the year ended December 31, 2009.

These unaudited interim consolidated financial statements are prepared following accounting policies consistent with the Company's audited annual consolidated financial statements and notes thereto for the year ended December 31, 2009.

3 Measurement Uncertainty

The preparation of these financial statements required management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenue and expenses during the reporting periods. By their nature these estimates are subject to measurement uncertainty. The effect on the financial statements of changes in such estimates in future periods could be material and would be accounted for in the period the change occurs.

- Carrying value of long-lived assets

  The Company holds property, plant and equipment, (note 8) and intangible assets (note 9) on the balance sheet amounting to $18,402,000 (December 31, 2009: $19,164,000). The recoverability of the carrying value of these assets is, in part, dependant on the estimates used in determining the expected period of future benefits over which to amortize. In addition, such recoverability is 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. If operations perform below anticipated recoverable levels, the portion of deferred tooling costs that cannot be recovered is expensed immediately when known. At March 31, 2010, $4,123,000 (December 31, 2009: $3,923,000) in unamortized deferred tooling costs (note 7), which are expected to be recoverable from the related future cash flows of such new operations, are presented as Development Costs in the balance sheet.

4 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 balance sheet.

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 12, 17 and 19). The financial covenants by which the Company's debt agreements are bound are working capital, debt to tangible net worth, and debt service coverage ratios (notes 10 and 11a). Other matters relating to capital risk management are set out in note 1.

5 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 gain recorded in first quarter 2010 was $42,000 as compared to a $1,044,000 loss for the quarter-ended March 31, 2009.

As at the balance sheet date, the Company had the following US dollar denominated balances:

Accounts receivable	$ 3,584,000
Bank cash position	1,962,000
Accounts payable	1,507,000
Long-term debt	1,727,000

With other variables unchanged, each $0.10 strengthening (weakening) of the US dollar against the Canadian dollar would result in a (decrease) increase of approximately $231,000 in net earnings for the quarter ended March 31, 2010 as a result of holding a net asset US dollar position.

Foreign Exchange Forward Contracts

During 2008, the Company entered into USD25,000,000 of foreign-exchange-forward contracts which were executed during 2009, with the provider of its operating lines of credit. No such instruments were in place as at March 31, 2010. Accordingly, the Company has not recorded a derivative gain or loss during the quarter-ended March 31, 2010 (March 31, 2009: $656,000 unrealized derivative loss).

b) 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) and Cessna Aircraft Company (Cessna). The maximum exposure to credit risk is represented by the amount of accounts receivable in the balance sheet.

As at the balance sheet date 76% (March 31, 2009: 60%) 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 as outlined in note 4 to the consolidated financial statements. Other matters related to liquidity risk are set out in note 1.

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

The Company's operating line of credit is due on demand. Long-term debt repayments are as outlined in note 11.

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 3% (note 10). The maximum operating line of credit availability is $15,000,000. The Company lowers interest rate costs by managing utilization of the operating lines of credit to the lowest amount practical. For the quarter ended March 31, 2010, with other variables unchanged, a 1% change in the bank prime interest rate would have a $18,000 (March 31, 2009: $38,000) impact on net earnings or cash.

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

e) Price Risk

The Company uses derivative financial instruments to reduce its 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 March 31, 2010, the Company has $7,202,000 (December 31, 2009: $4,442,000) of firmly committed orders that include price adjustment clauses of this nature. A $Nil gain or loss has been recorded in unrealized derivative gains for the quarter ended March 31, 2010 as compared to a $2,000 gain for the quarter ended March 31, 2009 as a result of the change in the fair value of the underlying embedded derivatives.

Purchase Contracts

A number of the Company's purchase contracts have a price adjustment clause where the final purchase price is determined by certain indices in a period prior to the date of purchase. As a result, the final purchase 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 purchase. As at March 31, 2010, the Company has $139,000 (December 31, 2009: $445,000) of firmly committed purchases that include price adjustment clauses of this nature. A $Nil gain or loss has been recorded in unrealized derivative income for the quarter ended March 31, 2010 as compared to a $Nil gain or loss for the quarter ended March 31, 2009 as a result of the change in the fair value of the underlying embedded derivatives.

Other Assets and Liabilities

Other assets are comprised of $23,000 inflation derivatives assets arising from the Company's sales and purchase contracts having price adjustment clauses within their terms (December 31, 2009: $24,000).

f) Fair values

The fair values of the Company's accounts receivable are estimated to approximate their carrying values due to the immediate or short-term maturity of these financial instruments. The fair value of the Company's bank indebtedness, accounts payable and accrued liabilities and current portion of long-term debt are significantly lower than carrying value due to the Company's current financial condition. The fair value of the long-term debt cannot be reliably estimated due to the current financial condition of the Company.

6 Inventories

	March 31, 2010	December 31, 2009
Raw materials	$ 5,238	$ 6,419
Work in progress	8,583	8,646
Finished products	485	432
	14,306	15,497

The amount of inventory expensed in cost of sales during the quarter-ended March 31, 2010 amounted to $14,437,000. The carrying value of inventory pledged as security as at March 31, 2010 is $14,306,000.

7 Development Costs

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

	March 31, 2010	December 31, 2009
Opening balance	$ 3,923	$ 3,299
Additions	238	712
Amortization	(38)	(88)
	4,123	3,923

8 Property, Plant and Equipment

	March 31, 2010			December 31, 2009		
	Cost	Accumulated depreciation	Net	Cost	Accumulated depreciation	Net
Computer hardware and software	$ 7,697	$ 5,848	$ 1,849	$ 7,608	$ 5,655	$ 1,953
Machinery and equipment	35,802	21,483	14,319	35,704	20,832	14,872
Leasehold improvements	987	487	500	985	464	521
	44,486	27,818	16,668	44,297	26,951	17,346

9 Intangible Assets

	Remaining Estimated Useful Lives (years)	March 31, 2010			December 31, 2009		
		Cost	Accumulated Amortization	Net	Cost	Accumulated amortization	Net
Customer relationships	5	$ 1,320	$ 425	$ 895	$ 1,320	$ 378	$ 942
Trade name	3	300	135	165	300	120	180
Patents	8	870	196	674	870	174	696
		2,490	756	1,734	2,490	672	1,818

The Company amortizes intangible assets on a straight-line basis over their estimated useful lives, which range between one and ten years.

10 Bank Indebtedness

The Company has operating lines of credit with a Canadian chartered bank totalling $15,000,000 (December 31, 2009: $15,000,000). The facilities are due on demand.

As a condition of obtaining these operating lines of credit, security has been provided in the form of:

- general security agreement creating a first priority security interest in all present and after-acquired personal property of the Company and a floating charge over all of the Company's present and after-acquired real property;
- assignment/endorsements by the Company to the Bank of all risk insurance on all of the Company's real and personal property with the Bank as first loss payee;
- the credit available to the Company under its operating lines of credit shall be equal to the amount determined by the margin formula currently in place less $1,000,000 until such time as an equivalent amount is guaranteed by a party acceptable to the bank (note 17a);
- interest at Bank prime plus 3.0%; and
- the Company shall pay the Bank a monthly forbearance fee of $10,000;

The Company is required to maintain certain measures of working capital, debt to tangible net worth, and debt service coverage. As at March 31, 2010, the Company was not in compliance with a financial covenant. In addition, the Company is forecasting that it will be in default of one or more of its covenants in the next 12 months. In the absence of obtaining a waiver of such breach, the lender is entitled to demand immediate payment.

On March 11, 2010, the Company entered into a Forbearance Agreement with the bank providing its operating lines of credit. The Forbearance Agreement ends on June 9, 2010. The Company is subject to a quarterly review within which the Bank determines if there has occurred an event of default. Provided no default has occurred, the Forbearance Agreement is extended for a recurring period of 90 days.

11 Long-Term Debt

	March 31, 2010	December 31, 2009
Convertible debenture (a)	$ 4,391	$ 4,338
Capital leases (b)	2,395	2,689
Accrued government royalties (c)	835	915
	7,621	7,942
Less: Current portion	(5,241)	(6,131)
	2,380	1,811

a) Export Development Canada Convertible Debenture

During 2009, certain terms of the convertible debenture were changed. $241,000 of accrued interest was capitalized resulting in a principal balance of $4,338,000 outstanding as at December 31, 2009.

The principal outstanding debenture amount of $4,338,000 is convertible at the option of the holder (Export Development Canada) into 1,141,512 shares at a conversion price of $3.80. 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.

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

Provided no default has occurred, the Company will not be obligated to pay any interest or principal until the debenture matures on March 31, 2011.

The Company is required to maintain certain measures of working capital, debt to tangible net worth, and debt service coverage.

As at March 31, 2010, the Company was not in compliance with a financial covenant associated with the convertible debenture. The Company has obtained a waiver from the debt holder for this non-compliance; it has not obtained a waiver for anticipated future breaches. In the absence of obtaining a waiver of such future breach, the lender would be entitled to demand immediate payment. Accordingly, the convertible debenture is classified as current debt.

b) Capital Leases

There are various equipment leases that have a weighted average interest rate of 7.08% 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. $1,754,000 of the leases are held in US dollars.

c) Accrued Government Royalties

Royalties of $835,000 (December 31, 2009: $915,000) are payable to Industrial Technologies Office. On February 5, 2010, the Company signed an amended agreement with Industrial Technologies Office deferring royalty repayments to April 30, 2012.

12 Capital Stock

a) On March 1, 2010, the Company completed a private placement of 17,773,211 common shares at $0.055 per share for gross proceeds of approximately $978,000. Subscribers in the private placement are Panta Holdings B.V., which has subscribed for 15,995,890 common shares, and Working Opportunity Fund (EVCC) Ltd., which has subscribed for 1,777,321 common shares. The common shares issued under the private placement are subject to a restriction on resale for a period of four months and one day from the date of issue, in accordance with applicable Canadian securities laws

b) During 2009, the Company issued 145,417,183 common shares from the following transactions:

On July 21, 2009, the Company issued 16,157,465 common shares to Panta Holdings B.V. at $0.15 per share providing gross proceeds of $2,423,000. The Company received aggregate net proceeds of $858,000 after set off against certain bridge loan obligations owed to Panta Holdings B.V.

On October 7, 2009, the Company completed a rights offering within which 129,259,718 common shares were issued at $0.06 per share providing gross proceeds of $7,755,000. The Company received aggregate net proceeds of $4,386,000 after set off against certain bridge loan obligations owed to Panta Holdings B.V.

The costs of issuing capital stock during 2009 amounted to $493,000 and were deducted from total proceeds of $10,178,000 to record $9,685,000 as capital stock.

13 Defined Contribution Plan

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

For the quarter ended March 31	2010	2009
Defined contribution plan	$ 285	$ 334

The Company's contribution to the plan is calculated on a percentage of employee wages. The range of percentages is 1.5% to 8.5%. The plan is available to all employees.

14 Interest Expense and Financing Charges

For the quarter ended March 31	2010	2009
Interest on capital leases	$ 46	$ 68
Interest on other long-term debt	11	-
Interest on short-term debt	151	404
Interest on related party debt	49	57
Net interest expense	257	529

15 Supplementary Cash Flow Information

a) Items not affecting cash:

For the quarter ended March 31	2010	2009
Accrued interest and government royalties	$ 109	$ 254
Amortization and depreciation	951	1,066
Deferred tooling revenue amortization	(198)	(112)
Development cost amortization	38	27
Prepaid rent amortization	-	374
Provision for loss-making contracts	105	23
Provision for obsolete inventory	(15)	130
Unrealized derivative gains	1	661
Warranty provisions	417	-
Other items	(94)	68
	1,314	2,491

b) Changes in non-cash items:

For the quarter ended March 31	2010	2009
Accounts receivable	$ (906)	$ 3,711
Inventories	1,101	(2,982)
Prepayments	(34)	7
Accounts payable and accrued liabilities	1,302	711
	1,463	1,447

c) Non-cash financing and investing activities:

For the quarter ended March 31	2010	2009
Uncollected deferred tooling revenue	$ 801	$ -

16 Contingencies

During 2007, the Company became aware of a requirement to rework previously delivered product. As at the date of this report, it is uncertain as to when the rectification will take place. In consideration of the nature of rework required, and the possible extent to which the defect effects delivered product, the Company accrued a $1,454,000 discounted charge within cost of sales in 2007. In the opinion of the Company, an equivalent claim against the manufacturer of a sub-component to the product can be made. Accordingly, a $1,454,000 recovery was accrued within cost of sales. During 2009, the Company revised its discounted warranty provision to $1,647,000 and discounted warranty recovery to $1,637,000. During the current quarter 2010 the Company provisioned for $417,000 of expected warranty expenditures relating to a manufacturing deficiency arising within its supply chain, this provision is in addition to the $1,647,000 balance of warranty expenditures provided for to December 31, 2009. The amounts recorded are based on management's best estimate of the amount of product affected and the timing of the rework, which is expected to occur during the next two to three year period.

17 Related Party Transactions

a) During the year ended December 31, 2005, the Company entered into an agreement under which the former Chairman of the Board and shareholder in consideration of mutual agreements with a Canadian chartered bank under which the former Chairman of the Board and shareholder guarantees the indebtedness of the Company to the Bank limited to $2,000,000. As at October 7, 2009, the guarantee was reduced to $1,000,000. In connection with providing the limited guarantee on the operating line of credit, the Company will pay a fee of 20% on the remaining $1,000,000 limited guarantee calculated on a daily basis. Fees paid to the former Chairman of the Board and shareholder during the quarter ended March 31, 2010 amounted to $49,000 (March 31, 2009: $149,000). Fees payable to the former Chairman of the Board and shareholder as at March 31, 2010 are $Nil (March 31, 2009: $Nil). These fees are included in the Statements of Operations as interest expense and financing charges and amount to $49,000 for the quarter ended March 31, 2010 (March 31, 2009: $50,000).

b) On February 3, 2006, a performance guarantee was provided by certain shareholders and former directors on production contracts with a certain customer. Fees ranging to $20,000 per month were provided as consideration for the performance guarantee. Fees paid to the former Chairman of the Board and shareholder during the quarter ended March 31, 2010 amounted to $Nil (March 31, 2009: $120,000). Fees payable to the former Chairman of the Board and shareholder as at March 31, 2010 are $Nil (March 31, 2009: $Nil). These fees are included in the Statements of Operations as cost of sales and amount to $Nil for the quarter ended March 31, 2010 (March 31, 2009: $Nil).

c) During the quarter ended March 31, 2010, no consulting services were provided by certain directors. Fees paid to certain directors, or Companies with which they have beneficial ownership, during the quarter ended March 31, 2010 amounted to $Nil (March 31, 2009: $Nil). Fees payable to certain directors or Companies with which they have beneficial ownership, as at March 31, 2010 are $10,000 (March 31, 2009: $Nil). These fees are included in the Statements of Operations as administrative and general expenses and amount to $Nil for the quarter ended March 31, 2010 (March 31, 2009: $Nil).

18 Economic Dependence and Segmented Information

a) Sales to three major customers for the quarter ended March 31, 2010, which comprise several programs and contracts, accounted for approximately 88.7% (March 31, 2009: 83.5%) of sales.

	2010		2009	
	Revenue	% of Total	Revenue	% of Total
Boeing	$ 6,556	37.7	$ 4,221	19.1
Bombardier	5,041	29.0	5,677	25.7
Cessna	3,818	22.0	8,538	38.7
Other	1,961	11.3	3,651	16.5
Total	17,376	100.0	22,087	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.

19 Subsequent Events

On April 16, 2010, the Company completed a secured subordinated convertible loan with a principal amount of $1,771,000 which, subject to shareholder approval, is convertible into a maximum of 29,516,666 common shares.

The secured subordinated convertible loan has been provided by Panta Holdings B.V. through a wholly-owned subsidiary. The loan, which is evidenced by a promissory note, has a five year term with an interest rate of 6% per year. The $1,771,000 principal amount is convertible into common shares at a conversion price of $0.06 per common share in the first two years of the loan, $0.07 per common share in the third and fourth years of the loan, and $0.08 per common share in the fifth year of the loan. Accumulated interest will not be convertible.

As per the requirements of the Toronto Stock Exchange, exercise of the conversion right of the loan is subject to disinterested shareholder approval, which approval is being sought at the 2010 annual meeting of shareholders to be held on May 18, 2010. If the conversion right is not approved at the meeting, the interest rate on the loan will change from 6% per year to 12% per year, and the loan will become payable on demand.

notes

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

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

Jaap Rosen Jacobson (2)
DIRECTOR
Mijdrecht, The Netherlands

Kees de Koning (3)
DIRECTOR
Nootdorp, The Netherlands

Elizabeth Otis (3*)
DIRECTOR
Vashon, Washington, USA

Mark van Rooij (3)
DIRECTOR
Chief Executive Officer
White Rock, British Columbia

Paul Kalil
President
Vancouver, British Columbia

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

(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

DIRECTORY

Bank

HSBC Bank Canada
Vancouver, British Columbia

Legal Counsel

Lang Michener LLP
Barristers & Solicitors
Vancouver, British Columbia

Registrar and Transfer Agent

CIBC Mellon Trust Company
Vancouver, British Columbia

Auditors

PricewaterhouseCoopers LLP
Chartered Accountants
Vancouver, British Columbia

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