Second Quarter Report
2016

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ABOUT AVCORP INDUSTRIES INC. The Avcorp Group designs and builds major airframe structures for some of the world's leading aircraft companies, including BAE Systems, Boeing, Bombardier, Fuji Heavy Industries and Lockheed Martin. The Avcorp Group has more than 50 years of experience, over 750 skilled employees and 636,000 square feet of facilities. Avcorp Structures & Integration located in Delta British Columbia, Canada is dedicated to metallic and composite aerostructures assembly and integration; Avcorp Engineered Composites located in Burlington Ontario, Canada is dedicated to design and manufacture of composite aerostructures, and Avcorp Composite Fabrication located in Gardena California, USA has advanced composite aerostructures fabrication capabilities for composite aerostructures. The Avcorp Group 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. Comtek Advanced Structures Ltd., at our Burlington, Ontario, Canada location also provides operators and MRO's aircraft structural component repair services for commercial aircraft.

Avcorp Composite Fabrication Inc. is wholly owned by Avcorp US Holdings Inc. Both companies are incorporated in The State of Delaware, USA, and are wholly owned subsidiaries of Avcorp Industries Inc.

Comtek Advanced Structures Ltd., incorporated in the Province of Ontario, Canada, is a wholly owned subsidiary of Avcorp Industries Inc.

Avcorp Industries Inc. is a federally incorporated reporting company in Canada and traded on the Toronto Stock Exchange (TSX:AVP).

management discussion & analysis

This Management Discussion and Analysis has been prepared as of June 30, 2016, and should be read in conjunction with the Company's consolidated financial statements and notes thereto for the year ended December 31, 2015.

Description of Business

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

We currently operate from two locations in Canada and one location in the United States. Located in Delta, British Columbia, Avcorp Industries Inc., named as Avcorp Structures & Integration ("ASI"), is dedicated to metallic and composite aerostructures assembly and integration. Within Comtek Advanced Structures Ltd., located in Burlington, Ontario, exists two divisions, one ("Comtek") dedicated to aircraft structural component repair services, and the second Avcorp Engineered Composites ("AEC") dedicated to design and manufacture of composite aerostructures. Located in Gardena, California, Avcorp Composite Fabrication Inc. ("ACF") is dedicated to advanced composite aerostructures fabrication.

Avcorp Industries Inc. is a federally incorporated reporting company in Canada and traded on the Toronto Stock Exchange (TSX:AVP).

Avcorp Composite Fabrication Inc. is wholly owned by Avcorp US Holdings Inc. Both companies are incorporated in The State of Delaware and are subsidiaries of Avcorp Industries Inc.

Comtek Advanced Structures Ltd., incorporated in the Province of Ontario is a wholly owned subsidiary of Avcorp Industries Inc.

Avcorp is in compliance with industry standard quality certifications.

Financial Overview

Quarterly Results

The following table provides selected unaudited quarterly condensed interim consolidated financial information for the eight most recent fiscal quarters to June 30, 2016 prepared in accordance with IAS 34 – Interim Financial Reporting ("IAS 34") as issued by the International Accounting Standards Board ("IASB").

QUARTERLY RESULTS

(unaudited, prepared in accordance with IAS 34, expressed in thousands of Canadian dollars except per share amounts)

	2016		2015				2014	
FOR THE THREE MONTHS ENDED	**Jun 30**	Mar 31	Dec 31	Sept 30	Jun 30	Mar 31	Dec 31	Sep 30
Revenue	**$44,246**	$35,347	$22,285	$21,610	$20,369	$15,661	$13,744	$14,675
Operating income (loss)	**(12,781)**	(12,399)	(6,287)	(2,030)	(1,125)	(2,672)	(3,848)	(2,321)
EBITDA[1]	**(10,913)**[2]	(9,976)[2]	10,796	(556)	(623)	(2,348)	(3,442)	(1,794)
Net income (loss)	**(12,951)**[2]	(12,091)[2]	9,157	(2,053)	(1,135)	(2,761)	(3,890)	(2,229)
EBITDA per share[1]								
Basic	**(0.04)**	(0.03)	0.04	(0.00)	(0.00)	(0.01)	(0.01)	(0.01)
Diluted	**(0.04)**	(0.03)	0.04	(0.00)	(0.00)	(0.01)	(0.01)	(0.01)
Net income (loss) per share								
Basic	**(0.04)**	(0.04)	0.03	(0.01)	(0.00)	(0.01)	(0.01)	(0.01)
Diluted	**(0.04)**	(0.04)	0.03	(0.01)	(0.00)	(0.01)	(0.01)	(0.01)
Long-term debt	**1,650**	1,649	1,646	1,634	1,542	1,434	943	152

1. EBITDA = earnings before interest, taxes, depreciation and amortization. This is not a recognized term under International Financial Reporting Standards ("IFRS").
2. It should be noted that in 2016, the loss and EBITDA incorporated substantial costs incurred which have yet to be recovered from the seller of Hitco.

Three and Six Months Ended June 30, 2016 and 2015 Overview

During the quarter ended June 30, 2016 Avcorp Group revenues totaled $44,246,000 as compared to $20,369,000 revenue for the same quarter in the previous year. The December 18, 2015 acquisition of the US based composite Aerostructures division of Hitco, a subsidiary of Frankfurt-listed SGL has added $22,595,000 to current quarter revenues.

The Company operates within "general terms agreements" with its customers. These agreements are typically for five years or longer. The contracts provide for long lead-time orders; the civil aerospace business is also slightly seasonal as some aircraft manufacturers reduce or suspend production in December and for a period of time during the summer months.

Effective December 18, 2015, Avcorp completed the acquisition of the US-based composite Aerostructures division of Hitco, a subsidiary of Frankfurt-listed SGL. The Acquisition was completed pursuant to the terms of an asset purchase agreement that was entered into on July 20, 2015, and subsequent amendments to December 18, 2015. Pursuant to the Agreement Avcorp's subsidiary, Avcorp Composite Fabrication Inc., purchased the assets of the division of Hitco which produces composite structural parts for commercial and military aerostructures. Avcorp was indemnified, under its asset purchase agreement and ancillary agreements by SGL for all product liabilities prior to closing, and entered into a service agreement to assist in rectifying and resolving these liabilities subject to remuneration by Hitco and or SGL.

The Aerostructures division of Hitco was a large carbon composites aerostructures manufacturer which produced and supplied composite aerostructures assemblies to aerospace markets. Its products comprise complex mold line structures such as beams, stringers, wing skins, tailcones, pressurized bulkheads and control surfaces. The products are sold within the commercial and defence aerospace industries.

The acquisition of Hitco's Aerostructures composite division offers a unique opportunity to transform the Avcorp Group's existing metal fabrication and integrated assembly business by broadening the product range and strengthening Avcorp's composite capabilities. Advanced composite fabrication capabilities, provided by this acquisition, has enhanced Avcorp Group's ability to participate in large aerospace assembly programs which combine mixed material components.

On a year-to-date basis, for the period ending June 30, 2016, the Avcorp Group revenues totalled $79,593,000 (year-to-date June 30, 2015: $36,030,000). The increase in revenues during 2016 relative to 2015 is primarily due to the Hitco acquisition.

June 30, 2016 year-to-date revenues arising from the assignment by customers of commercial aerospace contracts to Avcorp Industries Inc., in conjunction with the December 18, 2015 Hitco acquisition have generated $34,810,000 in revenue (June 30, 2015: $Nil). These contracts support customer production of commercial aircraft. Manufacturing of the composite parts occurs in Avcorp Group's newly acquired Gardena facility. The Gardena facility was assigned defence aerospace contracts by Hitco's customers upon the finalization of the acquisition. These contracts generated $6,835,000 of revenue during the first two quarters 2016 for ACF (June 30, 2015: $Nil).

The Burlington facility continued its production ramp-up of composite floor panels in supply to Bombardier Aerospace's Global 5000/6000 and Global 7000/8000 programs during the current quarter, with continued slightly higher rates of production expected for 2016. Full rate production for these programs establishes the wholly owned subsidiary as a leading manufacturer of composite floor panels. Composite floor panel revenues arising from aftermarket or spare component sales decreased by 5.2% during the first six months of 2016 relative to the same period in 2015; while composite floor panel revenues derived from sales to original equipment manufacturers ("OEM") have significantly increased by 23.9% during the same six month period. Comtek's long term relationships with aircraft operators has resulted in a significant 83.6% increase in revenues in 2016 relative to the same period in 2015, indicating that its growth in composite and metal aircraft structure repair revenues continues to provide a strong operating cash flow from this market segment. In summary, Avcorp's Burlington operations increased revenue in the first half 2016 relative to the first half 2015 by $3,485,000 (43.6%).

The Delta facility revenues generated by legacy production contracts have decreased by $1,559,000 during the first two quarters of 2016 relative to the same period in the previous year; program revenue mix has remained relatively consistent in 2016 relative to 2015 for production contracts manufactured out of the Delta facility.

Avcorp's Delta location continues to actively pursue production contracts on aerospace programs throughout North America, Asia, and Europe both in the commercial and defence aerospace sectors. These efforts have commenced producing value as noted in the recent contract awards, in addition to 2015 awards for the expanded scope of production on the Lockheed Martin F-35 Carrier Variant Outboard Wing, as well as production and supply of 767-2C Panoramic Camera Fairings, as part of The Boeing Company's KC-46 Tanker program. Further contract awards are expected.

On a year-to-date basis, for the period ending June 30, 2016, the Avcorp Group recorded losses from operations totaling $25,180,000 from $79,593,000 revenue, which include costs incurred and yet to be recovered under the Hitco acquisition agreement, as compared to $3,797,000 operating losses from $36,030,000 revenue during the same six month period in 2015.

During the quarter ended June 30, 2016, the Avcorp Group recorded a loss from operations of $12,781,000, which includes costs incurred and yet to be recovered under the Hitco acquisition agreement, on $44,246,000 revenue; as compared to a $1,125,000 operating loss on $20,369,000 revenue for the same quarter in the previous year; and net loss for the current quarter of $12,951,000 which include costs incurred yet to be recovered under the Hitco acquisition agreement as compared to net loss of $1,135,000 for the quarter ended June 30, 2015.

Pre-Hitco acquisition operational events although indemnified and on which Avcorp was required to assist, adversely impacted operations and caused excessive personnel costs, administrative and legal expenditures at ACF Avcorp's Gardena facility. These costs have yet to be recovered are included in all the costs for 2016.

The financial results presented for the quarter ended June 30, 2016 do not take into account any recovery provision for these operational expenditures for which the Company believes it is indemnified for under its asset purchase agreement, and ancillary agreements, with SGL. These expenditure recovery amounts are not finalized and cannot be quantified for their full extent at this time.

Operating losses due to production which were planned as part of the post-strategy and business plan, primarily arising from certain unfavourable customer contracts assumed with the December 18, 2015 Hitco acquisition as well as pre-existing operational inefficiencies have amounted to approximately $10,394,000 during the quarter ended June 30, 2016 (June 30, 2015: $Nil) and $19,963,000 for the six months ended June 30, 2016 (year-to-date June 30, 2015: $Nil). An unfavourable contract liability accrued on December 18, 2015, for these customer contracts for which unavoidable costs are expected to exceed the corresponding revenue earned during a period of manufacturing process rectification and improvements amounted to $90,654,000 upon acquisition; of which $78,614,000 remains unamortized as at June 30, 2016 (December 31, 2015: $89,971,000). The unfavourable contract liability is amortized into income on a units-of-production basis over the expected life of the contract. The unamortized unfavourable contracts provision will be reviewed in the final quarter 2016 to ensure that the provision does not exceed the estimated future losses. The amount of unfavourable contract liability amortized into income during the second quarter 2016 was $3,661,000 (June 30, 2015: $Nil). As at June 30, 2016, the remaining unamortized unfavourable contract liability amounted to $78,614,000. The unamortized unfavourable contract liability is accrued in US dollars and therefore the unamortized balance will vary from quarter to quarter as the estimated provision is adjusted for foreign currency fluctuations.

Although recent customer contract awards will continue to increase facility utilization, there remain within operations significant levels of unutilized plant capacity within the Company's Delta, British Columbia facility. The Company has expensed $935,000 of overhead costs during the current quarter (June 30, 2015: $1,204,000) in respect of unutilized plant capacity. The amount of overhead costs expensed, as a result of unutilized capacity, will fluctuate from quarter to quarter as production in support of deliveries varies. Revenue growth in this facility would benefit Company profitability via a contribution to the recovery of fixed overhead expenditures. Avcorp is engaged with aerospace original equipment manufacturers as well as industry tier 1 suppliers in North America, Asia and Europe in collaborative production initiatives which support the Company's recent transition to composite manufacturing capabilities, further leveraging existing production capacity and investments.

During the quarter ended June 30, 2016, cash flows from operating activities, excluding the impact of changes in non-cash working capital, utilized $12,762,000 of cash as compared to utilizing $523,000 of cash during the quarter ended June 30, 2015. Cash flows from operating activities were most significantly impacted as a result of operating losses incurred from the integration and productionization costs expended for the newly acquired Hitco operations, losses arising from unfavourable customer contracts assumed, and operational, administrative, and legal expenditures, incurred at Avcorp's Gardena facility as a direct result of pre-Hitco acquisition operational events.

Changes in non-cash working capital during the current quarter increased cash flows from operating activities by $7,664,000 (June 30, 2015: $2,057,000 decrease) primarily as accounts payable and accrued liabilities grew during the current quarter.

Also, pursuant to the Hitco acquisition, the Company assumed a customer advance for pre-funding of product deliveries. The customer advance is re-paid as the Company delivers to its customer, ordered products for a specific program. The customer advance is subject to an access and security agreement along with a general security agreement entered into with the Company's bank. The remaining unamortized customer advance has been discounted to arrive at the June 30, 2016 amount of $16,739,000 (December 31, 2015: $23,105,000) of which it is estimated $9,791,000 will be amortized during the next twelve months. The Company re-paid and amortized into income $2,473,000 of the customer advance during the quarter ended June 30, 2016 (June 30, 2015: $Nil).

As at June 30, 2016, the Company had $5,052,000 cash on hand (December 31, 2015: $14,484,000) and utilized $1,511,000 of its operating line of credit (December 31, 2015: $Nil). The Company has a working capital surplus of $30,351,000 as at June 30, 2016 which has decreased from the December 31, 2015 $55,045,000 surplus. The Company's accumulated deficit as at June 30, 2016 is $87,507,000 (December 31, 2015: $62,465,000).

ACF Gardena Start-up

The Gardena facility defence programs have been successful and are meeting delivery to customers as planned and have not experienced the extraordinary unanticipated issues relative to process quality and operational disruptions of the commercial programs. The planned improvement initiatives for the defence programs, including the F-35 program for Lockheed Martin, continue and are performing as forecasted; this has resulted in an award of a follow-on contract from Lockheed Martin that was previously announced.

The start-up, post-acquisition of the ACF new commercial operations in Gardena faced several unanticipated challenges during the first quarter which continued to have an adverse financial impact during the second quarter 2016. Operational losses incurred at the Gardena facility amounted to $10,394,000 for the quarter ended June 30, 2016 and $19,963,000 for the six month period ended June 30, 2016. Pre-Hitco acquisition operational events, although indemnified and on which Avcorp was required to assist, adversely impacted operations and caused excessive personnel costs, administrative and legal expenditures at ACF Avcorp's Gardena facility. These costs have yet to be recovered and included in all the costs for 2016.

As a result of legacy quality issues raised by customers on products delivered or completed prior to the acquisition, a substantial and large number of items were identified that required corrective action under the service agreement with Hitco and SGL. These items accounted for substantial expenditures, including extra contract personnel beyond normal production costs, and these extra costs have yet to be recovered. The implementation of the necessary corrective actions which limited production output during the first quarter and into the second quarter was the major contributor to lower than forecasted sales.

The majority of the corrective actions implemented in the second quarter of 2016 will allow the Gardena operations to achieve fully contracted output levels. Avcorp's key commercial customers have worked collaboratively with Avcorp to mitigate production schedules risks and support the earliest resolution of the outstanding process and product issues.

During the month of March, the Gardena ACF operations also experienced an extended power outage, over which ACF had no control, lasting most of a week, resulting in the partial suspension of manufacturing operations for the commercial programs under production in Gardena. This power outage accounted for lower than planned sales and the loss of some in-process material. The power outage and the unanticipated corrective actions have created a build-up of order backlog. Deferred first quarter revenues form part of subsequent quarter deliveries.

The complexity and challenge of executing the production start-up and improvement plans for the Gardena operations increased from pre-acquisition estimates. Avcorp continues to work successfully with the commercial aerospace customers to update plans and commitments to ensure support for their programs and a return to purchase order schedules as soon as possible and by no later than the end of third quarter of 2016.

Revenue

During the quarter ended June 30, 2016 Avcorp Group revenues totaled $44,246,000 as compared to $20,369,000 revenue for the same quarter in the previous year; a significant 117.2% revenue increase for the second quarter of 2016 as compared to 2015. Acquisition based revenues have added $22,595,000 to current quarter revenues.

The Company operates within "general terms agreements" with its customers. These agreements are typically for five years or longer. The contracts provide for long lead-time orders; the civil aerospace business is also slightly seasonal as some aircraft manufacturers reduce or suspend production in December and for a period of time during the summer months.

The Delta facility revenues generated by legacy production contracts have decreased by $239,000 during the current quarter relative to the same quarter in the previous year; program revenue mix has remained relatively consistent in 2016 relative to 2015 for production contracts manufactured out of the Delta facility.

Avcorp's Delta location continues to actively pursue production contracts on aerospace programs throughout North America, Asia, and Europe both in the commercial and defence aerospace sectors. These efforts have commenced producing value as noted in the recent contract awards, in addition to 2015 awards for the expanded scope of production on the Lockheed Martin F-35 Carrier Variant Outboard Wing, as well as production and supply of 767-2C Panoramic Camera Fairings, as part of The Boeing Company's KC-46 Tanker program. Further contract awards are expected.

The Burlington facility continued its production ramp-up of composite floor panels in supply to Bombardier Aerospace's Global 5000/6000 and Global 7000/8000 programs during the current quarter, with continued higher rates of production expected for 2016. Full rate production for these programs establishes the wholly owned subsidiary as a leading manufacturer of composite floor panels. Composite floor panel revenues arising from aftermarket or spare component sales decreased by 6.5% in second quarter 2016 relative to second quarter 2015; while composite floor panel revenues derived from sales to original equipment manufacturers ("OEM") have more than offset non-OEM sales reduction, with an increase of 9.5%. Comtek's long term relationships with aircraft operators has resulted in a 76.2% increase in revenues in 2016 relative to the same period in 2015, indicating that its growth in composite and metal aircraft structure repair revenues continues to provide a strong operating cash flow from this market segment. In summary, Avcorp's Burlington operations increased revenue in the second quarter 2016 relative to the second quarter 2015 by $1,521,000 (35.2%).

Effective December 18, 2015, Avcorp completed the acquisition of the US-based composite Aerostructures division of Hitco, a subsidiary of Frankfurt-listed SGL. The Acquisition was completed pursuant to the terms of an asset purchase agreement that was entered into on July 20, 2015, and subsequent amendments to December 18, 2015. Pursuant to the Agreement Avcorp's subsidiary, Avcorp Composite Fabrication Inc., purchased the assets of the division of Hitco which produces composite structural parts for commercial and military aerostructures.

The Aerostructures division of Hitco was a large carbon composites aerostructures manufacturer which produced and supplied composite aerostructures assemblies to aerospace markets. Its products comprise complex mold line structures such as beams, wing skins, tailcones, pressurized bulkheads and control surfaces. The products are sold within the commercial and defence aerospace industries.

The acquisition of Hitco's Aerostructures composite division offers a unique opportunity to transform the Avcorp Group's existing metal fabrication and integrated assembly business by broadening the product range and strengthening Avcorp's composite capabilities. Advanced composite fabrication capabilities, provided by this acquisition, will enhance Avcorp Group's ability to participate in large aerospace assembly programs which combine mixed material components.

Current quarter revenues arising from the assignment by customers of commercial aerospace contracts to Avcorp Industries Inc., in conjunction with the December 18, 2015 Hitco acquisition have generated $18,257,000 in revenue (June 30, 2015: $Nil). These contracts support customer production of commercial aircraft. Manufacturing of the composite parts occurs in Avcorp Group's newly acquired Gardena facility. The Gardena facility was assigned defence aerospace contracts by Hitco's customers upon the finalization of the acquisition. These contracts generated $4,338,000 of revenue during the second quarter 2016 for ACF (June 30, 2015: $Nil).

Deliveries and quality performance as at June 30, 2016 for Canadian manufacturing operations were at customer required levels. The manufacturing operations have achieved, and continue to maintain, top quality and delivery ratings for the majority of their programs.

Avcorp in the course of its due diligence of the assets and liabilities prior to closing the acquisition of ACF, the carve out of Hitco, discovered a number of issues. The seller and its ultimate parent SGL Carbon SE have the contractual responsibility and liability for all completed products before the closing with the exception of a limited amount of finished goods and manufacturing work in process for which Avcorp elected to assume the responsibility and verify the quality of these products. Immediately after the ACF acquisition, a thorough quality and delivery review and audit was conducted of the ACF Gardena manufacturing operations by ACF, which has produced improvement plans together with its customers. ACF continues to work collaboratively with customers to ensure any quality and delivery issues are resolved at the earliest date. These issues have adversely impacted the Gardena facility's production capacity, flows and efficiencies thereby causing the Group's deliveries to fall short of customers' demand.

Revenues from Avcorp Group customers are as follows.

REVENUE DISTRIBUTION

(unaudited, prepared in accordance with IAS 34, expressed in thousands of Canadian dollars)

	Three months ended June 30				Six months ended June 30			
	2016		2015		**2016**		2015	
	Revenue	**% of Total**	Revenue	% of Total	**Revenue**	**% of Total**	Revenue	% of Total
BAE Systems	**$4,998**	**11.3**	$4,609	22.6	**$4,998**	**6.3**	$6,902	19.2
Boeing	**20,631**	**46.6**	6,968	34.2	**40,478**	**50.9**	13,812	38.3
Bombardier	**4,207**	**9.5**	4,071	20.0	**8,701**	**10.9**	7,939	22.0
Fuji Heavy Industries	**3,200**	**7.2**	-	-	**6,527**	**8.2**	-	-
Lockheed Martin	**2,725**	**6.2**	-	-	**4,630**	**5.8**	-	-
Other	**8,485**	**19.2**	4,721	23.2	**14,259**	**17.9**	7,377	20.5
Total	**44,246**	**100.0**	20,369	100.0	**79,593**	**100.0**	36,030	100.0

The Avcorp Delta BC facility is the single source supplier for the F-35 Carrier Variant Outboard Wing ("CV-OBW") assembly under contract with BAE Systems ("BAES"), and delivers directly to Lockheed Martin. The Outboard Wing is the foldable portion of the wing on the carrier version of the F-35 aircraft which allows for 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 CV-OBW is regarded as one of the most complex assemblies that the Canadian aerospace industry contributes to the F-35 program. Production rates for the F-35 CV-OBW were reduced in 2016 relative to 2015. Production contracts have been secured through to May 2018, with discussions underway with the customer to secure constant production through 2019. The Company announced that further to the contract award from Lockheed Martin announced on October 15, 2015 for the expanded scope on the F-35 CV OBW, Avcorp has received a firm order for the remaining units in the next two production phases, referred to as Low Rate Initial Production ("LRIP") nine and LRIP ten. Avcorp's established New Product Introduction ("NPI") process will ensure the successful knowledge and skills transfer from Lockheed Martin, required for the intricate work of paint preparation and complex installation of control surfaces and systems such as the outboard leading edge flaps, ailerons, fairings and sub-systems. The delivery of the first shipset to Lockheed Martin's Final Assembly and Check Out facility in Fort Worth, Texas, USA is on-schedule for August 2016, with subsequent confirmed orders extending out to 2018. In addition to the production for the F-35 aircraft occurring in the Group's Delta facility, its Gardena facility, Avcorp Composite Fabrication manufactures complex composite flight control surfaces in support of Lockheed Martin's F-35 program. Revenues for this long-term defence program totaled $7,723,000 for the quarter ended June 30, 2016 (June 30, 2015: $4,609,000).

Shipments of large metallic assemblies to Boeing Commercial Airplane Group ("Boeing CA"), primarily for the 737 commercial jet program, increased by 3.3% during the second quarter 2016 relative to 2015. Concurrently, deliveries of fabricated parts to Boeing CA increased by 15.3%. During 2016, Avcorp delivered its first significant quantity of shipsets of composite fabricated aerostructures parts from its recently acquired Gardena production facility. Total revenues generated for the Company from various Boeing Commercial aircraft programs amounted to $19,501,000 (June 30, 2015: $5,897,000). The Company also delivers components to Boeing Defense, Space & Security ("Boeing DSS") for the Chinook CH47 helicopter. During the second quarter 2016 the Company generated $1,130,000 of revenues in supply to Boeing DSS, a slight increase in revenues recorded for the same period in 2015. The Avcorp Delta BC facility announced on October 26, 2015 that it has been awarded the production contract for the supply of Boeing 767-2C Panoramic Camera Fairings with initial deliveries commencing in the third quarter 2016. Furthermore, the Delta facility was able to secure the production contract for the Boeing 767 Flap Track Fairings with deliveries targeted for the second half of 2016. The Company continues to work towards obtaining additional new contracts supporting Boeing commercial jet programs as well as other Boeing DSS defense programs.

Revenues from Bombardier Aerospace ("Bombardier") programs slightly increased during the current quarter relative to the quarter ended June 30, 2015. Shipments of large assemblies for the CL605 business jet program decreased by $597,000 during the current quarter, while the Company experienced a $732,000 increase in its deliveries of composite floor panels to Bombardier as Avcorp adjusted production to match Bombardier demand. Avcorp Group's primary source of revenues from Bombardier in 2016 will continue to be from components for the CL605 and CL850 business jets, and composite floor panels for the CRJ and Q400 aircraft programs as well as a sustained high rate of production of composite floor panels in supply to Bombardier's Global 5000/6000 and Global 7000/8000 programs.

Avcorp's deliveries to Fuji Heavy Industries ("FHI") of large composite components in support of Boeing CA's 787 commercial jet program totalled $3,200,000 for the current quarter (June 30, 2015: $Nil).

Composite aircraft structure repair revenues out of Comtek continued with a strong performance, as current quarter 2016 revenues increased 76.2% over revenues in the previous year's second quarter. The Group also supplies Canadian aircraft retro-fit programs out of its Delta facility and large composite structures in support of various US defense programs out of its Gardena facility. These Other revenues are of significant importance to the Group's operations as they generated $8,485,000 in revenue during the second quarter 2016 (June 30, 2015: $4,721,000).

Gross Profit

Gross profit (revenue less cost of sales) for the quarter ended June 30, 2016 was negative 13.9% of revenue as compared to positive 10.7% of revenue for the quarter ended June 30, 2015, a decrease of $8,311,000.

Gross profit as a percentage of revenues has decreased during 2016 relative to the same quarter in 2015 primarily as a result of significant start-up operational deficiencies and production process inefficiencies for Avcorp's recently acquired Hitco operations.

The start-up, post-acquisition of the new operations in Gardena faced several unanticipated challenges during the first half of 2016. As a result of legacy quality issues raised by customers, a number of items were identified that required corrective action. These items accounted for substantial expenditures beyond normal production costs. Staffing levels during the second quarter 2016, for the Gardena facility, continued to remain very high relative to production deliveries as the operations utilized production resources to implement customer supported corrective actions. The implementation of the necessary corrective actions limited production output during the first half of 2016 and was the major contributor to lower than forecasted sales. Gross margin on production contracts acquired from the Hitco acquisition, inclusive of legacy operational deficiency rectification costs amounted to negative $7,647,000 for the current quarter (June 30, 2015:$Nil).

Many corrective actions have been implemented; and as legacy operational deficiencies are rectified, additional operational improvements will be made in the second half of 2016 thereby allowing the Gardena operations to achieve fully contracted output levels. Avcorp's key commercial customers have worked collaboratively with Avcorp to mitigate production schedule risks and support the earliest resolution of the outstanding process and product issues.

Delta and Burlington production contracts, which were pre-existing to the Hitco acquisition, produced a gross margin for the quarter ended June 30, 2016 which amounted to $1,514,000 as compared to $2,178,000 for the same quarter in 2015; a $664,000 decrease.

There remain within operations significant levels of unutilized plant capacity. The Company has expensed $935,000 of overhead costs during the current quarter (June 30, 2015: $1,204,000) in respect of unutilized plant capacity.

Administration and General Expenses

As a percentage of revenue, the administration and general expenses decreased to 14.8% for the quarter ended June 30, 2016 from 15.6% for the quarter ended June 30, 2015. In absolute terms, administration and general costs increased by $3,384,000 during the current quarter relative to the same quarter in the prior year. Legal and professional services incurred during the current quarter have been substantial as the Company administers various contracts and agreements assigned from and ancillary to its asset purchase agreement with Frankfurt-listed SGL on December 18, 2015.

Foreign Exchange Gain or Loss

Avcorp Group recorded a $150,000 foreign exchange loss during the second quarter 2016 (June 30, 2015: $61,000 gain) as a result of holding US dollar denominated cash, receivables, payables and debt. The Company's US operations are entirely denominated in US dollars, giving rise to foreign exchange gains and losses as the US dollar/Canadian dollar rate of exchange fluctuates.

Earnings Before Interest, Taxes, Depreciation & Amortization

Avcorp Group presents earnings before interest, taxes, depreciation and amortization ("EBITDA") to assist the Company's stakeholders with their assessment of its financial performance. EBITDA is a financial measure not recognized as a term under IFRS. However, the Company's management believes that the Company's stakeholders consider this metric to be useful information to assist them in evaluating profitability and liquidity.

EBITDA was negative $10,913,000 for the quarter ended June 30, 2016 compared to a negative EBITDA of $623,000 for the quarter ended June 30, 2015. Significant pre-existing operational deficiencies and excessive cost structure within the newly acquired Hitco operations have resulted in poor production contract performance and adversely affected Group earnings for the first half of 2016.

The financial results presented for the quarter ended June 30, 2016 do not take into account any recovery provision for these operational expenditures for which the Company believes it is indemnified for under its asset purchase agreement, and ancillary agreements, with SGL. These expenditure recovery amounts are not finalized and cannot be quantified for their full extent at this time.

The start-up, post-acquisition of the new operations in Gardena faced several unanticipated challenges during the first quarter 2016. As a result of legacy quality issues raised by customers, a number of items were identified that required corrective action. These items accounted for substantial expenditures beyond normal production costs. The implementation of the necessary corrective actions limited production output during the current quarter and was a major contributor to lower than forecasted sales.

The complexity and challenge of executing the production start-up and improvement plans for the Gardena operations have increased from the pre-acquisition estimates. Avcorp has worked successfully with the commercial aerospace customers to update plans and commitments to ensure support for their programs and a return to purchase order schedules by the end of third quarter of 2016.

EBITDA[1]

(unaudited, expressed in thousands of Canadian dollars)

	Three months ended June 30		Six months ended June 30	
	2016	2015	**2016**	2015
Income (loss) for the year	**$(12,951)**	$(1,135)	**$(25,042)**	$(3,896)
Interest expense and financing charges	**22**	71	**43**	95
Income tax expense	**-**	-	**-**	-
Depreciation	**868**	395	**1,728**	782
Amortization of development costs and intangibles	**1,148**	46	**2,382**	48
	(10,913)	(623)	**(20,889)**	(2,971)

1. This is not a recognized term under International Financial Reporting Standards.

Finance Costs

Total interest and financing charges on both short- and long-term debt for the quarter ended June 30, 2016 was $22,000, net of $2,000 interest income (June 30, 2015: $Nil), as compared to net $71,000 expense for the quarter ended June 30, 2015.

Income Taxes

Avcorp Group has not incurred a tax expense during the quarter (June 30, 2015: $Nil) nor recorded a tax benefit as it is not more likely than not that the benefit would be recognized.

Income or Loss

Loss for the quarter ended June 30, 2016 was $12,951,000 as compared to a $1,135,000 loss for the quarter ended June 30, 2015. The loss recorded for the current quarter relative to 2015, is primarily a result of significant start-up operational inefficiencies for Avcorp's recently acquired Hitco operations, as well as legal and professional services incurred during the current quarter which have been substantial as the Company administers various contracts and agreements assigned from and ancillary to its asset purchase agreement with Frankfurt-listed SGL on December 18, 2015. Significant pre-existing operational deficiencies and excessive cost structure within the newly acquired Hitco operations have resulted in poor production contract performance and significantly adversely affected Group earnings.

The financial results presented for the quarter ended June 30, 2016 do not take into account any recovery provision for these operational expenditures for which the Company believes it is indemnified for under its asset purchase agreement, and ancillary agreements, with SGL. These expenditure recovery amounts are not finalized and cannot be quantified for their full extent at this time.

Liquidity and Capital Resources

Avcorp Group's operating line of credit provides for a total utilization of $12,000,000. Avcorp Group ended the current quarter with bank operating line utilization of $1,511,000 offset by $5,052,000 cash compared to utilization of $Nil with $14,484,000 cash on hand as at December 31, 2015. Based on net collateral provided to its bank, Avcorp Group is able to draw $6,590,000 on its operating line of credit as at June 30, 2016 (December 31, 2015: $8,805,000).

On June 23, 2016, the Company's bank extended its banking agreement from June 30, 2016 to December 31, 2016.

Management is actively working to secure additional production orders, extension to its banking agreements, will continue to work with existing common shareholders, and will seek additional financing as necessary.

Cash Flows from Operating Activities

Cash flows from operating activities, before consideration of changes in non-cash working capital, decreased by $12,762,000 during the quarter ended June 30, 2016 as compared to utilizing $523,000 of cash during the quarter ended June 30, 2015. Cash flows from operating activities were most significantly impacted as a result of operational losses incurred under customer contracts assigned with the December 18, 2015 Hitco acquisition.

Non-cash operating assets and liabilities increased by $7,664,000 during the current quarter, compared to utilizing $2,057,000 of cash during the same quarter in 2015 primarily as accounts payable and accrued liabilities grew during the current quarter. There remains $17,747,000 consideration receivable from the Hitco acquisition as at June 30, 2016 (December 31, 2015: $38,720,000). Avcorp Group continues to closely monitor accounts receivable and work with its customers in order to ensure cash is collected on a timely basis.

Cash Flows from Investing Activities

During the quarter ended June 30, 2016, Avcorp Group purchased capital assets totalling $1,146,000 as compared to $147,000 during the quarter ended June 30, 2015. Avcorp Group continues to minimize its capital expenditures in order to conserve cash, with only operation critical expenditures being made.

Cash Flows from Financing Activities

Avcorp Group finances working capital through a combination of bank debt and equity financings.

Cash flows from financing activities provided $1,511,000 of cash during the current quarter as compared to providing $3,131,000 of cash in the same quarter in 2015; The Company's operating line was $1,511,000 drawn as at June 30, 2016 with $6,249,000 drawn as at June 30, 2015.

Under the SADI program from the Government of Canada, the Company was able to secure $28,000 in project financing (June 30, 2015: $91,000).

During the current quarter, the Company repaid long-term debt consisting of $58,000 of equipment financing (June 30, 2015: $109,000). No additional long term debt financing was secured during the quarter ended June 30, 2016 (June 30, 2015: $450,000).

On June 30, 2016, the ratio of the Company's current assets to current liabilities was 1.53:1 (June 30, 2015: 1.13:1), with the debt to equity ratio at (1.76):1 (June 30, 2015: 0.52:1).

Contractual Obligations

PAYMENTS DUE BY PERIOD

(unaudited, prepared in accordance with IAS 34, expressed in thousands of Canadian dollars)

	Total	2016	2017 – 2019	2020 – 2021	Post 2021
Finance lease obligations	**$169**	$22	$140	$7	$-
Term loan	**317**	55	262	-	-
Other long-term obligations[1]	**1,321**	-	69	71	1,181
Purchase obligations[2]	**44,571**	30,681	13,466	424	-
Total contractual obligations	**46,378**	30,758	13,937	502	1,181

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

The Company expects that payment of contractual obligations will come from funds generated by operations, utilization of the bank operating line of credit, cash on hand 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 condensed interim consolidated financial statements.

Capital Stock

As at June 30, 2016, there were 307,141,184 common shares, 30,263,318 common share purchase warrants, and 52,525,000 stock options issued and outstanding.

Common Shares

During the second quarter 2016 holders of the Company's stock options exercised 960,500 stock options at a price of $0.085 and 625,500 stock options at a price of $0.05 resulting in the issuance of 1,586,000 common shares with a value of $113,000.

No common shares were issued by the Company during the second quarter 2015.

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 307,141,184 common shares issued at June 30, 2016. The book value of common shares issued and outstanding as at June 30, 2016 was $80,302,000 (December 31, 2015: $80,158,000).

Accounting standards issued but not yet applied

The following is a brief summary of the new standards:

IFRS 15 – Revenue from Contracts with Customers

The International Accounting Standards Board ("IASB") and the US Financial Accounting Standards Board ("FASB") (collectively, "the Boards") have jointly issued a new revenue standard, IFRS 15 *Revenue from Contracts with Customers*, that will supersede virtually all revenue recognition requirements in IFRS and US GAAP.

IFRS 15 establishes principles to address the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers.

This standard is required to be applied for accounting periods beginning on or after January 1, 2018, 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 9 – Financial Instruments

In July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments* which reflects all phases of the financial instruments project and replaces IAS 39 *Financial Instruments: Recognition and Measurement* and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting. IFRS 9 is effective for annual periods beginning on or after January 1, 2018, with early application permitted. Retrospective application is required, but comparative information is not compulsory. Early application of previous versions of IFRS 9 (2009, 2010 and 2013) is permitted if the date of initial application is before February 1, 2015. The adoption of IFRS 9 will have an effect on the classification and measurement of the Group's financial assets, but no impact on the classification and measurement of the Group's financial liabilities.

IFRS 16 - Leases

In January 2016, the IASB issued IFRS 16 – Leases which replaces IAS 17 – Leases and its associated interpretative guidance. IFRS 16 applies a control model to the identification of leases, distinguishing between a lease and a service contract on the basis of whether the customer controls the asset being leased. For those assets determined to meet the definition of a lease, IFRS 16 introduces significant changes to the accounting by lessees, introducing a single, on-balance sheet accounting model that is similar to current finance lease accounting, with limited exceptions for short-term leases or leases of low value assets. Lessor accounting remains similar to current accounting practice. The standard is effective for annual periods beginning on or after January 1, 2019, with early application permitted for entities that apply IFRS 15. The Company has not yet assessed the impact the final standard is expected to have on its condensed interim consolidated financial statements.

Operations Overview

Delivery and Quality Performance

Deliveries and quality performance as at June 30, 2016 for Canadian manufacturing operations were at customer required levels. The manufacturing operations have achieved, and continue to maintain, top quality and delivery ratings for the majority of their programs.

Avcorp in the course of its due diligence of the assets and liabilities prior to closing the acquisition of ACF, the carve out of Hitco, discovered a number of issues. The seller and its ultimate parent SGL Carbon SE have the contractual responsibility and liability for all completed products before the closing with the exception of a limited amount of finished goods and manufacturing work in process for which Avcorp elected to assume the responsibility and verify the quality of these products. Immediately after the ACF acquisition, a thorough quality and delivery review and audit was conducted of the ACF Gardena manufacturing operations by ACF, which has produced improvement plans together with its customers. ACF continues to work collaboratively with customers to ensure any quality and delivery issues are resolved at the earliest date. ACF is on schedule to meet all the targets established in the improvement plans with its customers.

Order Backlog

Avcorp Group 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; new production contracts entered into during 2015 and 2016 extend to 2028 and 2019 respectively. Production contracts underlying Boeing's general term agreements, which were assigned to Avcorp with the Hitco acquisition, extend to 2023.

Agreements with Boeing Defense, Space and Security extend from 2013 into 2019 with established minimum base delivery quantity requirements.

The Bombardier agreements extend for the life of the individual aircraft programs.

Agreements with Lockheed Martin extend into 2018, with negotiations occurring for follow-on orders to existing statements of work through to 2020.

Agreements with BAE Systems (Operations) Limited extend into 2018 and continue to generate additional sales order backlog.

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. Order backlog is a financial measure not recognized as a term under IFRS. However, the Company's management believes that the Company's stakeholders consider this metric to be useful information to assist them in evaluating profitability and liquidity.

The order backlog, as at June 30, 2016, is $395 million, ($84 million of which pertains to 2016), compared to $404 million as at March 31, 2016. The changes in order backlog are as follows:

- $44 million decrease in order backlog resulting from revenues recorded during the quarter ended June 30, 2016;
- $37 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 continued to meet targeted levels during the quarter; the Company continues to monitor supplier performance in all aspects of quality, delivery and price. The Company works closely with its supply chain to ensure a stable, uninterrupted delivery of compliant products and is making changes in product sourcing processes where necessary.

During 2014 the company qualified certain suppliers in support of its in-house transition to increasingly value-added production processes. These suppliers will support the Company by providing manufacturing capabilities, to which Avcorp has transitioned in 2015; the process is a critical cost reduction process which will continue into 2016.

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 were in a surplus position of $30,351,000 at June 30, 2016 and $55,045,000 at December 31, 2015. Working capital decreased during 2016 as cash was utilized in operating activities.

Financial Resources

Avcorp Group has invested in its chosen strategies of organic growth, capabilities acquisition, lean manufacturing and strategic outsourcing. Management believes that significant investments necessary to better position Avcorp Group 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, business systems, technologies, processes and qualifications. 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 June 30, 2016 was 814 (December 31, 2015: 776). 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 Avcorp Group faces are summarized as follows:

- additional financing is required to maintain and grow its business;
- no agreement on extension of customer contracts, or terminated customer programs are not replaced;

- increases in material costs, primarily aluminum plate, composite materials, 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 changes in revenue levels;
- the trend to greater use of composite material in primary structures in each new generation of aircraft; and
- decrease in the value of the Canadian dollar, relative to the US dollar, has an adverse effect on the Canadian dollar equivalent value of those Company procured goods and services which are denominated in US dollars.

The Company's view is that with its strategic plan in place and the continued integration of composite design and manufacturing capabilities, 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

Avcorp Group'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 transitional operating losses incurred upon integration of newly acquired entities;
- 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.

Customer Contracts

The Company is exposed to the risk that existing customer fixed-term contracts are not renewed at expiration date. Avcorp Group operates within "general terms agreements" with its customers. These agreements are typically for five years or longer. The Company's agreements with Boeing CA extend from current date, with various expiry timelines, through to the end of 2023. Agreements with Boeing DSS have been renewed and established which extend from 2013 into 2019 with minimum base quantity requirements. It is the Company's objective to successfully renew Boeing production contracts in advance of expiry dates.

The Bombardier agreements extend for the life of the individual aircraft programs.

BAE and Lockheed Martin customer contracts extend into 2018. The Company is currently negotiating the extension of follow-on contracts.

The Company continues to face the financial risk that the wind-down in previous years of certain program contracts have not been replaced on a timely basis thereby causing the Company to continue to bear significant levels of expenses related to under-utilized operational capacity. The Company has restructured its business development strategy in order to best mitigate this risk and is now commencing to be awarded new customer production contracts.

Procured Materials and Parts

The Company is engaging suppliers and customers to properly align production requirements and pricing, ensuring uninterrupted delivery of compliant products with a cost structure closely matching product pricing. 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 larger business jets would continue to grow beyond 2015. The lighter business jets' market is expected to show modest growth.

- 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 CL650 aircraft production requirements have reduced in 2016 relative to 2015. The production build is expected to increase slightly in 2017 and the forecast is to remain flat through 2020.
- The market for defence aircraft flattened in 2015, after growth in previous years, due to general global budget challenges. Defence spending in North America and Europe is expected to decrease in the near term.
- The F-35 remains, on a global scale, one of the largest Defence Airplane programs for the foreseeable future. However, under the current North American Federal Governments' initiatives of cost controls regarding defence 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 exists to provide additional revenue from this aerospace sector.

Competitors

The long-term trend continues towards more intense competition from larger entities having operations in Asia, Mexico and Europe, while original equipment manufacturers 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 62% of Avcorp Group's cost of sales is related to labour and overhead and 38% related to procurement of raw materials and finished parts. The Company's wage rates are generally lower than its western European and north western United States competitors and higher than those in the south eastern United States, Asia, Eastern Europe and Mexico. On July 30, 2013 the labour force, at the Delta facility, ratified a new six year collective agreement. The agreement was ratified by a two-thirds majority, with the new agreement expiring on March 31, 2019. Subsequent to the Hitco acquisition the Company and the labour force, in Gardena, agreed to a four month extension of the current collective agreement, which was to expire February 29, 2016. On June 29, 2016 the labour force at the Gardena facility ratified a new six year collective agreement, adding language that allows for High Performance Work Teams and incentive bonus payments for accomplishing annual targets regarding operational and quality performance.

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 with 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 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. As well, the Company's Delta location is supplementing its current operations with composite manufacturing capabilities leveraging existing production capacity and investments.

Effective December 18, 2015, Avcorp completed the acquisition of the US-based composite Aerostructures division of Hitco Carbon Composites Inc., a subsidiary of Frankfurt-listed SGL Carbon SE. The Acquisition was completed pursuant to the terms of an asset purchase agreement that was entered into on July 20, 2015, and subsequent amendments to December 18, 2015. Pursuant to the Agreement Avcorp's subsidiary, Avcorp Composite Fabrication Inc., purchased the assets of the division of Hitco which produces composite structural parts for commercial and military aerostructures.

The acquisition of Hitco's Aerostructures composite division has provided a unique opportunity to transform the Avcorp Group's existing metal fabrication and integrated assembly business by broadening the product range and strengthening our composite capabilities. Advanced composite fabrication capabilities, provided by this acquisition, enhances Avcorp Group's ability to participate in large aerospace assembly programs which combine mixed material components.

US Dollar Revenues

Avcorp Group sells a significant proportion of its products in US dollars, partially from its Canadian operations and entirely within its United States operations, at prices which are often established well in advance of manufacture and shipment dates. As the value of the Canadian dollar decreases, the equivalent value of US dollar denominated revenues increases; conversely, the cost of US dollar denominated purchases will increase. The Company is continuing to structure new agreements with customers which mitigate the risk associated with currency fluctuations. It should be noted that a significant portion of the Company's purchases of raw materials, supplier fabricated parts, as well as equipment purchases, are denominated in US dollars. The Company's US operations are entirely denominated in US dollars giving rise to foreign exchange gains and losses as the US dollar/Canadian dollar rate of exchange fluctuates.

Outlook

Variability of the Canadian dollar relative to the US dollar continues to cause the value of the Company's current order backlog to fluctuate. The Company continues to work towards securing additional defence program production contracts in order to augment and diversify its backlog. The Company began delivering products under its defence contracts in 2009 and continues to negotiate long-term supply agreements. Both defence and commercial production contracts are being renewed, with select new customer agreements extending into 2023. The Company expects to finance investment in the start-up of new production programs primarily by milestone payments from customers, though this cannot be assured. Avcorp Group may require financing for capital expenditures required for new programs.

Boeing is the Company's largest customer in the second quarter 2016, followed by BAE Systems, Bombardier, Fuji Heavy Industries, and Lockheed Martin. The Company forecasts its 2016 revenues to increase significantly above 2015 levels as the December 18, 2015 Hitco Aerostructures division acquisition takes effect for an entire year.

The Company forecasts its working capital financing requirements for 2016 to be met by the current availability of the operating line of credit and the current working capital surplus. However, further debt and equity financing may be required.

Transactions with Related Parties

During the quarter ended June 30, 2016, consulting services were provided by certain directors. Fees paid to certain directors, or companies with which they have beneficial ownership, during the quarter ended June 30, 2016 amounted to $129,000 (June 30, 2015: $39,000). Fees payable to certain directors or Companies with which they have beneficial ownership, as at June 30, 2016 are $22,000 (June 30, 2015: $17,000). These fees are included in the Condensed Interim Consolidated Statements of (Loss) Income and Comprehensive (Loss) Income as administrative and general expenses and amount to $151,000 for the quarter ended June 30, 2016 (June 30, 2015: $56,000).

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

KEY MANAGEMENT COMPENSATION

(unaudited, expressed in thousands of Canadian dollars)

	Three months ended June 30		Six months ended June 30	
	2016	2015	2016	2015
Salaries and other short-term employee benefits	**$764**	$336	$1,151	$765
Contributions to defined contribution plan	**19**	11	33	22
Option-based awards	**600**	245	727	490
	1,383	592	1,911	1,277

The balance of loans receivable from key management as at June 30, 2016 is $15,000 (December 31, 2015: $15,000).

Other related party transactions are disclosed elsewhere in these condensed interim consolidated financial statements.

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

Business Acquisition

Effective December 18, 2015, Avcorp completed the acquisition of the US-based composite Aerostructures division of Hitco Carbon Composites Inc., a subsidiary of Frankfurt-listed SGL Carbon SE. The Acquisition was completed pursuant to the terms of an asset purchase agreement that was entered into on July 20, 2015, and subsequent amendments to December 18, 2015. Pursuant to the Agreement Avcorp's subsidiary, Avcorp Composite Fabrication Inc., purchased the assets of the division of Hitco which produces composite structural parts for commercial and military aerostructures.

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 interim consolidated financial statements for the quarter ended June 30, 2016.

Critical Accounting Estimates and Judgment

The preparation of condensed interim consolidated financial statements in conformity with IAS 34 requires management to make estimates and judgments that affect the amounts which are reported in the condensed interim 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 condensed interim consolidated statements of financial position amounting to $29,291,000 (December 31, 2015: $29,880,000). 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 production 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 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 June 30, 2016, $4,615,000 (December 31, 2015: $3,187,000) in unamortized deferred tooling costs, which are expected to have a future economic benefit, are presented as Development costs in the condensed interim consolidated statements of financial position. Development costs of $569,000 (December 31, 2015: $569,000) are internally generated and 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. As at June 30, 2016 the provision for anticipated losses was $75,000 (December 31, 2015: $114,000).
- Estimating the fair value of the unfavorable contract liability assumed in conjunction with the acquisition of the US-based composite Aerostructures division of Hitco Carbon Composites Inc., a subsidiary of Frankfurt-listed SGL Carbon SE, is subject to significant judgment, including selecting margin assumptions that would be used by market participants and the selection of an appropriate discount rate that reflects the risk and uncertainty associated with the liability. The Company has a provision for unfavourable contracts in the amount to $78,614,000 as at June 30, 2016 (December 31, 2015: $89,971,000). This unamortized unfavourable contract liability is accrued in US dollars and therefore the unamortized balance will vary from quarter to quarter as the estimated provision is adjusted for foreign currency fluctuations.

- On a periodic basis the Company reviews its plant capacity and estimates the portion of its under-utilized overhead expenditures. The Company has expensed $935,000 of overhead costs during the current quarter (June 30, 2015: $1,204,000) in respect of unutilized plant capacity.

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 $1,511,000 is utilized as at June 30, 2016 (June 30, 2015: $6,249,000). The Company lowers interest rate costs by managing utilization of the operating lines of credit to the lowest amount practical. For the quarter ended June 30, 2016, with other variables unchanged, a 1% change in the bank prime interest rate would have a $4,000 (June 30, 2015: $16,000) 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 and component parts in US dollars at prices that are usually established at the order date. All of the Company's operations are based in Canada and in the US. 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 during the second quarter of 2016 was $150,000 as compared to a $61,000 gain for the quarter ended June 30, 2015.

The Company had the following US dollar denominated balances:

CURRENCY RISK

(unaudited, expressed in thousands of US dollars)

FOR THE PERIOD ENDED JUNE 30	**2016**	2015
Bank cash position	**US$ 3,371**	US$ 543
Accounts receivable	**18,439**	4,604
Consideration receivable	**13,739**	-
Accounts payable net of prepayments	**20,172**	1,316

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 $1,538,000 in net income for the quarter ended June 30, 2016 (June 30, 2015: $383,000 increase (decrease) in net income) 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 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 ("BAES"), Fuji Heavy Industries Ltd. ("FHI"), Lockheed Martin Corporation ("LM") and Northrop Grumman Corporation ("Northrop"). During 2016 and 2015, 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 condensed interim consolidated statements of financial position.

As at the condensed interim consolidated statements of financial position date 70% (June 30, 2015: 82%) of the Company's trade accounts receivable are attributable to these customers.

Consideration receivable, arising from a 2015 business acquisition, is guaranteed by the Seller and in part a Canadian chartered bank.

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.

Capital Risk

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 condensed interim 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.

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 Chief 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 Chief Financial Officer have evaluated the Company's disclosure controls and procedures, and internal controls over financial reporting, as of June 30, 2016 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 June 30, 2016, that have materially affected, or are reasonably likely to materially affect the Company's internal controls over financial reporting.

Limitations on scope of design

The scope of design over disclosure controls and internal controls over financial reporting has been limited to exclude control, policies and procedures of ACF, which was acquired effective December 18, 2015.

The scope limitation is in accordance with section 3.3(1) (c) of National Instrument 52-109, which allows an issuer to limit the design of disclosure and control procedures and internal control over financial reporting to exclude controls, policies and procedures of a business that the issuer acquired not more than 365 days prior to June 30, 2016, the end of fiscal period.

Forward Looking Statements

This management discussion and analysis should be read in conjunction with the Company's audited consolidated 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, cancellation of orders or changes in production scheduling; (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 condensed interim consolidated financial statements of Avcorp Industries Inc. and all other information contained in the Management Discussion and Analysis are the responsibility of management. The condensed interim consolidated financial statements were prepared in conformity with IAS 34 Interim Financial Reporting ("IAS 34") appropriate in the circumstances, in a manner consistent with the previous quarter, 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 interim consolidated financial statements.

Management is responsible for maintaining a system of internal accounting controls and procedures to provide reasonable assurance. As at 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 IAS 34. 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 MERLO Chief Financial Officer and Corporate Secretary		**PETER GEORGE** Executive Officer and Group Chief Executive Officer

CONDENSED INTERM CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

(unaudited, prepared in accordance with IAS 34, expressed in thousands of Canadian dollars)

	June 30, 2016	December 31, 2015
ASSETS		
Current assets		
Cash (note 11)	**$5,052**	$14,484
Accounts receivable (note 5)	**28,386**	30,124
Consideration receivable (note 6)	**17,747**	26,624
Inventories (note 7)	**35,442**	36,383
Prepayments and other assets	**1,432**	1,424
	88,059	109,039
Non-current assets		
Prepaid rent and security	**428**	449
Consideration receivable (note 6)	**-**	12,096
Development costs (note 8)	**4,615**	3,187
Property, plant and equipment (note 9)	**29,291**	29,880
Intangibles (note 10)	**12,987**	16,095
Total assets	**135,380**	170,746
LIABILITIES AND EQUITY		
Current liabilities		
Bank indebtedness (note 11)	**1,511**	-
Accounts payable and accrued liabilities (note 13)	**33,242**	27,087
Current portion of long-term debt (note 16)	**156**	240
Customer advance (note 12)	**9,791**	10,408
Deferred program revenues (note 14)	**3,709**	4,924
Unfavourable contracts liability (note 15)	**9,299**	11,335
	57,708	53,994
Non-current liabilities		
Deferred gain	**97**	121
Lease inducement	**222**	271
Long-term debt (note 16)	**1,650**	1,646
Customer advance (note 12)	**6,948**	12,697
Unfavourable contracts liability (note 15)	**69,315**	78,636
Deferred program revenues (note 14)	**177**	-
Deferred income taxes payable	**1,152**	1,235
	137,269	148,600
Equity		
Capital stock (note 17)	**80,302**	80,158
Contributed surplus	**4,887**	4,453
Accumulated other comprehensive income	**429**	-
Deficit	**(87,507)**	(62,465)
	(1,889)	22,146
Total liabilities and equity	**135,380**	170,746

Nature of operations (note 1)

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

Approved by the Board of Directors on August 14, 2016

David Levi
Chairman

Eric Konn TD
Committee Chair, Audit & Corporate Governance Committee

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

(unaudited, prepared in accordance with IAS 34, expressed in thousands of Canadian dollars, except number of shares and per share amounts)

	Three months ended June 30		Six months ended June 30	
	2016	2015	**2016**	2015
Revenues	**$44,246**	$20,369	**$79,593**	$36,030
Cost of sales (note 3)	**50,379**	18,191	**92,291**	33,319
Gross profit	**(6,133)**	2,178	**(12,698)**	2,711
Administrative and general expenses (note 3)	**6,566**	3,182	**12,175**	6,259
Office equipment depreciation (note 3)	**82**	121	**307**	249
Operating (Loss)	**(12,781)**	(1,125)	**(25,180)**	(3,797)
Finance costs – net (note 18)	**20**	71	**32**	94
Foreign exchange (gain) loss	**150**	(61)	**(120)**	5
Gain on sale of equipment	**-**	-	**(50)**	-
(Loss) Income before income tax	**(12,951)**	(1,135)	**(25,042)**	(3,896)
Income tax expense	**-**	-	**-**	-
Net (loss) income for the period	**(12,951)**	(1,135)	**(25,042)**	(3,896)
Other comprehensive income	**58**	-	**(429)**	-
(Loss) and total comprehensive (loss) income for the period	**(13,009)**	(1,135)	**(24,613)**	(3,896)
(Loss) Earnings per share:				
Basic (loss) earnings per common share (note 21)	**(0.04)**	(0.00)	**(0.08)**	(0.01)
Diluted (loss) earnings per common share (note 21)	**(0.04)**	(0.00)	**(0.08)**	(0.01)
Basic weighted average number of shares outstanding (000's) (note 21)	**306,570**	302,633	**306,065**	302,633
Diluted weighted average number of shares outstanding (000's) (note 21)	**306,570**	302,633	**306,065**	302,633

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

CONDENSED INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS

(unaudited, prepared in accordance with IAS 34, expressed in thousands of Canadian dollars)

	Three months ended June 30		Six months ended June 30	
	2016	2015	**2016**	2015
Cash flows from (used in) operating activities				
Net (loss) income for the period	**$(12,951)**	$(1,135)	**$(25,042)**	$(3,896)
Adjustment for items not affecting cash:				
Accrued interest and government royalties	**18**	18	**38**	36
Depreciation	**868**	395	**1,728**	782
Development cost amortization	**134**	46	**287**	48
Intangible assets amortization	**1,014**	-	**2,095**	-
Loss (gain) on disposal of equipment	**-**	-	**(50)**	-
Provision for onerous contracts	**(3,224)**	-	**(5,498)**	-
Provision for loss-making contracts and obsolete inventory	**963**	(63)	**996**	130
Provision for doubtful accounts	**(204)**	-	**-**	-
Stock based compensation	**652**	246	**465**	492
Other items	**(32)**	(30)	**(64)**	(62)
	(12,762)	(523)	**(25,045)**	(2,470)
Changes in non-cash working capital				
Accounts receivable	**1,447**	(102)	**(356)**	(1,540)
Consideration receivable	**(612)**	-	**18,939**	-
Inventories	**2,509**	(89)	**(445)**	(1,603)
Prepayments and other assets	**33**	(179)	**(20)**	164
Accounts payable and accrued liabilities	**8,762**	432	**7,644**	1,749
Customer advance	**(2,358)**	-	**(4,969)**	-
Deferred program revenues	**(2,117)**	(2,119)	**(1,575)**	(3,471)
Net cash from (used in) operating activities	**(5,098)**	(2,580)	**(5,827)**	(7,171)
Cash flows from (used in) investing activities				
Proceeds from sale of equipment	**-**	-	**50**	-
Purchase of equipment	**(1,146)**	(147)	**(2,628)**	(788)
Payments relating to development costs and tooling	**(671)**	(403)	**(1,715)**	(1,095)
Net cash from (used in) investing activities	**(1,817)**	(550)	**(4,293)**	(1,883)
Cash flows from (used in) financing activities				
Increase (decrease) in bank indebtedness	**1,511**	3,131	**1,511**	6,249
Payment of interest	**(6)**	(8)	**(14)**	(17)
Proceeds from current and long term debt	**28**	91	**59**	753
Proceeds from issuance of common shares	**113**	-	**113**	-
Repayment of current and long-term debt	**(58)**	(109)	**(163)**	(184)
Net cash from (used in) financing activities	**1,588**	3,105	**1,506**	6,801
Net increase (decrease) in cash	**(5,327)**	(25)	**(8,614)**	(2,253)
Net foreign exchange difference	**(114)**	(26)	**(818)**	(76)
Cash - Beginning of period	**10,493**	881	**14,484**	3,159
Cash - End of period	**5,052**	830	**5,052**	830

Supplementary Cash Flow Information (note 19)

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

CONDENSED INTERIM CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY

(unaudited, prepared in accordance with IAS 34, expressed in thousands of Canadian dollars, except number of shares)

	Share capital					
	Shares	**Amount**	**Contributed Surplus**	**Deficit**	**Accumulated Other Comprehensive Income**	**Total equity**
Balance December 31, 2014	302,633,184	$79,921	$3,129	$(65,673)	$ -	$17,377
Stock based compensation expense	-	-	492	-	-	492
Loss for the period	-	-	-	(3,896)	-	(3,896)
Balance June 30, 2015	302,633,184	79,921	3,621	(69,569)	-	13,973
Balance December 31, 2015	305,555,184	80,158	4,453	(62,465)	-	22,146
Issue of Common Shares	1,586,000	113	-	-	-	113
Stock-based compensation expense	-	-	885	-	-	885
Cancellation of issued stock options	-	-	(420)	-	-	(420)
Transfer to share capital on exercise of stock options	-	31	(31)	-	-	-
Unrealized currency gain on translation for the period	-	-	-	-	429	429
Loss for the quarter	-	-	-	(25,042)	-	(25,042)
Balance June 30, 2016	**307,141,184**	**80,302**	**4,887**	**(87,507)**	**429**	**(1,889)**

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

1. Nature of Operations

Avcorp Industries Inc. (the "Company" or "Avcorp") 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 currently operate from two locations in Canada and one location in the United States. Located in Delta, British Columbia, Avcorp Industries Inc., named as Avcorp Structures & Integration ("ASI"), is dedicated to metallic and composite aerostructures assembly and integration. Within Comtek Advanced Structures Ltd. ("Comtek") located in Burlington, Ontario, exists two divisions: Comtek, dedicated to aircraft structural component repair services, and Avcorp Engineered Composites ("AEC") dedicated to design and manufacture of composite aerostructures. Located in Gardena, California, Avcorp Composite Fabrication Inc. ("ACF") is dedicated to advanced composite aerostructures fabrication.

Avcorp Composite Fabrication Inc. is wholly owned by Avcorp US Holdings Inc. Both companies are incorporated in The State of Delaware and are subsidiaries of Avcorp Industries Inc.

Comtek Advanced Structures Ltd., incorporated in the Province of Ontario is a wholly owned subsidiary of Avcorp Industries Inc.

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

The condensed interim consolidated financial statements of the Company for the quarter ended June 30, 2016 were authorized for issue in accordance with a resolution of its Board of Directors on August 14, 2016.

2. Basis of Preparation and Measurement

The condensed interim consolidated financial statements of the Company have been prepared in accordance with IAS 34 – Interim Financial Reporting ("IAS 34").

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

Accounting standards issued but not yet effective

The following is a brief summary of the new standards issued but not yet effective:

IFRS 15 – Revenue from Contracts with Customers

The International Accounting Standards Board ("IASB") and the US Financial Accounting Standards Board ("FASB") (collectively, "the Boards") have jointly issued a new revenue standard, IFRS 15 *Revenue from Contracts with Customers*, that will supersede virtually all revenue recognition requirements in IFRS and US GAAP.

IFRS 15 establishes principles to address the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers.

This standard is required to be applied for accounting periods beginning on or after January 1, 2018, 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 9 – Financial Instruments

In July 2014, the IASB issued the final version of IFRS 9 *Financial Instruments* which reflects all phases of the financial instruments project and replaces IAS 39 *Financial Instruments: Recognition and Measurement* and all previous versions of IFRS 9. The standard introduces new requirements for classification and measurement, impairment, and hedge accounting. IFRS 9 is effective for annual periods beginning on or after January 1, 2018, with early application permitted. Retrospective application is required, but comparative information is not compulsory. The adoption of IFRS 9 will have an effect on the classification and measurement of the Group's financial assets, but no impact on the classification and measurement of the Group's financial liabilities.

IFRS 16 - Leases

In January 2016, the IASB issued IFRS 16 – Leases which replaces IAS 17 – Leases and its associated interpretative guidance. IFRS 16 applies a control model to the identification of leases, distinguishing between a lease and a service contract on the basis of whether the customer controls the asset being leased. For those assets determined to meet the definition of a lease, IFRS 16 introduces significant changes to the accounting by lessees, introducing a single, on-balance sheet accounting model that is similar to current finance lease accounting, with limited exceptions for short-term leases or leases of low value assets. Lessor accounting remains similar to current accounting practice. The standard is effective for annual periods beginning on or after January 1, 2019, with early application permitted for entities that apply IFRS 15. The Company has not yet assessed the impact the final standard is expected to have on its condensed interim consolidated financial statements.

3. Expenses by Nature

The Condensed Interim Consolidated Statements of (Loss) Income and Comprehensive (Loss) Income presents expenses by function. Accordingly, amortization and depreciation is not 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.

Expenses by nature:

	Three months ended June 30		Six months ended June 30	
	2016	2015	**2016**	2015
Raw materials, purchased parts and consumables	**$24,590**	$8,625	**$42,065**	$15,051
Salary, wages and benefits	**20,354**	8,397	**41,140**	16,491
Contracted services and consulting	**4,702**	713	**7,625**	1,309
Plant equipment rental and maintenance	**2,015**	68	**4,108**	123
Other expenses and conversion of costs into inventory	**1,746**	868	**2,429**	1,530
Utilities	**1,565**	275	**2,776**	539
Amortization of intangible assets	**1,014**	-	**2,095**	-
Rent	**907**	642	**1,755**	1,283
Depreciation	**868**	395	**1,728**	782
Legal and audit fees	**842**	340	**973**	428
Transportation	**543**	266	**1,122**	472
Travel costs	**523**	170	**937**	398
Office equipment rental/maintenance	**236**	176	**659**	338
Royalties	**137**	88	**193**	174
Amortization of development costs	**134**	46	**287**	48
Insurance	**75**	96	**379**	192
Performance Guarantee fees	**-**	329	**-**	669
Change in onerous contracts provision	**(3,224)**	-	**(5,498)**	-
	57,027	21,494	**104,773**	39,827

4. Fair Value Measurement

The fair values of the Company's accounts receivable, accounts payable and accrued liabilities are estimated to approximate their carrying values due to their immediate or short-term maturity. The portion of the consideration receivable which was long-term and has been discounted to take this into effect. A portion of the Company's long-term debt is held with Industrial Technologies Office, which is a governmental body; the remaining long-term debt is in the form of finance leases which will be re-paid within five years, for which fair value is not materially different from the value recorded.

The following table provides the fair value measurement hierarchy of the Company's financial assets and liabilities.

				June 30, 2016
	Total	**Quoted prices in active markets (Level 1)**	**Significant observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**
Assets not measured at fair value:				
Consideration receivable	$17,747	-	-	$17,747
Liabilities not measured at fair value:				
Long-term debt	1,806	-	1,806	-

				December 31, 2015
	Total	**Quoted prices in active markets (Level 1)**	**Significant observable inputs (Level 2)**	**Significant unobservable inputs (Level 3)**
Assets not measured at fair value:				
Consideration receivable	$38,720	$ -	$ -	$38,720
Liabilities not measured at fair value:				
Long-term debt	1,886	-	1,886	-

5. Accounts Receivable

	June 30, 2016	December 31, 2015
Trade receivables	**$27,959**	$29,815
Input tax credits	**311**	230
Accrued receivables	**116**	79
	28,386	**30,124**

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

	June 30, 2016	December 31, 2015
US dollar	**US$ 18,439**	US$ 18,487
Canadian dollar	**4,568**	4,538

6. Consideration Receivable

On December 18, 2015, in conjunction with the acquisition of the US-based composite Aerostructures division of Hitco Carbon Composites Inc., a subsidiary of Frankfurt-listed SGL Carbon SE, Avcorp received $32,826,000 (USD$23,540,000) in cash consideration with $17,747,000 (USD$14,220,000 undiscounted) consideration receivable as at June 30, 2016 on a discounted basis (December 31, 2015: $38,720,000). The consideration receivable takes the form of:

- Avcorp received $5,864,000 (USD$4,237,000) in cash from SGL, the parent company of Hitco on January 4, 2016 in payment of past due trade payables assumed by Avcorp on acquisition close date;
- Avcorp received $14,048,000 (USD$10,000,000) in cash from SGL, the parent company of Hitco on January 31, 2016;
- Avcorp will receive in kind supplies and/or payments totaling up to $6,459,000 (USD$5,000,000) through December 31, 2016 with any unused portion collectible in cash; and

- Avcorp will receive $11,909,000 net in cash from SGL, parent company of Hitco on or before March 31, 2017. The USD$9,220,000 undiscounted long-term gross consideration receivable has been discounted to arrive at the acquisition date fair market value. This amount is guaranteed by SGL as well as a Canadian chartered bank.

7. Inventories

	June 30, 2016	December 31, 2015
Raw materials	**$13,202**	$16,914
Work-in-progress	**18,064**	14,243
Finished products	**4,176**	5,226
	35,442	36,383

The amount of inventory expensed in cost of sales during the quarter ended June 30, 2016 amounted to $49,398,000 (June 30, 2015: $16,941,000). The carrying value of inventory pledged as security under the Company's operating line of credit (note 16) as at June 30, 2016 is $16,299,000 (December 31, 2015: $14,460,000).

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 June 30, 2016 provision for anticipated losses was $75,000 (December 31, 2015: $114,000). 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.

8. Development Costs

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

	June 30, 2016	December 31, 2015
Opening balance	**$3,187**	$3,303
Additions	**1,715**	1,405
Amortization	**(287)**	(1,521)
	4,615	3,187

	June 30, 2016	December 31, 2015
Cost	**$10,279**	$8,564
Accumulated amortization	**(5,664)**	(5,377)
Net book amount	**4,615**	3,187

Customers have funded non-recurring costs incurred during the introduction of new production programs. These costs are deferred as development costs and will be amortized to income in conjunction with the associated revenue upon commencement of production, on a units-of-production basis over the expected life of the programs.

9. Property, Plant and Equipment

	Machinery and equipment	Computer hardware and software	Leasehold improvements	Total
Year ended December 31, 2015				
Opening net book amount	$6,525	$1,204	$475	$8,204
Additions	22,842	322	192	23,356
Disposals – cost	(133)	(28)	-	(161)
Disposals – accumulated depreciation	133	28	-	161
Depreciation charge	(1,079)	(460)	(141)	(1,680)
Closing net book amount	28,288	1,066	526	29,880
At December 31, 2015				
Cost	52,266	7,725	1,352	61,343
Accumulated depreciation	(23,978)	(6,659)	(826)	(31,463)
Net book amount	28,288	1,066	526	29,880
Period ended June 30, 2016				
Opening net book amount	28,288	1,066	526	29,880
Additions	2,325	290	13	2,628
Disposals – cost	-	-	-	-
Disposals – accumulated depreciation	-	-	-	-
Depreciation charge	(1,371)	(288)	(69)	(1,728)
Currency translation adjustment	(1,480)	(9)	-	(1,489)
Closing net book amount	27,762	1,059	470	29,291
At June 30, 2016				
Cost	53,104	8,006	1,365	62,475
Accumulated depreciation	(25,342)	(6,947)	(895)	(33,184)
Net book amount	27,762	1,059	470	29,291

The Company has $136,000 in commitments at June 30, 2016 (December 31, 2015: $221,000) to purchase property, plant and equipment in 2016.

Included in computer hardware and software are assets held under finance leases at a cost of $24,000 (December 31, 2015: $104,000) having accumulated depreciation of $7,000 (December 31, 2015: $85,000).

Included in machinery and equipment are assets held under finance leases at a cost of $237,000 (December 31, 2015: $930,000) having accumulated depreciation of $27,000 (December 31, 2015: $54,000).

10. Intangibles

	Lease	Customer contract – re-compete	Customer contract – order backlog	Total
Year ended December 31, 2015				
Opening net book amount	$ -	$ -	$ -	$ -
Additions	3,085	9,965	3,045	16,095
Disposals – cost	-	-	-	-
Disposals – accumulated amortization	-	-	-	-
Amortization charge	-	-	-	-
Closing net book amount	3,085	9,965	3,045	16,095
At December 31, 2015				
Cost	3,085	9,965	3,045	16,095
Accumulated depreciation	-	-	-	-
Net book amount	3,085	9,965	3,045	16,095
Period ended June 30, 2016				
Opening net book amount	3,085	9,965	3,045	16,095
Additions	-	-	-	-
Disposals – cost	-	-	-	-
Disposals – accumulated amortization	-	-	-	-
Amortization charge	(495)	(573)	(1,028)	(2,095)
Currency translation adjustment	(190)	(649)	(173)	(1,012)
Closing net book amount	2,400	8,743	1,844	12,987
At June 30, 2016				
Cost	2,880	9,300	2,842	15,022
Accumulated amortization	(480)	(557)	(997)	(2,034)
Net book amount	2,400	8,743	1,845	12,987

11. 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 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 term is in effect:

- A permanent block of $2,500,000 against available credit.

On June 23, 2016, the Company's bank extended its banking agreement from June 30, 2016 to December 31, 2016.

The Company ended the current quarter with bank operating line utilization of $1,511,000 offset by $5,052,000 cash compared to utilization of $Nil with $14,484,000 cash on hand as at December 31, 2015. Based on net collateral provided to its bank, the Company is able to draw $6,590,000 on its operating line of credit as at June 30, 2016 (December 31, 2015: $8,805,000).

12. Customer advance

On December 18, 2015, in conjunction with the acquisition of the US-based composite Aerostructures division of Hitco Carbon Composites Inc., a subsidiary of Frankfurt-listed SGL Carbon SE, the Company assumed a customer advance for pre-funding of product deliveries. The customer advance is re-paid as the Company delivers to its customer, ordered products for a specific program. The customer advance is subject to an access and security agreement along with a general security agreement entered into with the Company's bank.

The remaining unamortized customer advance has been discounted to arrive at the June 30, 2016 amount of $16,739,000 (December 31, 2015: $23,105,000) of which it is estimated $9,791,000 will be amortized during the next twelve months. The Company re-paid and amortized into income $2,364,000 of the customer advance during the quarter ended June 30, 2016 (June 30, 2015: $Nil).

13. Accounts Payable and Accrued Liabilities

	June 30, 2016	December 31, 2015
Trade payables	**$26,637**	$21,080
Payroll-related liabilities	**5,580**	5,022
Performance guarantee fees	**-**	330
Restructuring provision	**594**	207
Other	**431**	448
	33,242	27,087

14. Deferred Program Revenues

	June 30, 2016	December 31, 2015
Opening balance	**$4,924**	$7,782
Additions	**4,347**	12,699
Realized	**(5,385)**	(15,557)
	3,886	4,924

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

Additionally, customers have funded non-recurring costs incurred during the introduction of new production programs. These costs are deferred as development costs and will be amortized to income, on a units-of-production basis over the expected life of the programs, in conjunction with the associated deferred revenue upon commencement of production.

15. Unfavourable Contracts Liability

On December 18, 2015, in conjunction with the acquisition of the US-based composite Aerostructures division of Hitco Carbon Composites Inc., a subsidiary of Frankfurt-listed SGL Carbon SE, the Company assumed an unfavorable contract liability on certain long term revenue contracts for which unavoidable costs are expected to exceed the corresponding revenues earned. The unfavorable contract liability is amortized into income on a units-of-production basis over the expected life of the contract.

As at June 30, 2016, the remaining unamortized unfavourable contract liability amounted to $78,614,000 (December 31, 2015: $89,971,000).

16. Long-Term Debt

	June 30, 2016	December 31, 2015
Finance leases (a)	**$169**	$278
Term loans (b) (c)	**317**	371
SADI (d)	**1,320**	1,237
	1,806	1,886
Less: Current portion	**(156)**	(240)
	1,650	1,646

a) Finance Leases

There are various equipment leases that have a weighted average interest rate of 7.58% 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.

b) Term Loan

On July 31, 2015, Avcorp entered into a non-revolving term loan agreement ("loan") with Panta Canada B.V. ("Panta") to fund the Company to a maximum aggregate principal amount of $5,000,000. The Company received full funding from the loan in three advances, with the final amount received on September 23, 2015.

Panta Canada B.V. is Avcorp's majority shareholder owning approximately 65.1% of the issued and outstanding common shares on June 30, 2016. Panta Canada B.V. is wholly owned by Panta Holdings B.V. Both companies are incorporated in The Netherlands and Mr. Jaap Rosen Jacobson, a director of the Company, is the sole shareholder of Panta Holdings B.V.

The Company's acceptance of this loan was subject to a 3% commitment fee ($150,000) paid by the Company to Panta Canada B.V. from proceeds of the first advance.

As consideration for the loan, the Company issued to Panta 30,263,318 common share purchase warrants ("warrants"), each warrant is exercisable for a period of 24 months following the date of issuance with respect to one common share at an exercise price of $0.07 per common share.

The proceeds of $5,000,000 were allocated between the debt and warrants and the debt was accrued over its term.

The loan bore interest at 8% per year, was subordinated to existing security agreements and could be prepaid without interest and penalties.

On December 29, 2015, Avcorp repaid $5,000,000 principal amount of the term loan and all accrued and outstanding interest. The difference between the face value and book value of the loan at the repayment date was charged to finance costs.

c) On March 13, 2015, the Company completed a secured term loan with a principal amount of $450,000. The Company received full funding from the loan on March 26, 2015. The purpose of the loan was to finance machinery and equipment required for new production programs at its Burlington ON facility.

The term loan has been provided by a Canadian chartered bank. The loan has a four year term; it is secured by a general security agreement constituting a first ranking security interest in all personal property of the Company and a first ranking and specific interest in the equipment financed. Export Development Canada ("EDC") has guaranteed 50% of the aggregate borrowings outstanding under the loan. The fee associated to the guarantee provided by EDC is equal to 3% of 50% of the outstanding loan amount. Interest will be calculated and paid monthly at a rate of bank prime plus 1%. The loan will be repaid over 48 months by way of blended principal and interest payments. The balance outstanding for this term loan as at June 30, 2016 is $317,000.

d) SADI

On April 23, 2014, the Company secured funding for certain non-recurring expenditures and manufacturing equipment. The Government of Canada under the Strategic Aerospace and Defence Initiative ("SADI") program has committed up to $4.4 million for funding of program eligible costs. The contribution amount represents 40% funding for eligible costs.

The contribution agreement has the following terms:

- The maximum amount to be repaid by the Company is 1.5 times the amount contributed by the Government of Canada;
- Repayments are to occur over a 15 year term, commencing two years following the fiscal year end, in which the contributions are completed; and
- Amounts repayable are unsecured.

$1,320,000 was drawn on this facility as at June 30, 2016 (December 31, 2015: $1,237,000).

17. Capital Stock

During the second quarter 2016 holders of the Company's stock options exercised 960,500 stock options at a price of $0.085 and 625,500 stock options at a price of $0.05 resulting in the issuance of 1,586,000 common shares with a value of $113,000.

No common shares were issued by the Company during the second quarter 2015.

18. Finance Costs

	Three months ended June 30		Six months ended June 30	
	2016	2015	**2016**	2015
Interest on finance leases	**$3**	$7	**$8**	$16
Interest on other long-term debt	**16**	15	**31**	24
Interest on short-term debt	**3**	49	**4**	55
Interest expense	**22**	71	**43**	95
Interest income	**(2)**	-	**(11)**	(1)
Net interest expense	**20**	71	**32**	94

19. Supplementary Cash Flow Information

Non-cash financing and investing activities:

	Three months ended June 30		Six months ended June 30	
	2016	2015	**2016**	2015
Equipment acquired under capital lease	**$ -**	$84	**$ -**	$84
Uncollected deferred tooling revenue	**(1,131)**	3,053	**537**	3,613

20. Related Party Transactions

a) During the quarter ended June 30, 2016, consulting services were provided by certain directors. Fees paid to certain directors, or companies with which they have beneficial ownership, during the quarter ended June 30, 2016 amounted to $129,000 (June 30, 2015: $39,000). Fees payable to certain directors or Companies with which they have beneficial ownership, as at June 30, 2016 are $22,000 (June 30, 2015: $17,000). These fees are included in the Condensed Interim Consolidated Statements of (Loss) Income and Comprehensive (Loss) Income as administrative and general expenses and amount to $151,000 for the quarter ended June 30, 2016 (June 30, 2015: $56,000).

b) 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.

	Three months ended June 30		Six months ended June 30	
	2016	2015	**2016**	2015
Salaries and other short-term employee benefits	**$764**	$336	**$1,151**	$765
Contributions to defined contribution plan	**19**	11	**33**	22
Option-based awards	**600**	245	**727**	490
	1,383	592	**1,911**	1,277

c) Loans to related parties

The balance of loans receivable from key management as at June 30, 2016 is $15,000 (December 31, 2015: $15,000).

Other related party transactions are disclosed elsewhere in these condensed interim consolidated financial statements (note 16b).

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

21. Earnings per share

Basic earnings per share amounts are calculated by dividing the net income 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 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.

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

	Three months ended June 30		Six months ended June 30	
	2016	2015	**2016**	2015
Weighted average number of common shares for basic earnings per share	**306,570**	302,633	**306,065**	302,633
Effect of dilution:				
Warrants	**-**	-	**-**	-
Share options	**-**	-	**-**	-
Weighted average number of ordinary shares adjusted for the effect of dilution	**306,570**	302,633	**306,065**	302,633

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

22. Economic Dependence and Segmented Information

For management purposes, the Company is organized into business units based on its products and services and has three reportable segments, as follows:

- The Avcorp Structures & Integration ("ASI") segment, which is dedicated to metallic and composite aerostructures assembly and integration.
- The Comtek Advanced Structures Ltd. ("Comtek") segment, which within exists two divisions dedicated to aircraft structural component repair services, and Avcorp Engineered Composites ("AEC") dedicated to design and manufacture of composite aerostructures.
- The Avcorp Composite Fabrication Inc. ("ACF") segment is dedicated to advanced composite aerostructures fabrication.

No operating segments have been aggregated to form the above reportable operating segments.

The Executive Management Committee monitors the operating results of its business units separately for the purpose of making decisions about resource allocation and performance assessment. Segment performance is evaluated based on profit or loss and is measured consistently with profit or loss in the condensed interim consolidated financial statements.

Transfer prices between operating segments are on an arm's length basis in a manner similar to transactions with third parties.

a) Sales to five major customers for the quarter ended June 30, 2016, which comprise several programs and contracts, accounted for approximately 80.8% (June 30, 2015: 76.8%) of sales.

	Three months ended June 30				Six months ended June 30			
	2016		2015		**2016**		2015	
	Revenue	**% of Total**	Revenue	% of Total	**Revenue**	**% of Total**	Revenue	% of Total
BAE Systems	**$4,998**	**11.3**	$4,609	22.6	**$4,998**	**6.3**	$6,902	19.2
Boeing	**20,631**	**46.6**	6,968	34.2	**40,478**	**50.9**	13,812	38.3
Bombardier	**4,207**	**9.5**	4,072	20.0	**8,701**	**10.9**	7,939	22.0
Fuji Heavy Industries	**3,200**	**7.2**	-	-	**6,527**	**8.2**	-	-
Lockheed Martin	**2,725**	**6.2**	-	-	**4,630**	**5.8**	-	-
Other	**8,485**	**19.2**	4,720	23.2	**14,259**	**17.9**	7,377	20.5
Total	**44,246**	**100.0**	20,369	100.0	**79,593**	**100.0**	36,030	100.0

b) The Company's sales are distributed amongst the following geographical locations:

	Three months ended June 30				Six months ended June 30			
	2016		2015		**2016**		2015	
	Revenue	**% of Total**	Revenue	% of Total	**Revenue**	**% of Total**	Revenue	% of Total
Canada	**$6,386**	**14.4**	$6,086	29.9	**$11,965**	**15.0**	$10,875	30.2
USA	**25,910**	**58.6**	8,849	43.4	**48,353**	**60.7**	16,508	45.8
Europe	**7,938**	**17.9**	4,791	23.5	**11,437**	**14.4**	7,549	20.9
Asia	**3,615**	**8.2**	341	1.7	**7,271**	**9.1**	668	1.9
Australia	**310**	**0.7**	228	1.1	**438**	**0.6**	339	0.9
Other	**87**	**0.2**	74	0.4	**129**	**0.2**	91	0.3
Total	**44,246**	**100.0**	20,369	100.0	**79,593**	**100.0**	36,030	100.0

c) 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 and in the United States.

The Company operates from two locations in Canada and one in the United States. Located in Delta, British Columbia, Avcorp Industries Inc., named as Avcorp Structures & Integration ("ASI"), is dedicated to metallic and composite aerostructures assembly and integration. Within Comtek Advanced Structures Ltd. ("Comtek"), located in Burlington, Ontario, exists two divisions dedicated to aircraft structural component repair services, and Avcorp Engineered Composites ("AEC") dedicated to design and manufacture of composite aerostructures. Located in Gardena, California, Avcorp Composite Fabrication Inc. ("ACF") is dedicated to advanced composite aerostructures fabrication.

Revenues, income (loss) and total assets are distributed by operating segment as noted in the tables below. Intercompany revenues and cost of sales are eliminated from the operating results presented.

	Three months ended June 30				Six months ended June 30			
	2016		2015		**2016**		2015	
	Revenue	**% of Total**	Revenue	% of Total	**Revenue**	**% of Total**	Revenue	% of Total
Avcorp Industries Inc.	**$34,067**	**77.0**	$16,051	78.8	**$61,285**	**77.0**	$28,042	77.8
Comtek Advanced Structures Ltd.	**5,840**	**13.2**	4,318	21.2	**11,473**	**14.4**	7,988	22.2
Avcorp Composite Fabrication Inc.	**34,324**	**77.6**	-	-	**64,127**	**80.6**	-	-
Adjustments and eliminations	**(29,985)**	**(67.8)**	-	-	**(57,292)**	**(72.0)**	-	-
Total	**44,246**	**100.0**	20,369	100.0	**79,593**	**100.0**	36,030	100.0

	Three months ended June 30				Six months ended June 30			
	2016		2015		**2016**		2015	
	Income (loss)	**% of Total**	Income (loss)	% of Total	**Income (loss)**	**% of Total**	Income (loss)	% of Total
Avcorp Industries Inc.	**$(9,318)**	**72.0**	$(1,369)	120.6	**$(25,895)**	**103.4**	$(4,560)	117.0
Comtek Advanced Structures Ltd.	**647**	**(5.0)**	234	(20.6)	**1,320**	**(5.3)**	664	(17.0)
Avcorp Composite Fabrication Inc.	**(4,280)**	**33.0**	-	-	**(467)**	**1.9**	-	-
Total	**(12,951)**	**100.0**	(1,135)	100.0	**(25,042)**	**100.0**	(3,896)	100.0

FOR THE PERIOD ENDED	**June 30, 2016**		December 31, 2015	
	Total Assets	**% of Total**	Total Assets	% of Total
Avcorp Industries Inc.	**$67,725**	**50.0**	$95,971	56.2
Comtek Advanced Structures Ltd.	**10,898**	**8.1**	9,231	5.4
Avcorp Composite Fabrication Inc.	**56,757**	**41.9**	65,544	38.4
Total	**135,380**	**100.0**	170,746	100.0

notes

AVCORP INDUSTRIES INC.

BOARD OF DIRECTORS AND OFFICERS

David Levi [1][2][3]
CHAIRMAN OF THE BOARD
Executive Chairman
GrowthWorks Capital Ltd.
Vancouver, British Columbia

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

Kees de Koning [3]
DIRECTOR
Nootdorp, The Netherlands

Elizabeth Otis [3]
DIRECTOR
Palm Springs, California

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

Ray Castelli [1]
DIRECTOR
Chief Executive Officer
Weatherhaven
West Vancouver, British Columbia

Peter George
DIRECTOR
Avcorp Group Chief Executive Officer
Lake Tapps, Washington

(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 Merlo
CORPORATE SECRETARY
Chief Financial Officer
Richmond, British Columbia

Ken McQueen
Vice President, Human Resources
New Westminster, British Columbia

Brent Collver
President
Comtek Advanced Structures Ltd.
Oakville, Ontario

Marty Jones
General Manager – Defence
Avcorp Composite Fabrication Inc.
Redondo Beach, California

Amandeep Kaler
General Manager
Avcorp Structures & Integration
Surrey, British Columbia

Jim Renaud
General Manager – Commercial
Avcorp Composite Fabrication Inc.
Huntington Beach, California

DIRECTORY

Legal Counsel

McMillan LLP
Barristers & Solicitors
Vancouver, British Columbia

Auditors

Ernst & Young LLP
Chartered Accountants
Vancouver, British Columbia

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