



Annual Report  
**2020**

[www.avcorp.com](http://www.avcorp.com)

**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, Lockheed Martin and Subaru Corporation. The Avcorp Group has more than 60 years of experience, over 500 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 aircraft operators with 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 March 19, 2021 and should be read in conjunction with the Company's consolidated financial statements and notes thereto for the year ended December 31, 2020.

### 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.

The Company currently operates 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. Comtek Advanced Structures Ltd., located in Burlington, Ontario, ("Comtek") is dedicated to aircraft structural component repair services, and 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.

### 2020 Highlights

- 2020 revenue was \$150,962,000 compared to \$164,770,000 in 2019. 2020 revenue decreased by \$13,808,000, in comparison to 2019. The decrease in revenue in 2020 was due to lower customer requirements because of the impact of the Coronavirus ("COVID-19") on the commercial aerospace sector and 737 MAX grounding.
- 2020 net loss was \$6,725,000 compared to net loss of \$9,316,000 in 2019. The net loss improved by \$2,591,000 in comparison to 2019 mainly due to higher gross profit and savings in administrative and general expenses. In addition, the 2020 net loss was supported by \$11,397,000 in government grants while 2019 was supported by a net claim settlement of \$17,974,000.
- 2020 cash flows from operating activities was \$9,125,000 compared to \$10,911,000 in 2019. 2020 cash flows from operating activities was supported by the Canada Emergency Wage Subsidies of \$4,765,000 and 2019 was supported by the net cash settlement of \$14,431,000 (USD \$10,810,000) from the agreement with Hitco Carbon Composites Inc., SGL Carbon, SGL, and SGL Carbon SE (the "SGL Parties") and a customer.
- In 2020, the Company repaid \$7,368,000 of bank indebtedness (December 31, 2019: \$18,010,000) and paid trade payables down to \$10,980,000 (December 31, 2019: \$23,201,000).
- March 2, 2020, the Company entered into an amendment to the standby credit facility ("2019 Panta Loan") with Panta Canada B.V. ("Panta") securing and drawing an additional \$2,686,000 (USD \$2,000,000).
- On April 28, 2020, the Company received a loan in the amount of USD \$4,123,000 to support Avcorp Composite Fabrication Inc ("ACF") from a U.S. Chartered Bank through the U.S. Small Business Administration Paycheck Protection Program. The Company has recognized a forgiveness of USD \$3,430,000 in 2020 as the company has satisfied the requirements of loan forgiveness.
- BAE Systems awarded the Company a contract for the assembly of the F-35 Carrier Variant Outboard Wing. The total awards are approximately \$87 million extending Avcorp's current long-term contract with BAE systems into 2022.

### Highlights Subsequent to Year-End

- The Company received Canada Emergency Wage Subsidies of \$712,000 in February and March 2021 and applied for an additional \$2,415,000.
- On February 25, 2021, the Company amended the Avcorp Composite Fabrication Inc.'s Gardena facility lease agreement effective January 1, 2021 to vacate certain buildings and negotiated new lease terms.
- On March 12, 2021, the Company entered into a multiparty amended and restated Accommodation Agreement with each of a customer, and Panta Canada B.V. whereby, inter alia;
  - Panta Canada B.V. has agreed to provide a USD \$10,000,000 non-revolving standby loan facility and a USD \$3,000,000 equipment loan for an aggregate availability of USD \$13,000,000; and
  - The elimination of unamortized cash advance, mutual release and forgiveness of certain historic and future guarantee fees payable to the customer. As at December 31, 2020, the guarantee fee is \$8,178,000 (USD \$6,423,000), the customer advance is \$5,911,000 (USD \$4,643,000) and the legal claim is \$7,130,000 (USD \$5,600,000).
- On March 15, 2021, the Company received a USD \$2,000,000 second wave Small Business Administration Paycheck Protection Program Loan.

- On March 19, 2021, the Company approved the grant of an aggregate of 17,350,000 incentive stock options under the Company's 2007 Stock Option Plan to Directors, Officers and Employees. The options will have a five year term and will have an exercise price determined by the market price effective the close of markets March 22,2021.

## Financial Overview

### Three-Year Results

The following table provides selected financial information for the three years to December 31, 2020.

| <b>THREE-YEAR RESULTS</b>   |                         |                         |             |
|---|-------------------------|-------------------------|-------------|
| <i>(prepared in accordance with IFRS, expressed in thousands of Canadian dollars except per share amounts)</i>  |                         |                         |             |
| <b>FOR THE YEAR ENDED DECEMBER 31</b>   | <b>2020<sup>3</sup></b> | <b>2019<sup>3</sup></b> | <b>2018</b> |
| <b>OPERATIONS</b>   |                         |                         |             |
| Revenue   | <b>\$150,962</b>        | \$164,770               | \$170,710   |
| EBITDA <sup>1</sup>   | <b>19,492</b>           | 10,813                  | 35,338      |
| Operating income (loss)   | <b>2,371</b>            | (1,124)                 | 26,917      |
| Net (loss) income   | <b>(6,725)</b>          | (9,316)                 | 20,373      |
| Basic and diluted (loss) income per share   | <b>(0.02)</b>           | (0.03)                  | 0.06        |
| <b>FINANCIAL POSITION</b>   |                         |                         |             |
| Capital expenditures  | <b>1,769</b>            | 904                     | 1,809       |
| Total assets  | <b>121,538</b>          | 128,140                 | 116,068     |
| Bank indebtedness and term debt   | <b>112,744</b>          | 115,086                 | 94,150      |
| Shareholders' (deficit)   | <b>(49,140)</b>         | (43,475)                | (36,144)    |
| Net book value per share <sup>2</sup>   | <b>(0.13)</b>           | (0.12)                  | (0.10)      |
| Ratio: current assets/current liabilities   | <b>0.47</b>             | 0.47                    | 0.50        |
| Shares outstanding at period end  | <b>368,118,620</b>      | 368,118,620             | 368,118,620 |
| <ol style="list-style-type: none"> <li>EBITDA = earnings before interest, taxes, depreciation and amortization. This is not a recognized term under International Financial Reporting Standards ("IFRS"), refer to page 8.</li> <li>Net book value per share is not a recognized term under IFRS, refer to page 12.</li> <li>Excludes operating lease expense, recognizes right of use asset and lease liability as a result of change to lease accounting policy under IFRS 16. IFRS 16 was adopted on a modified retrospective basis, and therefore comparative figures have not been restated</li> </ol> |                         |                         |             |

For the year ended December 31, 2020, the Avcorp Group's revenue was \$150,962,000 compared to \$164,770,000 in 2019 and \$170,710,000 in 2018. The decrease in revenue in 2020 compared to 2019 was mainly attributed to lower deliveries caused by lower customer requirements due to the impact of Coronavirus ("COVID-19") on the commercial aerospace sector, and the decrease from 2018 to 2019 was due to the 737 MAX grounding.

The 2020 \$2,371,000 operating income contains \$308,000 provision of onerous contracts and \$11,642,000 government grant and other income. The decrease in the operating loss in 2020 compared to 2019 is due to continued operational improvement, cost reduction initiatives, growth in defense program revenue, and the recognition of variable consideration on the contract termination of convenience. The 2019 \$1,124,000 operating loss contains \$1,665,000 amortization of onerous contract and \$17,325,000 net claim settlement gain and other loss. The 2018 \$26,917,000 operating income was supported by a \$41,470,000 net contract modification gain, a \$4,617,000 amortization of an unfavourable contracts liability, a \$9,115,000 amortization of onerous contracts provision, and a \$5,421,000 loss on net claim position.

Capital expenditures during the three-year period presented have been limited to upgrading and sustaining manufacturing equipment and capabilities, new program introductions, and information technology assets.

Bank indebtedness and term debt has decreased by \$2,342,000 in 2020 compared to 2019 due to the repayment of 7,368,000 in bank indebtedness and foreign exchange translation gain offset by the Panta Loan draw of \$6,924,000. Bank indebtedness and term debt increased by \$20,936,000 in 2019 over 2018 largely due to the transition to IFRS 16 and recognition of lease liabilities included in term debt.

### Impact of COVID-19

In March 2020, the World Health Organization (“WHO”) declared coronavirus (“COVID-19”) a global pandemic. Governments worldwide enacted emergency measures including travel bans, social distancing measures and mandatory quarantine requirements. The measures have negatively impacted the global economy and adversely impacted the aviation industry worldwide particularly in the commercial airline industry. The significant decrease in air travel resulting from the COVID-19 pandemic is adversely affecting Avcorp’s customers and their demand for the Company’s products. The situation remains dynamic and the ultimate duration and magnitude of the impact on the economy and the financial effect on the Company remains unknown at this time.

The Company has been closely monitoring and actively implementing and updating its response to the evolving COVID-19 pandemic and its impacts on employees and operations. Avcorp has implemented additional safety, sanitization and physical distancing procedures, including remote work schedules where possible and ceased all non-essential business travel. The Company has formed a committee composed of the senior leadership team in the organization to monitor the evolution of the pandemic, to evaluate the measures being put in place by local, provincial/state and national governments and the resulting impacts on the Company and to implement necessary contingency plans as the current situation continues to evolve, with a focus on protecting our employees’ health and safety; supporting customers; and ensuring that the Company can successfully navigate through this global crisis. The Company actions are closely aligned with both the health and safety mandates that have been announced by the local or provincial/state health authorities.

In addition, the company has implemented measures to align its cost structure and maximize cash preservation during the current market conditions, including headcount reductions to ensure that it emerges from the current crisis on solid footing, and expenses were reduced in various areas. The Company applied and received the Canada Emergency Wage Subsidy (“CEWS”) for its Canadian operations and support as part of Paycheck Protection Plan for its US operations. On a consolidated basis, the COVID-19 pandemic had a material negative impact on free cash flow for the full year due to lower revenue.

### Quarterly Results

The following table provides selected quarterly consolidated financial information for the eight most recent fiscal quarters to December 31, 2020 prepared in accordance with IAS 34 – Interim Financial Reporting (“IAS 34”) as issued by the International Accounting Standards Board (“IASB”).

#### QUARTERLY RESULTS

(prepared in accordance with IFRS, expressed in thousands of Canadian dollars except per share amount)

|                               | 2020            |          |          |          | 2019     |          |          |          |
|-------------------------------|-----------------|----------|----------|----------|----------|----------|----------|----------|
|                               | Dec 31          | Sep 30   | Jun 30   | Mar 31   | Dec 31   | Sep 30   | Jun 30   | Mar 31   |
| Revenue                       | <b>\$44,742</b> | \$33,769 | \$32,246 | \$40,205 | \$38,309 | \$37,437 | \$46,799 | \$42,225 |
| Operating (loss) income       | <b>8,477</b>    | (326)    | (1,080)  | (4,700)  | (8,114)  | (5,164)  | (2,903)  | 15,057   |
| EBITDA <sup>1</sup>           | <b>17,895</b>   | 3,623    | 2,937    | (4,963)  | (4,455)  | (2,901)  | 172      | 17,997   |
| Net (loss) income             | <b>6,546</b>    | (1,263)  | (1,594)  | (10,414) | (10,846) | (7,511)  | (4,568)  | 13,609   |
| EBITDA per share <sup>1</sup> |                 |          |          |          |          |          |          |          |
| Basic                         | <b>0.05</b>     | 0.01     | 0.01     | (0.01)   | (0.01)   | (0.01)   | 0.00     | 0.05     |
| Diluted                       | <b>0.05</b>     | 0.01     | 0.01     | (0.01)   | (0.01)   | (0.01)   | 0.00     | 0.05     |
| Net income (loss) per share   |                 |          |          |          |          |          |          |          |
| Basic                         | <b>0.02</b>     | (0.00)   | (0.00)   | (0.03)   | (0.03)   | (0.02)   | (0.01)   | 0.04     |
| Diluted                       | <b>0.02</b>     | (0.00)   | (0.00)   | (0.03)   | (0.03)   | (0.02)   | (0.01)   | 0.04     |
| Long-term debt                | <b>19,168</b>   | 24,801   | 25,240   | 35,358   | 26,848   | 22,018   | 22,496   | 22,229   |

1. EBITDA = earnings before interest, taxes, depreciation and amortization. This is not a recognized term under International Financial Reporting Standards (“IFRS”), refer to page 8.

2020 revenue was \$150,962,000 compared to \$164,770,000 in 2019. 2020 revenue decreased by \$13,808,000, in comparison to 2019. The decrease in revenue in 2020 was attributed to lower deliveries caused by lower customer requirements due to the Coronavirus (“COVID-19”) on commercial aerospace sector and 737 MAX grounding. For the quarter ended December 31, 2020, the Avcorp Group’s revenue was \$44,742,000 compared to \$38,309,000 in 2019. The Company recognized an estimate of variable consideration in the current quarter related to a contract termination of convenience. Variable consideration is estimated as the most likely amount to which we expect to be entitled and is recognized to the extent it is probable that a significant reversal will not occur when the uncertainty associated with the variable consideration is subsequently resolved. We were also adversely impacted in the second to fourth quarter by lower customer requirements for certain commercial programs due to COVID-19.

For the quarter ended December 31, 2020, the Avcorp Group recorded income from operations of \$8,477,000 (December 31, 2019: \$8,114,000 loss). Operating results in the fourth quarter of 2020 improved in comparison to 2019 by \$16,591,000, because the fourth quarter 2020 operating income included government grants and other income of \$7,646,000 (December 31, 2019: other loss of \$630,000). In addition, the Company recognized an estimate of variable consideration for the contract termination of convenience. Included in the government grant income in the quarter ended December 31, 2020 is the forgiveness of \$4,601,000 (USD \$3,430,000) as the company has satisfied the requirements of loan forgiveness. The forgiveness application was submitted in March 2021 and the forgiveness amount may change once reviewed and confirmed by our U.S. Chartered Bank and the Small Business Administration. The improvement in operating result is due to higher revenue, continued operational improvement and cost reduction initiatives.

### 2020 and 2019 Results Overview

During the year ended December 31, 2020 Avcorp Group revenues totaled \$150,962,000 compared with \$164,770,000 for the previous year.

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.

**Gardena facility** commercial aerospace contracts have generated \$18,382,000 in revenue (December 31, 2019: \$31,256,000). These contracts, whose production occurs in the Gardena facility, support customer production of commercial aircraft and have decreased from 2019 as customer requirements have decreased due to the impact of COVID-19. The Gardena facility defence aerospace contracts generated \$29,315,000 of revenue during the year ended December 31, 2020 for ACF (December 31, 2019: \$34,960,000). Defence revenue in 2021 is expected to decline further compared to 2020 and 2019, as we continue to fulfill all delivery requirements on certain purchase orders extending to the second quarter of 2021. The Company is actively pursuing follow-on purchase orders and bidding for new work.

**Burlington facility** revenues have decreased by \$3,946,000 during the current year relative to the year ended December 31, 2019 due to the impact of COVID-19. There was a decline in customer delivery requirements and repairs services.

**Delta facility** revenues, for all programs generated by production contracts, have increased by \$8,657,000 during the current year relative to the year ended December 31, 2019. Delta revenues from the production and delivery of business and commercial jet programs has decreased by approximately \$22,438,000 in 2020 relative to 2019 primarily due to COVID-19 and 737 MAX grounding, while defence programs' revenues increased by \$31,095,000 as it was supported by the inclusion of variable consideration on a termination of convenience and the growth in the F-35 programs.

Avcorp Group continues to actively pursue production contracts on aerospace programs throughout North America, Asia, and Europe both in the commercial and defence aerospace sectors. These production contracts consist of complex metal bond and multi-material structural assemblies that complement Avcorp's capability as a strategic integrated supplier within the aerospace industry.

For the year ended December 31, 2020, the **Avcorp Group** recorded income from operations totaling \$2,371,000 from \$150,962,000 revenue, as compared to \$1,124,000 operating loss from \$164,770,000 revenue for the previous year. The 2019 operating loss contains \$1,665,000 amortization of onerous contract and \$17,325,000 net claim settlement gain and other loss. The 2020 operating income contains \$308,000 provision of onerous contracts, \$11,642,000 government grant and other income, and the estimate of variable consideration on the contract termination of convenience. The operating loss improvement was also due to continued operational improvement and cost reduction initiatives, growth in revenue related to defence programs, and offset by a decrease in revenue related to commercial programs as a result of COVID-19.

Although recent customer contract awards in Canadian operations will continue to increase facility utilization, there remains unutilized plant capacity within the Company's Delta, British Columbia facility, and within the Gardena, California facility due to the transition out of certain loss-making production contracts and the reduction in customer requirements due to COVID-19 and the 737 MAX grounding. The Company has expensed \$8,346,000 of overhead costs during the year as compared to \$7,004,000 in prior year 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 these facilities would benefit Company profitability via a contribution to the recovery of fixed overhead expenditures. Avcorp is engaged with aerospace OEM's as well as industry tier 1 suppliers in North America, Asia and Europe in collaborative production initiatives that support the Company's composite manufacturing capabilities, further leveraging existing production capacity and investments.

During the year ended December 31, 2020, cash flows from operating activities was \$9,125,000 compared with \$10,911,000 in 2019. 2020 cash flows from operating activities was supported by the Canada Emergency Wage Subsidies of \$4,765,000 and 2019 was supported by the net cash settlement of \$14,431,000 (USD \$10,810,000) from the agreement with Hitco Carbon Composites Inc., SGL Carbon, SGL, and SGL Carbon SE (the "SGL Parties") and a customer.

As at December 31, 2020, the Company had \$7,044,000 cash on hand (December 31, 2019: \$4,316,000) and had utilized \$76,439,000 of its operating line of credit (December 31, 2019: \$84,661,000). The balance of the net loss and related adjustments on modification of bank indebtedness as a result of executing an amending agreement in 2019 was \$269,000 as at December 31, 2020 (December 31, 2019 \$809,000). The Company has a working capital deficit of \$77,780,000 as at December 31, 2020 which has increased from the December 31, 2019 \$71,561,000 deficit. Working capital is defined as the difference between current assets and current liabilities. However, the Company's accounts and other receivables, contract assets, and inventories net of accounts payable, amount to a \$33,174,000 surplus as at December 31, 2020 (December 31, 2019: \$18,542,000 surplus). The Company's accumulated deficit as at December 31, 2020 is \$148,919,000 (December 31, 2019: \$142,194,000).

## Revenue

For the year ended December 31, 2020 revenues totaled \$150,962,000, a \$13,808,000 decrease in revenues relative to 2019 (December 31, 2019; \$164,770,000).

### Operating segment revenues are as follows:

#### REVENUE DISTRIBUTION

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

#### FOR THE YEAR ENDED DECEMBER 31

|   | 2020     |            | 2019     |            |
|---|----------|------------|----------|------------|
|   | Revenue  | % of Total | Revenue  | % of Total |
| Avcorp Structures & Integration. (ASI)  | \$86,756 | 57.5       | \$78,099 | 47.4       |
| Comtek Advanced Structures Ltd. (AEC)   | 16,509   | 10.9       | 20,455   | 12.4       |
| Avcorp Composite Fabrication Inc. (ACF) | 47,697   | 31.6       | 66,216   | 40.2       |
| Total                                   | 150,962  | 100.0      | 164,770  | 100.0      |

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.

**Delta facility** revenues 2020 totaled \$86,756,000 (December 31, 2019: \$78,099,000).

The Delta facility continues to actively pursue production contracts on aerospace programs throughout North America, Asia, and Europe both in the commercial and defence aerospace sectors. These production contracts consist of complex metal bond and multi-material structural assemblies that complement Avcorp's capability as a strategic integrated supplier within the aerospace industry.

Delta facility commercial aircraft programs production revenues have decreased by \$22,438,000 of which established commercial aircraft production contract revenues have contributed \$18,275,000 of this revenue decrease in 2020 relative to 2019. The Delta facility had lower customer delivery requirements due to COVID-19 and the 737 Max grounding. This was more than offset with production for defence programs which increased by \$31,095,000 in 2020 relative to 2019. The defence revenue was supported by an estimate of variable consideration related to the termination of convenience of certain defence contracts and continued growth of the F-35 program.

**Burlington facility** revenues for 2020 totaled \$16,509,000 (December 31, 2019: \$20,455,000).

The Burlington facility is dedicated to aircraft structural component repair services, and design and manufacture of composite aerostructures. They service customers from around the world.

The Burlington facility revenues decreased by \$3,946,000 during the current year relative to the year ended December 31, 2019. The impact of COVID-19 has contributed significantly to a reduction in customer demand and deliveries during 2020.

**Gardena facility** revenues for 2020 totaled \$47,697,000 (December 31, 2019: \$66,216,000).

The Gardena facility provides a unique aerostructures composite capability to the Avcorp Group's existing metal fabrication and integrated assembly business through broadening the product range and strengthening Avcorp's composite capabilities. Advanced composite fabrication capabilities enhance Avcorp Group's ability to participate in large aerospace assembly programs which combine mixed material components.

Year ended December 31, 2020 revenues arising from the assignment by customers of commercial aerospace contracts to Avcorp Industries Inc. have generated \$18,382,000 in production revenue (December 31, 2019: \$31,256,000). The decline in Commercial revenues resulted from a decline in customer requirements due largely to the impact of COVID-19. These contracts support customer production of commercial aircraft with manufacturing of the composite parts occurring in Avcorp Group's Gardena facility. The Gardena facility defence aerospace contracts generated \$29,316,000 of production revenue during the year ended December 31, 2020 for ACF (December 31, 2019: \$34,960,000) with the impact of COVID-19 attributing to this decline in revenue. In addition, Defence revenue in 2021 is expected to decline further compared to 2020 and 2019, as we continue to fulfill all delivery requirements on certain purchase orders extending to the second quarter of 2021. The Company is actively pursuing follow-on purchase orders and bidding for new work.

Deliveries and quality performance as at December 31, 2020 for Avcorp 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.

## Revenues from Avcorp Group customers are as follows:

## REVENUE DISTRIBUTION

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

## FOR THE YEAR ENDED DECEMBER 31

|                     | 2020     |            | 2019     |            |
|---------------------|----------|------------|----------|------------|
|                     | Revenue  | % of Total | Revenue  | % of Total |
| BAE Systems         | \$31,332 | 20.8       | \$18,181 | 11.0       |
| Boeing <sup>1</sup> | 48,237   | 31.9       | 50,351   | 30.6       |
| Bombardier          | 12,998   | 8.6        | 18,535   | 11.2       |
| Lockheed Martin     | 30,444   | 20.2       | 35,812   | 21.8       |
| Subaru Corporation  | 16,311   | 10.8       | 28,306   | 17.2       |
| Other               | 11,640   | 7.7        | 13,585   | 8.2        |
| Total               | 150,962  | 100.0      | 164,770  | 100.0      |

1. Includes Boeing program partner revenue consisting of industry tier-one suppliers to Boeing.

The Avcorp Delta BC facility is the single source supplier for the F-35 CV-OBW assembly under contract with **BAE Systems ("BAE")** 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 characteristics. The CV-OBW is regarded as one of the more complex assemblies that the Canadian aerospace industry contributes to the F-35 program. Production demand for the F-35 CV-OBW increased by \$13,151,000 in 2020 relative to 2019. Production contracts have been secured through to end of Q1 2022, with discussions underway with the customer to secure constant production through to the first quarter of 2025. 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 Lot fourteen; and are in discussions with the customer for production under Lot fifteen through seventeen.

Avcorp's Gardena California facility provides content for all three models of the F-35 fighter aircraft. Fabricated components include; wing skins, nacelles, access panels, and a strap component that serves as a structural backbone to the aircraft. Avcorp fabricates these complex structures through a combination of both automated robotic fiber placement and hand laid graphic fabric methods. Avcorp is under a multi-year contract with Lockheed Martin Corporation, who release order quantity and schedule requirements that coincide with their fiscal year. The current period of performance extends through to the second quarter of 2021. Avcorp is in discussion with Lockheed Martin pursuing follow-on contract, assuming acceptable quality and delivery performance. Total revenues for the defence program totaled \$27,588,000 for the year ended December 31, 2020 (December 2019 \$33,469,000).

Shipments of large complex metal assemblies and fabricated parts and components out of the Delta facility to **Boeing Commercial Airplane Group ("Boeing")**, primarily for the 737 commercial jet program, decreased by 49% in 2020 relative to 2019, primarily as a result of Boeing 737 MAX grounding, decreased customer demand, and the shutdown of Boeing facilities due to COVID-19. Total production deliveries generated for the Company from various Boeing Commercial aircraft programs amounted to \$23,728,000 for the year ended December 31, 2020 (December 31, 2019: \$41,930,000). The Company also delivers components to **Boeing Defence, Space & Security ("Boeing DSS")** totaling \$2,718,000, a decrease in production revenues recorded for the same period in 2019 (December 31, 2019: \$6,849,000) as a result of the planned shutdown of Boeing facilities due to COVID-19.

Production deliveries for **Bombardier Aerospace ("Bombardier")** programs decreased by 32% during the current year relative to the year ended December 31, 2019. Shipments of large assemblies for the CL605 business jet program decreased by \$2,589,000 during the current year as demand for these products decreased relative to 2019, partially as a result of the COVID-19 impact; while concurrently the Company experienced a \$3,432,000 decrease in its deliveries of composite panels and related products to Bombardier. Avcorp Group's primary source of revenues from Bombardier in 2021 will continue to be from components for the CL605 and Global Express business jets.

Avcorp's deliveries to **Subaru Corporation ("Subaru")** of large complex composite structural components which are integrated into the center wing box in support of the Boeing 787 commercial jet program totaled \$16,311,000 for the current year (December 31, 2019: \$28,306,000); a decrease in customer demand due to COVID-19. This is a significant commercial production contract being manufactured in the Gardena facility. This long-term agreement represents an important relationship with a long-standing industry tier one supplier.

Composite aircraft structure repair revenues out of Comtek decreased by 29% relative to revenues in the previous year due primarily to COVID-19. The Avcorp Group also supplies Canadian aircraft retrofit programs out of its Delta facility, and large composite structures in support of various US defence programs out of its Gardena facility, whose revenues decreased relative to 2019. These **Other** revenues are of significant importance to the Group's operations as they generated \$11,640,000 in revenue during the year ended December 31, 2020 (December 31, 2019: \$13,585,000).



**Defence program revenues** for the Avcorp Group in 2020 totaled \$87,783,000 (December 31, 2019: \$62,333,000); 58.1% of total production sales (December 31, 2019: 37.8%). **Commercial program sales** provided a lower portion of the Company's sales in 2020 (December 31, 2020: 41.9%; December 31, 2019: 62.2%) amounting to \$63,179,000 for 2020 and \$102,437,000 for 2019. The Group continues to move forward with its revenue diversification between commercial and defence aerospace programs.

### Gross Profit

Gross profit (revenue less cost of sales) for the year ended December 31, 2020 was positive 5.5% of revenue compared to positive 2.3% of revenue for the year ended December 31, 2019.

The Gardena facility gross margin for the current year was negative \$5,223,000 (December 31, 2019: \$1,650,000 negative gross margin). The Gardena facility gross margin decreased by \$3,573,000 in 2020 relative to 2019 mainly attributable to the decrease in revenue during the year due to COVID-19. The Gardena site was also challenged with high absenteeism related to COVID-19 and equipment down time.

The Delta facility gross margin for the current year was positive \$10,888,000 (December 31, 2019: \$1,893,000 positive gross margin). 2020 Delta facility gross margin increased by \$8,995,000 from the 2019 gross margin. The improvement was attributed to the inclusion of an estimate of variable consideration on a contract termination of convenience. There was continued operational efficiencies, cost reduction initiatives and changes in program revenue mix.

Burlington production contracts produced a positive gross margin for the year ended December 31, 2020 of \$2,568,000 as compared to a positive gross margin of \$3,545,000 for 2019 attributable to the decrease in revenue due to COVID-19.

Although recent customer contract awards in Canadian operations will continue to increase facility utilization, there remains unutilized plant capacity within the Company's Delta, British Columbia facility and the Gardena, California facility due to the transition out of certain loss-making production contracts. The Company has expensed \$8,346,000 of overhead costs during the year as compared to \$7,004,000 for December 31, 2019 in respect of unutilized plant capacity.

### Administration and General Expenses

As a percentage of revenue, administration and general expenses decreased to 11.1% for the year ended December 31, 2020 from 13.0% for the year ended December 31, 2019. In absolute terms, administration and general costs decreased by \$4,750,000 during the current year relative to the previous year. Management have taken steps to manage expenses due to COVID-19 by reducing headcount, and saving on various other expenses during the year.

### Foreign Exchange Gain or Loss

Avcorp Group recorded a \$364,000 foreign exchange loss during the year ended December 31, 2020 (December 31, 2019: \$843,000 gain) as a result of holding US dollar-denominated cash, receivables, payables and debt.

### 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.

EBITDA was positive \$19,492,000 for the year ended December 31, 2020 compared to EBITDA of positive \$10,813,000 for the year ended December 31, 2019. The EBITDA in 2020 was supported by \$6,796,000 of Canadian Emergency Wage Subsidies and \$4,601,000 of recognized loan forgiveness on the U.S. Small Business Administration's Paycheck Protection Program. In addition, the 2020 EBITA was supported by the estimate of variable consideration related to the contract termination of convenience. The EBITDA in 2019 was supported by the net gain on claims of \$17,974,000. In addition to these specific events the increase EBITDA was due to continued operational improvements, cost reduction initiatives, and change in program revenue product mix; offset by the adverse impact of COVID-19.

#### EBITDA<sup>1</sup>

(expressed in thousands of Canadian dollars)

#### FOR THE YEAR ENDED DECEMBER 31

|   | 2020             | 2019      | 2018     |
|---|------------------|-----------|----------|
| Income (loss) for the year                        | <b>\$(6,725)</b> | \$(9,316) | \$20,373 |
| Interest expense and financing charges            | <b>7,727</b>     | 8,941     | 5,813    |
| Income tax expense                                | -                | -         | -        |
| Depreciation                                      | <b>8,338</b>     | 8,218     | 4,482    |
| Amortization of development costs and intangibles | <b>10,152</b>    | 2,970     | 4,670    |
|   | <b>19,492</b>    | 10,813    | 35,338   |

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 year ended December 31, 2020 were \$7,605,000, which is net of \$122,000 interest income as compared to \$8,924,000 expense, net of \$17,000 interest income for the year ended December 31, 2019. Interest expenditures have decreased during the current year relative to the previous year mainly due to repayment of bank indebtedness.

### Income Taxes

Avcorp Group has not incurred a tax expense during the year ended December 31, 2020 (December 31, 2019: \$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 year ended December 31, 2020 was \$6,725,000 compared to a loss of \$9,316,000 for the year ended December 31, 2019. The December 31, 2020 net loss contains \$11,642,000 of other income and the recognition of an estimate of variable consideration on the termination of convenience.

The Canada Emergency Wage Subsidy from the Canadian Government for the year ended December 31, 2020 of \$6,796,000 were included in other income, \$657,000 was capitalized as deferred income which would be recognized as other income when the related inventory are sold by the Company. There are no unfulfilled conditions or other contingencies attaching to these grants.

On April 28, 2020, the Company received a loan in the amount of USD \$4,123,000 from a U.S. Chartered Bank through the U.S. Small Business Administration Paycheck Protection Program ("PPP Loan"). The loan has a term of 2 years. The loan bears interest at a fixed rate of 1% per annum. The Company has recognized an estimated forgiveness of \$4,601,000 (USD \$3,430,000) in 2020 as the Company has satisfied the requirements of loan forgiveness. On March 9, 2021, the Company submitted the application for review to receive this forgiveness.

On a comparative basis, the 2019 \$9,316,000 net loss contains, a \$1,665,000 amortization of the onerous contracts provision and a \$17,325,000 net claim settlement and other loss.

On January 25, 2019, the Company and its subsidiary Avcorp Composite Fabrication Inc. (the "Avcorp Parties") entered into an agreement with HITCO Carbon Composites, Inc., SGL Carbon, LLC, and SGL Carbon SE (the "SGL parties") and a customer to settle all claims related to alleged deficiencies in HITCO's non-destructive inspection processes and other business matters including a lease renewal and collection of a previously provisioned account receivable in exchange for gross consideration of USD \$12,000,000 from the SGL parties to Avcorp and mutual releases among the Avcorp Parties, SGL Parties and a customer related to the acquisition. The net cash payment received totaled USD \$10,810,000. The net claim settlement resulted in a gain of \$19,759,000.

The reduction in net loss for 2020 relative to 2019 was also attributed to continued improvements in cost saving initiatives to mitigate the impact of COVID-19, improved operational improvements, and change in program revenue product mix.

### Capital Resources

On November 15, 2019, the Company entered into a loan agreement to expand its operating credit facility with a Canadian Chartered Bank. This loan agreement amends, re-states and replaces the loan agreements entered into on September 27, 2012 and subsequently on May 26, 2017. The loan agreement extends the maturity to June 30, 2021. The Company is currently in discussions to extend the maturity date.

- Maximum availability under the Loan agreement cannot exceed USD \$68,000,000 less USD \$2,300,000 until June 30, 2021. USD \$45,000,000 borrowing capacity under the loan agreement is supported by a customer of the Company (the "Guarantor") by way of a guarantee (the "Guarantee"). On November 15, 2019, Panta Holdings B.V., the holding company of Panta Canada B.V. which is Avcorp's majority shareholder, entered into a guarantee agreement with the Guarantor. Pursuant to the guarantee agreement, Panta Holdings B.V. provided guarantee to the Guarantor in the maximum payment of USD \$10,000,000 if the bank draws on the Guarantee in whole or in part.
- Interest rate for advances made up to the maximum of the allowable borrowing base of USD \$23,000,000 revolving loan less USD \$2,300,000:
  - Royal Bank Prime ("RBP") plus 1.50% per annum
  - Royal Bank US Base Rate ("RBUSBR") plus 1.50% per annum
  - Banker's Acceptance ("BA") Equivalent Rate plus 3.00% per annum
  - LIBOR Rate plus 3.00% per annum
- Interest rate for advances made on the additional USD \$45,000,000 borrowing capacity up to USD \$68,000,000.
  - RBP plus 0.00% per annum
  - RBUSBR plus 0.00% per annum
  - BA Equivalent Rate plus 0.875% per annum
  - LIBOR Rate plus 0.875% per annum

- Pursuant to the terms of the amending loan agreement, the Company is required to meet certain financial covenants beginning in Q1 2020. In the event that the Company fails to meet the covenants, Panta Holdings B.V. and Panta Canada B.V. shall be entitled to make cash injections for a fiscal quarter by way of loan or equity investment in Avcorp. Such injections will be considered a positive addition to the calculation of the financial metrics for the purposes of determining compliance with the covenants. In addition, the Company will have a cure period measured cumulatively for the failed quarter and the subsequent quarter. There is uncertainty as to the ability of the Company to meet its financial covenants without the additional financial support from Panta Holdings B.V. and Panta Canada B.V.
  - The Company cannot provide assurance it will be able to meet the financial metrics going forward and may seek a waiver or amendment to the loan agreement if an event of default is to occur.
- On February 6, 2020, the Company entered into an amendment to its existing loan agreement with a Canadian Chartered Bank whereby the following amendments were made:
  - The threshold of the financial covenants for the first and second fiscal quarters for the 2020 fiscal year were amended in favor of the Company.
- On April 27, 2020 through to October 30, 2020, the Company entered into multiple extensions to the amendment above to its existing loan agreement with a Canadian Chartered Bank whereby the following amendment was made:
  - The maximum availability under the Loan agreement cannot exceed USD \$68,000,000 less USD \$1,000,000 until December 31, 2020 and thereafter less USD \$2,300,000.

On November 15, 2019, the Company entered into a standby credit facility agreement ("2019 Panta Loan") with Panta Canada B.V. which amended and re-stated the 2018 Panta Loan, as well as securing an additional \$4,566,000 (USD \$3,500,000). As at December 31, 2019, the company had drawn \$328,000 (USD \$250,000) on this 2019 Panta Loan. The Company drew the remaining available amount in January 2020 of \$4,238,000 (USD \$3,250,000). On March 2, 2020, the Company entered into an amendment to the standby credit facility ("2019 Panta Loan") securing an additional and drawing \$2,686,000 (USD \$2,000,000). As at the date of this report the company is able to draw up to an additional \$Nil on the standby credit facility.

On March 12, 2021, the Company entered into a multiparty amended and restated Accommodation Agreement with each of a customer, and Panta Canada B.V. whereby, inter alia;

- Panta Canada B.V. has agreed to provide a USD \$10,000,000 non-revolving standby loan facility and a USD \$3,000,000 equipment loan for an aggregate availability of USD \$13,000,000; and
- The elimination of unamortized cash advance, mutual release and forgiveness of certain historic and future guarantee fees payable to the customer. As at December 31, 2020, the guarantee fee is \$8,178,000 (USD \$6,423,000), the customer advance is \$5,911,000 (USD \$4,643,000) and the legal claim is \$7,130,000 (USD \$5,600,000).

On April 28, 2020, the Company received a loan in the amount of USD \$4,123,000 to support Avcorp Composite Fabrication Inc ("ACF") from a U.S. Chartered Bank through the U.S. Small Business Administration Paycheck Protection Program. The company has recognized a forgiveness of USD \$3,430,000 in 2020 as the company has satisfied the requirements of loan forgiveness. On March 9, 2021, the company submitted the application for review to receive this forgiveness. The remaining loan balance has a term of 2 years and bears interest at a fixed rate of 1% per annum. Subsequent to year end, the Company has applied for and received a second wave Paycheck Protection Program loan for an additional USD \$2,000,000 on March 15, 2021.

The Company received the Canada Emergency Wage Subsidy in the amount of \$4,765,000 in 2020. The Company has received \$712,000 and applied for an additional \$2,415,000 subsequent to year end and will continue to apply for additional government subsidies when eligible.

On March 15, 2021, the Company received a USD \$2,000,000 second wave Small Business Administration Paycheck Protection Program Loan.

### Cash Flows from Operating Activities

Cash flows from operating activities, before consideration of changes in non-cash working capital, generated \$13,022,000 during the year ended December 31, 2020 as compared to generating \$2,631,000 cash during the year ended December 31, 2019. The company received \$4,765,000 from the Canada Emergency Wage Subsidy in 2020 and a net cash settlement of \$14,431,000 (USD \$10,810,000) from the agreement with the SGL Parties and a customer in 2019.

Non-cash operating assets and liabilities utilized \$3,897,000 of cash during the current year, compared to generating \$8,280,000 of cash during the previous year; primarily due to timing in payments to suppliers, partially offset by increase in payments received from customers.

Avcorp Group continues to closely monitor accounts receivable and accounts payables, and to work with its customers and suppliers in order to ensure cash is collected on a timely basis and payment terms that can meet operational needs.

### Cash Flows from Investing Activities

During the year ended December 31, 2020, the Avcorp Group purchased equipment totalling \$1,769,000 compared with \$904,000 during the year ended December 31, 2019. Avcorp Group continues to minimize its capital expenditures in order to conserve cash, with only operation critical expenditures being made.

During 2020 and 2019, the Company commenced the new program introduction process in support of the recently awarded production contracts. The start-up of new production contracts requires significant investments in hard and soft tooling. Such tooling investments amounted to \$3,929,000 for the year ended December 31, 2020 (December 31, 2019: \$4,116,000).

### Cash Flows from Financing Activities

Avcorp Group finances working capital through a combination of government subsidies, shareholder loans, bank debt and equity financings.

Cash flows from financing activities utilized \$740,000 of cash during the current year compared with utilizing \$3,610,000 of cash in 2019.

The Company's operating line was \$76,439,000 drawn as at December 31, 2020 (December 31, 2019: \$84,661,000). The Company drew \$653,000 in cash during the year (December 31, 2019: \$20,844,000 was drawn) and repaid \$7,368,000 in cash during the year (December 31, 2019: \$18,010,000 was repaid).

Repayment of term debt during the current year amounted to \$2,524,000 (December 31, 2019: \$2,591,000); which was used to fund equipment, facility leases, and development costs and tooling.

Proceeds from term debt during the current year amounted to \$12,453,000 (December 31, 2019: \$1,196,000), which includes the drawdown of \$6,924,000 (USD \$5,250,000) of the 2019 Panta loan and receipts of \$5,529,000 (USD \$4,123,000) Paycheck Protection Program Loan from the U.S. Small Business Administration to ACF.

Payment of interest during the year amounted to \$3,954,000 (December 31, 2019: \$5,049,000); Decrease in payment mainly due to repayment of bank indebtedness and term debt during the year.

On December 31, 2020, the ratio of the Company's current assets to current liabilities was 0.47:1 (December 31, 2019: 0.47:1).

### Contractual Obligations

#### PAYMENTS DUE BY PERIOD

(unaudited, expressed in thousands of Canadian dollars)

|                                   | Total   | Within 1 year | Between 1-5 years | Over 5 years |
|-----------------------------------|---------|---------------|-------------------|--------------|
| Lease obligations                 | 18,243  | 2,619         | 11,639            | 3,985        |
| Bank indebtedness                 | 76,708  | 76,708        | -                 | -            |
| Term loan <sup>1</sup>            | 17,793  | 14,249        | 1,774             | 1,770        |
| Purchase obligations <sup>2</sup> | 35,238  | 31,601        | 3,637             | -            |
| Total contractual obligations     | 147,982 | 125,177       | 17,050            | 5,755        |

1. This amount includes loan with a related party, obligations the Company has with Industrial Technologies Office and the U.S. Small Business Administration
2. Purchase obligations include payments for the Company's 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 consolidated financial statements.

### Capital Stock

As at December 31, 2020, there were 368,118,620 common shares, no common share purchase warrants, and 5,441,000 stock options issued and outstanding.

### Common Shares

Panta Canada B.V., is 100% owned by Panta Holdings B.V. and is Avcorp's majority shareholder owning approximately 71.2% of issued and outstanding common shares as of December 31, 2020.

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 368,118,620 common shares issued at December 31, 2020. The book value of common shares issued and outstanding as at December 31, 2020 was \$86,219,000 (December 31, 2019: \$86,219,000), and a shareholders' deficiency of \$49,140,000 (December 31, 2019: \$43,475,000 deficiency).

### Accounting standards

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

#### Amendments to IAS 1: Classification of Liabilities as Current or Non-Current

In January 2020, the IASB issued Classification of Liabilities as Current or Non-current (Amendments to IAS 1). The amendments aim to promote consistency in applying the requirements by helping companies determine whether, in the statement of financial position, debt and other liabilities with an uncertain settlement date should be classified as current (due or potentially due to be settled within one year) or non-current. The amendments include clarifying the classification requirements for debt a company might settle by converting it into equity. The amendments are effective for annual reporting periods beginning on or after January 1, 2023, with earlier application permitted. The Company is currently assessing the impact and timing to adopt this amendment.

#### Amendments to IAS 37: Onerous Contracts – Costs of Fulfilling a contract

In May 2020, the IASB issued amendments to IAS 37 to specify which costs an entity needs to include when assessing whether a contract is onerous or loss-making.

The amendments apply a “directly related cost approach”. The costs that relate directly to a contract to provide goods or services include both incremental costs and an allocation of costs directly related to contract activities. General and administrative costs do not relate directly to a contract and are excluded unless they are explicitly chargeable to the counterparty under the contract.

The amendments are effective for annual reporting periods beginning on or after 1 January 2022, with earlier application permitted. The Company is currently assessing the impact and timing to adopt this amendment.

## Operations Overview

### Delivery and Quality Performance

Deliveries and quality performance as at December 31, 2020 for Canadian and US 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.

### 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 December 2022; certain select production contracts extend to 2027. Agreements with Boeing Defence, Space and Security extend to 2022 with established minimum base delivery quantity requirements. The Bombardier and Subaru agreements extend for the life of the individual aircraft programs. Agreements with Lockheed Martin extend into 2022. Agreements with BAE Systems (Operations) Limited extend into 2022 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 Avcorp’s management believes that the Company’s stakeholders consider this metric to be useful information to assist them in evaluating profitability. The order backlog, as at December 31, 2020, is \$407 million in consideration of attaining full award values, compared to \$664 million as at December 31, 2019. The changes in order backlog are as follows:

- \$151 million decrease in order backlog resulting from revenues recorded during the year ended December 31, 2020;
- \$112 million decrease in order backlog due to decreases in the production rates for several existing commercial programs, offset by an increase in BAE production requirements;
  - COVID-19 has significantly impacted the aviation and aerospace manufacturing industry causing disruptions in production and slowing demand as workers go home, passengers stop travelling and customers defer delivery of new aircrafts. Some of the Company’s major commercial programs have reduced their production requirements into 2021 with recovery expected by 2023.
- \$6 million increase 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 year; 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. 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. Critical supplier cost reduction initiatives are in process and continuing into the future.

### Working Capital Utilization

Total current assets less total current liabilities were in a deficit position of \$77,780,000 at December 31, 2020 and a \$71,561,000 deficit position at December 31, 2019. However, the Company's accounts receivable, contract assets, and inventories net of accounts payable, amount to a \$33,174,000 surplus as at December 31, 2020 (December 31, 2019: \$18,542,000).

### 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 number of employees at December 31, 2020 was 546 (December 31, 2019: 740). The decrease in the number of employees during 2020 was due to reduced requirements from our customers directly impacted by COVID-19.

#### 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;
- adverse impact of the COVID-19 virus on the aviation industry, employees, supply chain and customers;
- 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.

In March 2020, the World Health Organization ("WHO") declared coronavirus ("COVID-19") a global pandemic. Governments worldwide enacted emergency measures including travel bans, social distancing measures and mandatory quarantine requirements. The measures have negatively impacted the global economy and adversely impacted the aviation industry worldwide particularly in the commercial airline industry. The significant decrease in air travel resulting from the COVID-19 pandemic is adversely affecting Avcorp's customers and their demand for the Company's products. The situation remains dynamic and the ultimate duration and magnitude of the impact on the economy and the financial effect on the Company remains unknown at this time. The Company has continued operations at all locations throughout this period and has taken many steps to mitigate the risk to its personnel and business performance:

- Social distancing practices have been implemented at all sites surrounding meetings, working from home, sanitation procedures and rotating shifts.
- Regularly communicating with customers and suppliers to assess the impact to their businesses and the impact to the Company. Stopping supplier shipments as customer delivery schedules are pushed out.
- Management has taken extensive measures to cut costs by reducing headcount at the Burlington, Gardena and Delta facility, halting salary increases and bonuses, and reducing expenses in various other areas.
- A few commercial programs had production shutdowns for a period of a month in the Delta facility to adjust to customer delivery schedules.
- Applying for government grant support relief initiatives such as the Canada Emergency Wage Subsidy and U.S. Small Business Administration Paycheck Protection Program from the U.S. Small Business Administration.

- The Company has formed a committee composed of the senior leadership team in the organization to monitor the evolution of the pandemic, to evaluate the measures being put in place by local, provincial/state and national governments and the resulting impacts on the Company and to implement necessary contingency plans as the current situation continues to evolve.

#### **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 acquired entities;
- finance new program development and introduction;
- finance new equipment purchases;
- develop or enhance existing services and capabilities;
- respond to competitive pressures;
- finance business acquisitions.

#### **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 2027. Agreements with Boeing DSS have been renewed and established which extend to 2022 with minimum base quantity requirements. It is the Company's objective to successfully renew Boeing production contracts in advance of expiry dates.

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

BAE and Lockheed Martin customer contracts extend into 2022. 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 will continue to be depressed in 2021 due to the impact of COVID-19 with recoveries in 2022 to 2023.
- Boeing 737 MAX grounding has resulted in reduced production rates for 2021 and 2022.
- Bombardier Challenger CL650 aircraft production requirements declined in 2020 and expected to remain at current levels in 2021.
- The global market for defence aircraft has seen continued growth in 2021 and expected to grow further in 2022.
- The F-35 remains, on a global scale, one of the largest Defence Airplane programs for the foreseeable future.
- Offset opportunities created by Canadian Government procurement within military aerospace programs such as the Boeing F-18 and Airbus C295 FWSAR could lead to additional revenue opportunities from this aerospace sector.
- The COVID-19 virus has adversely impacted the aviation industry. As the pandemic continues to reduce passenger airline traffic, OEMs have reduced their future production rates with anticipated full recoveries in 2022 to 2023.

#### **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 58% of Avcorp Group's cost of sales is related to labour and overhead and 42% 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 September 25, 2019, the company reached a new labour agreement with the International Association of Machinists and Aerospace Workers (Lodge 250) (the "Union") at its Delta, British Columbia facility. The new six-year labour agreement was ratified by the Union and will expire on March 31, 2025. 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 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.

Subsequent to year end on February 25, 2021, the Company amended the Avcorp Composite Fabrication Inc.'s Gardena facility lease agreement effective January 1, 2021 to vacate certain buildings and negotiated new lease terms. This will reduce lease costs and shared operating costs.

### US Dollar

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 carries US dollar denominated debt within Bank Indebtedness, Term Debt, Accounts Payable, and Customer Advance. If the Canadian dollar weakens against the US Dollar, the Company will have a foreign exchange loss and if the Canadian dollar strengthens against the US dollar, the Company will have a foreign exchange gain. The impact of this will be mitigated by US dollar denominated cash, accounts receivable, and contract assets.

### Outlook

In March 2020, the World Health Organization ("WHO") declared coronavirus ("COVID-19") a global pandemic. Governments worldwide enacted emergency measures including travel bans, social distancing measures and mandatory quarantine requirements. The measures have negatively impacted the global economy and adversely impacted the aviation industry worldwide particularly in the commercial airline industry. The significant decrease in air travel resulting from the COVID-19 pandemic is adversely affecting Avcorp's customers and their demand for the Company's products. The situation remains dynamic and the ultimate duration and magnitude of the impact on the economy and the financial effect on the Company remains unknown at this time. The Company has continued operations at all locations throughout this period and has taken many steps to mitigate the risk to its personnel and business performance:

- Social distancing practices have been implemented at all sites surrounding meetings, working from home, sanitization procedures, and rotating shifts.
- Regularly communicating with customers and suppliers to assess the impact to their businesses and the impact to the Company. Stopping supplier shipments as customer delivery schedules are pushed out.
- Management has taken extensive measures to cut costs by reducing headcount at the Burlington, Gardena and Delta facility, halting salary increases and bonuses, and reducing expenses in various other areas.
- A few commercial programs had production shutdowns for a period of a month in the Delta facility to adjust to customer delivery schedules.
- Applying for government grant support relief initiatives such as the Canada Emergency Wage Subsidy and U.S. Small Business Administration Paycheck Protection Program from the U.S. Small Business Administration.
- The Company has formed a committee composed of the senior leadership team in the organization to monitor the evolution of the pandemic, to evaluate the measures being put in place by local, provincial/state and national governments and the resulting impacts on the Company and to implement necessary contingency plans as the current situation continues to evolve.

The Company continues to work towards securing additional defence and commercial program production contracts in order to augment and diversify its backlog. Both defence and commercial production contracts are being renewed, with select new customer agreements extending into 2027. 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 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 and start-up costs required for new programs.



The Company forecasts its working capital financing requirements for 2021 to be met by the operating line of credit and working capital surplus (exclusive of bank indebtedness). Working capital financing has been supplemented, at times, by shareholder loans.

Management assesses the Company's ability to continue as a going concern at each reporting date, using quantitative and qualitative information available. Material uncertainties have been identified which may cast significant doubt upon the Company's ability to continue as a going concern. The Company's ability to continue as a going concern is dependent upon its ability to successfully negotiate extended terms with its creditor, meet financial covenants, achieve improvements in operating results, and mitigate the adverse impact of the COVID-19 virus. In assessing whether the going concern assumption was appropriate, management considered all relevant information available about the future, which is the 12-month period from the date of this report. 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.

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

The Company, in conjunction with its Board of Directors, is currently implementing various strategies which include:

- The Company is in discussions to extend the maturity of a loan agreement with a Canadian Chartered Bank maturing on June 30, 2021. As of the date of this report, the Company has drawn USD \$60,037,000 (CAD \$76,439,000) of the loan. The Company cannot provide assurance it will be able to extend the maturity date.
- The Company ended the year with bank operating line utilization of \$76,439,000 (USD \$60,037,000) offset by \$7,044,000 cash compared to utilization of \$84,661,000 (USD \$65,184,000) with \$4,316,000 cash on hand as of December 31, 2019. The balance of the net loss and related adjustments on modification of bank indebtedness as a result of executing an amending agreement in 2019 was \$269,000 as at December 31, 2020 (December 31, 2019 \$809,000). As at the date of this report the Company is able to draw up to an additional \$20,000 (USD \$16,000) on its operating line of credit.
- The loan agreement with a Canadian Chartered Bank has certain financial covenants. The Company cannot provide assurance it will be able to meet the financial metrics going forward. The Company may seek a waiver or amendment to the loan agreement as described in the loan agreement, if an event of default is to occur. The financial covenants may also be cured by drawing additional funds from the non-revolving standby facility secured on March 12, 2021 with Panta Canada B.V.
- On March 12, 2021, the Company entered into a multiparty amended and restated Accommodation Agreement with each of a customer, and Panta Canada B.V. whereby, inter alia;
  - Panta Canada B.V. has agreed to provide a USD \$10,000,000 non-revolving standby loan facility and a USD \$3,000,000 equipment loan for an aggregate availability of USD \$13,000,000; and
  - The elimination of unamortized cash advance, mutual release and forgiveness of certain historic and future guarantee fees payable to the customer. As at December 31, 2020, the guarantee fee is \$8,178,000 (USD \$6,423,000), the customer advance is \$5,911,000 (USD \$4,643,000) and the legal claim is \$7,130,000 (USD \$5,600,000).
- On April 28, 2020, the Company received a loan in the amount of USD \$4,123,000 to support Avcorp Composite Fabrication Inc ("ACF") from a U.S. Chartered Bank through the U.S. Small Business Administration Paycheck Protection Program. The Company has recognized a forgiveness of USD \$3,430,000 in 2020 as the Company has satisfied the requirements of loan forgiveness. On March 9, 2021, the Company submitted the application for review to receive this forgiveness. The remaining loan balance has a term of 2 years and bears interest at a fixed rate of 1% per annum.
- On March 15, 2021, the Company received a second wave U.S. Small Business Administration Paycheck Protection Program loan in the amount of USD \$2,000,000.
- Close collaboration with customers has resulted in both financial and operational support for continued operations.

The assessment of the Company's ability to execute its strategy of reducing operating costs, and ability to mitigate the risk of the COVID-19 virus involves significant judgement. Estimates and assumptions regarding future operating costs, revenue and profitability levels and general business and customer conditions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

### Transactions with Related Parties

Periodically, consulting services are provided by certain directors. Fees paid to certain directors, or companies with which they have beneficial ownership, during the year ended December 31, 2020 amount to \$Nil (December 31, 2019: \$3,000). Fees payable to certain directors or Companies with which they have beneficial ownership, as at December 31, 2020 are \$Nil (December 31, 2019: \$Nil). These fees are included in the Consolidated statements of Loss and Comprehensive Loss as administrative and general expenses and amount to \$Nil for the year ended December 31, 2020 (December 31, 2019: \$3,000).

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***(expressed in thousands of Canadian dollars)*

|   | 2020           | 2019    |
|---|----------------|---------|
| Salaries and other short-term employee benefits | <b>\$1,746</b> | \$2,002 |
| Contributions to defined contribution plan      | <b>91</b>      | 82      |
| Option-based awards                             | <b>32</b>      | 76      |
|   | <b>1,869</b>   | 2,160   |

The balance of loans receivable from key management as at December 31, 2020 is \$5,000 (December 31, 2019: \$5,000). These loans are unsecured and payable on demand.

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

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

**Business Acquisition**

As at the date of this report, no agreements to merge with or acquire another entity have been entered into.

**Fourth Quarter**

The following summarizes financial results for the fourth quarter 2020.

Operating profit for the fourth quarter of 2020 was \$8,477,000 from \$44,742,000 in revenues, as compared to operating loss of \$8,114,000 from \$38,309,000 in revenues for the quarter ended December 31, 2019, mainly contributed by the government grant income of \$7,646,000 and an estimate of variable consideration related to a contract termination of convenience. The Company expensed \$2,684,000 of overhead costs during the fourth quarter 2020 (2019: \$2,072,000) in respect of unutilized plant capacity. Provision for onerous contracts accrued during the fourth quarter 2020 totaled \$188,000 (December 31, 2019: \$155,000 amortization).

**Critical Accounting Estimates and Judgment**

The preparation of consolidated financial statements in conformity with IFRS requires management to make estimates and judgments that affect the amounts which are reported in the consolidated financial statements during the reporting period. Estimates and other judgments are evaluated at each reporting date and are based on management's experience and other factors, including expectations about future events that are believed to be reasonable under the circumstances. Any changes in estimates and assumptions could have a material impact on the assets and liabilities at the date of the statement of financial position. The Company reviews its estimates and assumptions on an ongoing basis and uses the most current information available and exercises careful judgement in making these estimates and assumptions.

- **Functional currency:** The functional currency for the Company and its subsidiaries is the currency of the primary economic environment in which each operates. The Company has determined that the functional currency for the Company and all its subsidiaries except for Avcorp US Holdings Inc. and ACF is the Canadian dollar. The functional currency for Avcorp US Holdings Inc. and ACF is the US dollar. The determination of functional currency may require certain judgements to determine the primary economic environment. The Company reconsiders the functional currency used when there is a change in events and conditions which determined the primary economic environment.
- **Impairments:** The recoverable amount of intangible assets, development costs and property, plant and equipment are based on estimates and assumptions regarding the expected market outlook and cash flows from each of the Company's CGU. Assumptions, judgments and estimates about future values are complex and often subjective. They can be affected by a variety of factors, including external factors such as industry and economic trends, and internal factors such as changes in the Company's business strategy or internal forecasts. Although the Company believes the assumptions, judgments and estimates made in the past have been reasonable and appropriate, different assumptions, judgments and estimates could materially affect the Company's reported financial results.
- **Going concern and debt classification:** Management assesses the Company's ability to continue as a going concern at each reporting date, using quantitative and qualitative information available. Management also determines the appropriate classification of its debt arrangements based on terms of the various agreements based on the Company's financial condition. 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.
- **Capitalization of development costs:** When capitalizing development costs the Company must assess the technical and commercial feasibility of the projects and estimate the useful lives of resulting products. Determining whether future economic benefits will flow from the assets and therefore the estimates and assumptions associated with these calculations are instrumental in (i) deciding whether project costs can be capitalized, and (ii) accurately calculating the useful life of the projects for the Company. A change in estimate of the amortization period occurred for a contract that received a termination of convenience, an accelerated amortization of \$7,469,000 was recognized in the year ended December 31, 2020.

- Inventories are valued at the lower of cost and net realizable value. The costs of inventory involve estimates in determining the allocation of fixed and variable production overhead. These estimates involved include determination of normal production capacity and nature of expenses to be allocated.
- On a periodic basis the Company reviews its plant capacity and estimates the portion of its under-utilized overhead expenditures. The Company has expensed \$8,346,000 of overhead costs during the current year (December 31, 2019: \$7,004,000) in respect of unutilized plant capacity. These amounts are included in the Consolidated Statements of Loss and Comprehensive Loss as costs of sales.
- The Company has entered into production contracts in the ordinary course of its business. The unavoidable cost of meeting the obligations under certain of these contracts exceeds the associated expected future net benefits; consequently, an onerous contract provision has been recognized. The calculation of this provision involves the use of estimates including, but not limited to, program gross margin, and the effect of learning curves of production and the timing of achieving certain operational efficiencies. These actual results can vary significantly from these estimates with consequent variability in the amounts of the provision recorded. The onerous contract provision is calculated by taking the expected future costs that will be incurred under the contract and deducting any estimated revenues. The onerous contract provision is primarily due to a high cost structure and learning curves of production that cannot be recovered through current pricing of the associated contracts. The total onerous contract provision for the year ended December 31, 2020 is \$565,000 (December 31, 2019: \$251,000).
- While a formal claim has not been levied by the customer, the Company has provisioned for a claim asserted by a customer in the amount of \$7,130,000 (USD \$5,600,000) as at December 31, 2020 (December 31, 2019: \$7,273,000 (USD \$5,600,000)). Subsequent to year end on March 12, 2021, the Company has amended and restated the accommodation agreement with customer and Panta B.V. Canada providing a mutual release and settlement on all claims.
- Values of right of use assets and lease liabilities require judgement in determining lease terms such as extension option and discount rate used. In the case where incremental borrowing rate is used, the Company estimates the incremental borrowing rate based on the lease term, collateral assumptions, and the economic environment in which the lease is denominated.
- The Company has provisioned USD \$1,350,000 (December 31, 2019: USD \$1,350,000) for a legal action due to certain employment practices at the Gardena facility.
- Upon termination for convenience for customer contracts subject to the Federal Acquisition Regulation ("FAR"), the Company must assess the contractual provisions that permit termination and the related contractual remedies available to recover all or a portion of our incurred costs and fees for work performed. Variable consideration is recognized as estimated revenue to the extent it is probable that a significant reversal in the amount of revenue recognized will not occur when the uncertainty associated with the variable consideration is subsequently resolved. Management estimated the variable consideration using actual costs, an estimate of reasonable profit margin determined in accordance with the contractual provisions and historical experience, and delay cost estimates under the contractual entitlement subject to FAR. Although the Company believes its estimates and assumptions made are consistent with the terms and conditions of the contract, the actual settlement amount determined at a future date could materially affect the Company's reported financial results.
- The Company has determined that it will meet the eligibility requirements for the Canada Emergency Wage Subsidies not yet received and has estimated the amounts recognized as other income and deferred government grant to be \$2,031,000 and \$657,000 respectively in the current year.
- The Company has determined that it will meet the eligibility requirements for partial forgiveness of the U.S. Small Business Administration Paycheck Protection Program loan has recognized \$4,601,000 (USD3,430,000) in other income in the current year.

## Financial Instruments and Other Instruments

### Market Risk

Market risk is the risk that changes in the market prices, such as foreign exchange rates and interest rates, will affect the Company's income or the value of its holdings of financial instruments. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes. The Company may utilize derivative instruments in the management of its foreign currency and interest rate exposures.

### Currency Risk

Currency risk arises because the amount of the local currency receivable or payable for transactions denominated in foreign currencies may vary due to changes in exchange rate ("transaction exposures") and because the non-Canadian dollar denominated financial statements of the Company's subsidiaries may vary on consolidation into the reporting currency of Canadian dollars ("translation exposures").

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 components in US dollars at prices that are usually established at the order date. 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 for the year ended December 31, 2020 is \$364,000 (December 31, 2019: \$843,000 gain).

The Company had the following US dollar denominated balances:

**CURRENCY RISK***(expressed in thousands of dollars)*

| <b>AS AT DECEMBER 31</b> | <b>2020</b> (expressed in USD) | 2019 (expressed in USD) |
|--------------------------|--------------------------------|-------------------------|
| Bank cash position       | <b>\$3,285</b>                 | \$2,639                 |
| Accounts receivable      | <b>6,393</b>                   | 9,824                   |
| Accounts payable         | <b>3,726</b>                   | 6,948                   |
| Customer advance         | <b>4,643</b>                   | 4,643                   |
| Bank indebtedness        | <b>60,037</b>                  | 65,184                  |
| Term debt                | <b>10,322</b>                  | 4,273                   |

With other variables unchanged, each \$0.10 strengthening (weakening) of the CAD against the USD would result in an increase (decrease) of approximately \$6,905,000 in net income for the year ended December 31, 2020 as a result of holding a net liability position in USD as at December 31, 2020.

As at December 31, 2019, a \$0.10 strengthening (weakening) of the CAD against the USD would result in an increase (decrease) of approximately \$6,859,000 in net income for the year ended December 31, 2019 as a result of holding a net liability position in USD as at December 31, 2019.

**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 Defence, Space & Security ("BDS"), Bombardier Aerospace ("Bombardier"), BAE Systems (Operations) Limited ("BAE"), Lockheed Martin ("LM"), and Subaru Corporation ("Subaru"). The maximum exposure to credit risk is represented by the amount of accounts receivable in the consolidated statements of financial position.

As at the consolidated statements of financial position date 89.6% (December 31, 2019: 85.6%) of the Company's trade accounts receivable are attributable to these customers.

The Company is exposed to credit risk if counterparties to its trade receivables are unable to meet their obligations. The concentration of credit risk from its customers is minimized because the Company has an original equipment manufacturer and tier one aerospace customer base as at December 31, 2020. The customers are predominately large, well-capitalized, and long-established entities with a low risk of non-payment. The Company regularly monitors its credit risk and credit exposure.

**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.

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

Management assesses the Company's ability to continue as a going concern at each reporting date, using quantitative and qualitative information available. Material uncertainties have been identified which may cast significant doubt upon the Company's ability to continue as a going concern. The Company's ability to continue as a going concern is dependent upon its ability to successfully negotiate extended terms with its creditor, meet financial covenants, achieve improvements in operating results, and mitigate the adverse impact of the COVID-19 virus. In assessing whether the going concern assumption was appropriate, management considered all relevant information available about the future, which is the 12-month period from the date of this report. 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.

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- The loan agreement with a Canadian Chartered Bank has certain financial covenants. The Company cannot provide assurance it will be able to meet the financial metrics going forward. The Company may seek a waiver or amendment to the loan agreement as described in the loan agreement, if an event of default is to occur. The financial covenants may also be cured by drawing additional funds from the non-revolving standby facility secured on March 12, 2021 with Panta Canada B.V.
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- On March 15, 2021, the Company received a second wave U.S. Small Business Administration Paycheck Protection Program loan in the amount of USD \$2,000,000.
- Close collaboration with customers has resulted in both financial and operational support for continued operations.

The assessment of the Company's ability to execute its strategy of reducing operating costs, and ability to mitigate the risk of the COVID-19 virus involves significant judgement. Estimates and assumptions regarding future operating costs, revenue and profitability levels and general business and customer conditions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

### Interest Rate Risk

The Company is exposed to interest rate risk on the utilized portion of its operating line of credit.

Interest rate for advances made up to the maximum of the allowable borrowing base of USD \$23,000,000 revolving loan less USD \$2,300,000:

- Royal Bank Prime ("RBP") plus 1.50% per annum
- Royal Bank US Base Rate ("RBUSBR") plus 1.50% per annum
- Banker's Acceptance ("BA") Equivalent Rate plus 3.00% per annum
- LIBOR Rate plus 3.00% per annum

Interest rate for advances made on the additional USD \$45,000,000 borrowing capacity up to USD \$68,000,000.

- RBP plus 0.00% per annum
- RBUSBR plus 0.00% per annum
- BA Equivalent Rate plus 0.875% per annum
- LIBOR Rate plus 0.875% per annum

There is uncertainty as to the continued use of LIBOR in the future. LIBOR is the subject of national, international and other regulatory guidance and proposals for reform. These reforms and other pressures have outlined a complete phase out by June 30, 2023, with some plans starting as early as December 31, 2021. The consequences of these developments cannot be entirely predicted but could include an increase in the cost of our variable rate indebtedness and obligations.

Drawdown under the USD \$45,000,000 additional borrowing capacity is supported by a Guarantee provided by a Guarantor. Panta Holdings B.V. provided guarantee to the Guarantor in the maximum payment of USD \$10,000,000 if the bank draws on the Guarantee in whole or in part.

The Company will provide the Guarantor, as consideration for the Guarantee, a fee equal to 5.375% of the weighted average outstanding balance of the guaranteed portion over each full twelve (12) month period commencing on the funding date plus, for the partial year thereafter, 5.375% of the weighted average outstanding balance of the guaranteed portion multiplied by the number of days in the partial year divided by three hundred sixty (360). The fee will be payable on the maturity date. Subsequent to year end on March 12, 2021, the Company has amended and restated the accommodation agreement with a customer and Panta B.V. Canada waiving all rights to the Guarantee Fee.

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

### 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 and capital stock in its definition of capital, as shown in the Company's consolidated statements of financial position.

The Company's primary objective in its management of capital is to ensure that it has sufficient financial resources to fund ongoing operations and new program investment. In order to secure this capital the Company may attempt to raise funds via issuance of debt and equity, or by securing strategic partners.

The Company's loan agreement with a Canadian Chartered Bank restricts the declaration or payment of any dividend.

### 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 ("CEO") and the Vice President, Finance ("VP Finance") 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](http://www.sedar.com).

The Company has continued to undertake to engage additional, qualified financial reporting expertise and tax accounting resources to assist with complex accounting matters, as well as develop the expertise of in-house staff. Furthermore, the Company is aligning its business systems within its two largest facilities in order to simplify and increase consistency of internal controls over financial reporting.

#### Internal Controls over Financial Reporting

The CEO and the VP Finance have designed internal controls over financial reporting or have caused them to be designed under their supervision, in order to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements for external purposes in accordance with IFRS.

An evaluation was carried out, under the supervision of the CEO and the VP Finance, of the design and effectiveness of our internal controls over financial reporting. Based on this evaluation, the CEO and the VP Finance concluded that the internal controls over financial reporting are effective, using the criteria set forth by the Committee of Sponsoring Organizations of the Treadway Commission (COSO) on Internal Control – Integrated Framework (2013 Framework).

#### Disclosure Controls and Procedures ("DCP")

The CEO and the VP Finance have designed disclosure controls and procedures, or have caused them to be designed under their supervision, in order to provide reasonable assurance that:

- material information relating to the Corporation has been made known to them; and
- information required to be disclosed in the Corporation's filings is recorded, processed, summarized and reported within the time periods specified in securities legislation.

An evaluation was carried out, under the supervision of the CEO and the VP Finance, of the design and effectiveness of our disclosure controls and procedures. Based on this evaluation, the CEO and the VP Finance concluded that the disclosure controls and procedures are effective.

### 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 consolidated financial statements of Avcorp Industries Inc. and all other information contained in the Management Discussion and Analysis are the responsibility of management and has been reviewed and approved by the Board of Directors of the Company. The Board of Directors is responsible for ensuring that we fulfill our responsibilities for financial reporting and is ultimately responsible for reviewing and approving the MD&A. The Board of Directors carries out this responsibility principally through its Audit Committee. The Audit Committee is appointed by the Board of Directors and is comprised entirely of independent directors. The Audit Committee reports its findings to the Board of Directors for its consideration when it approves the MD&A and financial statements for issuance to shareholders. The consolidated financial statements were prepared in conformity with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") appropriate in the circumstances, and include some amounts based on management's best judgments and estimates. The financial information contained elsewhere in this Management Discussion and Analysis is consistent with that in the consolidated financial statements.

Management is responsible for maintaining a system of internal accounting controls and procedures. 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 IFRS. During the period covered by this report, there has been no change in internal control over financial reporting that has materially affected, or is reasonably likely to materially affect, the issuer's internal control over financial reporting.

|                         |  |                      |   |
|-------------------------|--|----------------------|---|
| <i>"Amandeep Kaler"</i> | <b>AMANDEEP KALER</b><br>Group Chief Executive Officer | <i>"Amish Patel"</i> | <b>AMISH PATEL</b><br>Group Vice President, Finance |
|-------------------------|--|----------------------|---|

# Independent auditor's report

To the Shareholders of  
**Avcorp Industries Inc.**

## Opinion

We have audited the consolidated financial statements of **Avcorp Industries Inc.** and its subsidiaries [the "Group"], which comprise the consolidated statements of financial position as at December 31, 2020 and 2019, and the consolidated statements of loss and comprehensive loss, consolidated statements of changes in shareholders' deficiency and consolidated statements of cash flows for the years then ended, and notes to the consolidated financial statements, including a summary of significant accounting policies.

In our opinion, the accompanying consolidated financial statements present fairly, in all material respects the consolidated financial position of the Group as at December 31, 2020 and 2019, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards ["IFRSs"].

## Basis for opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report. We are independent of the Group in accordance with the ethical requirements that are relevant to our audit of the consolidated financial statements in Canada, and we have fulfilled our other ethical responsibilities in accordance with these requirements. We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

## Material uncertainty related to going concern

We draw attention to note 1 in the consolidated financial statements, which indicates that the Group had a net loss of \$6,725,000, operating cash flows of \$9,125,000, shareholders' deficiency of \$49,140,000, and an accumulated deficit of \$148,919,000. These events or conditions, along with other matters as set forth in note 1, indicate that a material uncertainty exists that may cast significant doubt on the Group's ability to continue as a going concern. Our opinion is not modified in respect of this matter.

## Key audit matters

Key audit matters are those matters that, in our professional judgment, were of most significance in the audit of the consolidated financial statements of the current period. In addition to the matters described in the *Material uncertainty related to going concern* section, we have determined the matters described below to be the key audit matters to be communicated in our report. These matters were addressed in the context of the audit of the consolidated financial statements as a whole, and in forming our opinion thereon, and we do not provide a separate opinion on these matters. For each matter below, our description of how our audit addressed the matter is provided in that context.

We have fulfilled the responsibilities described in the *Auditor's responsibilities for the audit of the consolidated financial statements* section of our report, including in relation to these matters. Accordingly, our audit included the performance of procedures designed to respond to our assessment of the risks of material misstatement of the consolidated financial statements. The results of our audit procedures, including the procedures performed to address the matters below, provide the basis for our audit opinion on the accompanying consolidated financial statements.





| Key audit matter   | How our audit addressed the key audit matter  |
|--|---|
| <p><i>Valuation of Avcorp Structures &amp; Integration ["ASI"] and Avcorp Composite Fabrication ["ACF"] cash-generating units ["CGUs"]</i></p> <p>As at December 31, 2020, the Group has \$48,403,000 of long-lived assets allocated to three CGUs. At the end of each reporting period, the Group determines whether indicators of impairment exist for each CGU. If indicators of impairment are identified for a CGU, the Group compares the CGU's carrying value to its recoverable amount determined as the higher of the fair value less costs to sell ["FVLCS"] or value in use ["VIU"]. Management of the Group determined that indicators of impairment existed for the ASI and ACF CGUs and the Group determined that the recoverable amount, determined as the FVLCS, of each CGU exceeded its carrying value. The Group's policy is disclosed in notes 3 and 4 of the consolidated financial statements.</p> <p>We identified the determination of the recoverable amount for the ASI and ACF CGUs as a key audit matter because it involves significant judgment in determining certain key assumptions such as expected revenue, discount rate, EBITDA margin and terminal value. Key assumptions are affected by expectations about future market and economic conditions, which include the uncertainty of demand from customers resulting from the impact of COVID-19 on the industry, both globally and locally. Changes in these assumptions can have a material effect on the determination of the recoverable amount.</p> | <p>Our audit procedures included, among others, the following to address the key assumptions mentioned above:</p> <ul style="list-style-type: none"><li>• We involved valuation specialists to assist in: [1] evaluating the Company's application of the FVLCS model; [2] performing a comparison of key assumptions used to determine the EBITDA margin, terminal value and discount rate to other similar companies taking into account industry-specific risk data.</li><li>• To test management's cash flows forecast, we: [1] compared the prior-year forecast to actual results to assess the reliability of management's estimation process; [2] assessed the reasonability of future revenue by comparing to product delivery forecasts provided by customers, when available, and evaluating other relevant support; [3] performed a sensitivity analysis on forecasted revenues and discount rate; and [4] considered management's assumptions relative to industry and economic trends.</li></ul> |

| Key audit matter  | How our audit addressed the key audit matter   |
|---|--|
| <i>Valuation of variable consideration to be recognised in Revenue related to contract terminations</i>   |  |
| <p>As at December 31, 2020 the Company reported a Contract Asset balance of \$34,325,000, which includes variable consideration related to certain contracts with a customer, and which were terminated for the convenience of the U.S. government under the Federal Acquisition Regulation [“FAR”]. The regulation along with the terms within the Company’s contracts allow for the Company to claim certain costs incurred associated with the contracts plus a reasonable profit margin upon termination.</p> <p>The determination of the variable consideration requires significant judgment and estimation. The amount of variable consideration is based on the actual costs, reasonable profit margin and delay cost estimated under the contractual entitlement subject to FAR. The Company has recognised variable consideration in revenue to the extent that it is highly probable that a significant reversal will not occur when the uncertainty related to the amount is resolved.</p> <p>The Company’s policy related to variable consideration is described in notes 3 and 4 to the consolidated financial statements.</p> <p>We identified the valuation of variable consideration to be a key audit matter because it involves significant judgment by management in determining the constrained estimated value of the various key inputs involved such as actual costs incurred, a reasonable profit margin and the delay cost estimated.</p> | <p>Our audit procedures included the following, among others to address the judgments and inputs to the estimate:</p> <ul style="list-style-type: none"><li>• We obtained an understanding of the process of estimating variable consideration through inquiries with management, program managers and internal company analysts.</li><li>• We compared the inputs such as actual costs incurred, reasonable profit margin and delay costs, used in management’s estimate to the relevant contractual termination provisions including FAR.</li><li>• We compared FAR rates used by management in determining the claim to historical FAR rates.</li><li>• We compared labour and overhead hours to program budgets and forecasts and actual hours incurred over the life of the program.</li><li>• We compared management’s estimate of a reasonable profit margin to historical margins achieved and program forecasted margins.</li></ul> |

**Other information**

Management is responsible for the other information. The other information comprises:

- Management’s Discussion and Analysis
- The information, other than the consolidated financial statements and our auditor's report thereon, in the Annual Report



Our opinion on the consolidated financial statements does not cover the other information and we do not express any form of assurance conclusion thereon.

In connection with our audit of the consolidated financial statements, our responsibility is to read the other information, and in doing so, consider whether the other information is materially inconsistent with the consolidated financial statements, or whether our knowledge obtained in the audit or otherwise appears to be materially misstated.

We obtained Management's Discussion and Analysis and the Annual Report prior to the date of this auditor's report. If, based on the work we have performed, we conclude that there is a material misstatement of this other information, we are required to report that fact in this auditor's report. We have nothing to report in this regard.

### **Responsibilities of management and those charged with governance for the consolidated financial statements**

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

In preparing the consolidated financial statements, management is responsible for assessing the Group's ability to continue as a going concern, disclosing, as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Group or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Group's financial reporting process.

### **Auditor's responsibilities for the audit of the consolidated financial statements**

Our objectives are to obtain reasonable assurance about whether the consolidated financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditor's report that includes our opinion. Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists. Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of these consolidated financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional scepticism throughout the audit. We also:

- Identify and assess the risks of material misstatement of the consolidated financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion. The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.
- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Group's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management’s use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Group’s ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditor’s report to the related disclosures in the consolidated financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditor’s report. However, future events or conditions may cause the Group to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the consolidated financial statements, including the disclosures, and whether the consolidated financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the Group to express an opinion on the consolidated financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

We communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

We also provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and to communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, actions taken to eliminate threats or safeguards applied.

From the matters communicated to those charged with governance, we determine those matters that were of most significance in the audit of the consolidated financial statements of the current period and are therefore the key audit matters. We describe these matters in our auditor’s report unless law or regulation precludes public disclosure about the matter or when, in extremely rare circumstances, we determine that a matter should not be communicated in our report because the adverse consequences of doing so would reasonably be expected to outweigh the public interest benefits of such communication.

The engagement partner on the audit resulting in this independent auditor’s report is Nicole Poirier.

Vancouver, Canada  
March 19, 2021

*Ernst & Young LLP*

Chartered Professional Accountants



**CONSOLIDATED STATEMENTS OF FINANCIAL POSITION***(expressed in thousands of Canadian dollars)***AS AT DECEMBER 31****ASSETS****Current assets**

|  | 2020           | 2019    |
|--|----------------|---------|
| Cash (note 16)                         | <b>\$7,044</b> | \$4,316 |
| Accounts receivable (note 9)           | <b>14,436</b>  | 17,625  |
| Government grant receivable (note 27)  | <b>2,688</b>   | -       |
| Contract assets (note 10)              | <b>34,325</b>  | 26,162  |
| Inventories (note 11)                  | <b>9,657</b>   | 12,933  |
| Prepayments and other assets (note 12) | <b>2,108</b>   | 2,136   |

**Non-current assets**

|  |               |        |
|--|---------------|--------|
| Prepayments and other assets (note 12)   | <b>2,877</b>  | 2,738  |
| Development costs (note 13)              | <b>9,045</b>  | 14,075 |
| Property, plant, and equipment (note 14) | <b>38,703</b> | 46,328 |
| Intangibles (note 15)                    | <b>655</b>    | 1,827  |

**Total assets**

|                |         |
|----------------|---------|
| <b>121,538</b> | 128,140 |
|----------------|---------|

**LIABILITIES AND DEFICIENCY****Current liabilities**

|   |               |        |
|---|---------------|--------|
| Bank indebtedness (note 16)                               | <b>76,708</b> | 85,470 |
| Accounts payable and accrued liabilities (note 18 and 34) | <b>27,932</b> | 38,178 |
| Current portion of term debt (note 20)                    | <b>16,868</b> | 2,768  |
| Customer advance (note 17 and 34)                         | <b>5,911</b>  | 6,030  |
| Guarantee fee (note 16 and 34)                            | <b>8,178</b>  | -      |
| Deferred government grant (note 27)                       | <b>657</b>    | -      |
| Contract liability (note 19)                              | <b>11,502</b> | 2,036  |
| Onerous contract provision (note 21)                      | <b>282</b>    | 251    |

**Non-current liabilities**

|                                      |               |        |
|--------------------------------------|---------------|--------|
| Guarantee fee (note 16 and 34)       | -             | 5,277  |
| Term debt (note 20)                  | <b>19,168</b> | 26,848 |
| Contract liability (note 19)         | <b>3,189</b>  | 4,757  |
| Onerous contract provision (note 21) | <b>283</b>    | -      |

**(Deficiency) Equity**

|  |                  |           |
|--|------------------|-----------|
| Capital stock (note 23)                | <b>86,219</b>    | 86,219    |
| Contributed surplus                    | <b>5,478</b>     | 5,446     |
| Accumulated other comprehensive income | <b>8,082</b>     | 7,054     |
| Accumulated deficit                    | <b>(148,919)</b> | (142,194) |

**Total liabilities and deficiency**

|                |         |
|----------------|---------|
| <b>121,538</b> | 128,140 |
|----------------|---------|

Nature of operations and going concern (note 1)

Subsequent events (note 34)

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

**Approved by the Board of Directors on March 19, 2021***"David Levi"*David Levi  
Chairman*"Ken Robertson"*Ken Robertson  
Committee Chair, Audit & Corporate Governance Committee

**CONSOLIDATED STATEMENTS OF LOSS AND COMPREHENSIVE LOSS***(expressed in thousands of Canadian dollars, except number of shares and per share amounts)*

| <b>FOR THE YEAR ENDED DECEMBER 31</b>                                   | <b>2020</b>      | 2019      |
|---|------------------|-----------|
| <b>Revenues</b> (notes 3, 17, and 33)                                   | <b>\$150,962</b> | \$164,770 |
| <b>Cost of sales</b> (notes 3, 11, 21, and 33)                          | <b>142,729</b>   | 160,982   |
| <b>Gross profit</b>   | <b>8,233</b>     | 3,788     |
| Administrative and general expenses                                     | <b>16,717</b>    | 21,467    |
| Office equipment depreciation   | <b>787</b>       | 770       |
| Net gain on claims (note 26)  | -                | (17,974)  |
| Other (income) losses (note 27)   | <b>(11,642)</b>  | 649       |
| <b>Operating income (loss)</b>  | <b>2,371</b>     | (1,124)   |
| Finance costs – net (note 28)   | <b>7,605</b>     | 8,924     |
| Foreign exchange loss (gain)  | <b>364</b>       | (843)     |
| Net loss on sale and write-off of equipment                             | <b>1,127</b>     | 111       |
| <b>Loss before income tax</b>   | <b>(6,725)</b>   | (9,316)   |
| Income tax expense  | -                | -         |
| <b>Loss for the year</b>  | <b>(6,725)</b>   | (9,316)   |
| Other comprehensive income  | <b>1,028</b>     | 1,909     |
| <b>Total comprehensive loss for the year</b>                            | <b>(5,697)</b>   | (7,407)   |
| <b>Loss per share:</b>  |                  |           |
| Basic loss per common share (note 32)                                   | <b>(0.02)</b>    | (0.03)    |
| Diluted loss per common share (note 32)                                 | <b>(0.02)</b>    | (0.03)    |
| Basic weighted average number of shares outstanding (000's) (note 32)   | <b>368,118</b>   | 368,118   |
| Diluted weighted average number of shares outstanding (000's) (note 32) | <b>368,118</b>   | 368,118   |

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

**CONSOLIDATED STATEMENTS OF CASH FLOWS***(expressed in thousands of Canadian dollars)***FOR THE YEAR ENDED DECEMBER 31****Cash flows from operating activities**

|   | 2020             | 2019      |
|---|------------------|-----------|
| Net loss for the year   | <b>\$(6,725)</b> | \$(9,316) |
| Adjustment for items not affecting cash:  |                  |           |
| Net interest expense  | <b>7,605</b>     | 8,924     |
| Depreciation  | <b>8,338</b>     | 8,218     |
| Development cost amortization   | <b>8,955</b>     | 1,786     |
| Intangible assets amortization  | <b>1,197</b>     | 1,184     |
| Loss on disposal and write-off of equipment                                     | <b>1,127</b>     | 111       |
| Provision for onerous contracts   | <b>308</b>       | (1,665)   |
| Stock based compensation  | <b>32</b>        | 76        |
| Loss on Investment in AVS-SYS   | <b>-</b>         | 649       |
| Provision for obsolete inventory  | <b>(163)</b>     | (1,177)   |
| Provision for doubtful accounts   | <b>(326)</b>     | (1,425)   |
| Unrealized foreign exchange   | <b>(694)</b>     | (1,195)   |
| Government grant income   | <b>(6,632)</b>   | -         |
| Net claim settlement  | <b>-</b>         | (3,539)   |
| Cash flows from operating activities before changes in non-cash working capital | <b>13,022</b>    | 2,631     |
| Changes in non-cash working capital   |                  |           |
| Accounts receivable   | <b>9,195</b>     | 6,747     |
| Contract assets   | <b>(8,270)</b>   | (1,673)   |
| Inventories   | <b>3,397</b>     | 3,502     |
| Prepayments and other assets  | <b>13</b>        | 1,846     |
| Accounts payable and accrued liabilities  | <b>(10,265)</b>  | (3,324)   |
| Contract liability  | <b>2,033</b>     | 1,182     |
| <b>Net cash from operating activities</b>                                       | <b>9,125</b>     | 10,911    |
| <b>Cash flows used in investing activities</b>                                  |                  |           |
| Proceeds from sale of equipment   | <b>61</b>        | 99        |
| Purchase of equipment   | <b>(1,769)</b>   | (904)     |
| Payments relating to development costs and tooling                              | <b>(3,929)</b>   | (4,116)   |
| Initial lease payments and other direct costs incurred                          | <b>(31)</b>      | (102)     |
| <b>Net cash used in investing activities</b>                                    | <b>(5,668)</b>   | (5,023)   |
| <b>Cash flows used in financing activities</b>                                  |                  |           |
| Proceeds from bank indebtedness   | <b>653</b>       | 20,844    |
| Repayment of bank indebtedness  | <b>(7,368)</b>   | (18,010)  |
| Payment of interest   | <b>(3,954)</b>   | (5,049)   |
| Proceeds from term debt   | <b>12,453</b>    | 1,196     |
| Repayment of term debt  | <b>(2,524)</b>   | (2,591)   |
| <b>Net cash used in financing activities</b>                                    | <b>(740)</b>     | (3,610)   |
| <b>Net increase in cash</b>   | <b>2,717</b>     | 2,278     |
| <b>Net foreign exchange difference</b>  | <b>11</b>        | (13)      |
| <b>Cash - Beginning of the year</b>   | <b>4,316</b>     | 2,051     |
| <b>Cash - End of the year</b>   | <b>7,044</b>     | 4,316     |

Supplementary Cash Flow Information (note 29).

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

**CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' DEFICIENCY***(expressed in thousands of Canadian dollars, except number of shares)*

|  | Capital Stock      |               | Contributed Surplus | Accumulated Deficit | Accumulated Other Comprehensive Income | Total Deficiency |
|--|--------------------|---------------|---------------------|---------------------|--|------------------|
|  | Number of Shares   | Amount        |                     |                     |  |                  |
| <b>Balance at December 31, 2018</b>                  | 368,118,620        | 86,219        | 5,370               | (132,878)           | 5,145                                  | (36,144)         |
| Stock-based compensation expense                     | -                  | -             | 76                  | -                   | -                                      | 76               |
| Unrealized currency gain on translation for the year | -                  | -             | -                   | -                   | 1,909                                  | 1,909            |
| Net loss for the year                                | -                  | -             | -                   | (9,316)             | -                                      | (9,316)          |
| <b>Balance at December 31, 2019</b>                  | 368,118,620        | 86,219        | 5,446               | (142,194)           | 7,054                                  | (43,475)         |
| Balance at December 31, 2019                         | 368,118,620        | 86,219        | 5,446               | (142,194)           | 7,054                                  | (43,475)         |
| Stock-based compensation expense                     | -                  | -             | 32                  | -                   | -                                      | 32               |
| Unrealized currency gain on translation for the year | -                  | -             | -                   | -                   | 1,028                                  | 1,028            |
| Net loss for the year                                | -                  | -             | -                   | (6,725)             | -                                      | (6,725)          |
| <b>Balance at December 31, 2020</b>                  | <b>368,118,620</b> | <b>86,219</b> | <b>5,478</b>        | <b>(148,919)</b>    | <b>8,082</b>                           | <b>(49,140)</b>  |

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



**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

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**1. Nature of Operations and Going Concern**

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.

The Company currently operates 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 named 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 wholly owned 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 consolidated financial statements of the Company for the year ended December 31, 2020 were authorized for issue in accordance with a resolution of its Board of Directors on March 19, 2021.

During the year ended December 31, 2020, the Company had a net loss of \$6,725,000 (December 31, 2019: net loss of \$9,316,000), had operating cash flows of \$9,125,000 (December 31, 2019: positive \$10,911,000) and a shareholders' deficiency of \$49,140,000 as of December 31, 2020 (December 31, 2019: \$43,475,000 deficiency) and an accumulated deficit of \$148,919,000 (December 31, 2019: \$142,194,000).

Management assesses the Company's ability to continue as a going concern at each reporting date, using quantitative and qualitative information available. Material uncertainties have been identified which may cast significant doubt upon the Company's ability to continue as a going concern. The Company's ability to continue as a going concern is dependent upon its ability to successfully negotiate extended terms with its creditor, meet financial covenants, achieve improvements in operating results, and mitigate the adverse impact of the COVID-19 virus. In assessing whether the going concern assumption was appropriate, management considered all relevant information available about the future, which is the 12-month period from the date of this report. 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.

Management is actively working to secure extension to its banking agreements, will continue to work with an existing common shareholder, and will seek additional financing, as necessary. The Company cannot provide assurance that, if it needs to raise additional funds, such funds will be available on favorable terms, or at all. If the Company cannot raise adequate funds on acceptable terms, its business could be materially harmed.

The Company, in conjunction with its Board of Directors, is currently implementing various strategies which include:

- The Company is in discussions to extend the maturity of a loan agreement with a Canadian Chartered Bank maturing on June 30, 2021. As of the date of this report, the Company has drawn USD \$60,037,000 (CAD \$76,439,000) of the loan. The Company cannot provide assurance it will be able to extend the maturity date.
- The Company ended the year with bank operating line utilization of \$76,439,000 (USD \$60,037,000) offset by \$7,044,000 cash compared to utilization of \$84,661,000 (USD \$65,184,000) with \$4,316,000 cash on hand as of December 31, 2019. The balance of the net loss and related adjustments on modification of bank indebtedness as a result of executing an amending agreement in 2019 was \$269,000 as at December 31, 2020 (December 31, 2019 \$809,000). As at the date of this report the Company is able to draw up to an additional \$20,000 (USD \$16,000) on its operating line of credit.
- The loan agreement with a Canadian Chartered Bank has certain financial covenants. The Company cannot provide assurance it will be able to meet the financial metrics going forward. The Company may seek a waiver or amendment to the loan agreement as described in the loan agreement, if an event of default is to occur. The financial covenants may also be cured by drawing additional funds from the non-revolving standby facility secured on March 12, 2021 with Panta Canada B.V.
- On March 12, 2021, the Company entered into a multiparty amended and restated Accommodation Agreement with each of a customer, and Panta Canada B.V. whereby, inter alia;
  - Panta Canada B.V. has agreed to provide a USD \$10,000,000 non-revolving standby loan facility and a USD \$3,000,000 equipment loan for an aggregate availability of USD \$13,000,000; and
  - The elimination of unamortized cash advance, mutual release and forgiveness of certain historic and future guarantee fees payable to the customer. As at December 31, 2020, the guarantee fee is \$8,178,000 (USD \$6,423,000), the customer advance is \$5,911,000 (USD \$4,643,000) and the legal claim is \$7,130,000 (USD \$5,600,000).

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

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

- On April 28, 2020, the Company received a loan in the amount of USD \$4,123,000 to support Avcorp Composite Fabrication Inc ("ACF") from a U.S. Chartered Bank through the U.S. Small Business Administration Paycheck Protection Program. The Company has recognized a forgiveness of USD \$3,430,000 in 2020 as the Company has satisfied the requirements of loan forgiveness. On March 9, 2021, the Company submitted the application for review to receive this forgiveness. The remaining loan balance has a term of 2 years and bears interest at a fixed rate of 1% per annum.
- On March 15, 2021, the Company received a second wave U.S. Small Business Administration Paycheck Protection Program loan in the amount of USD \$2,000,000.
- Close collaboration with customers has resulted in both financial and operational support for continued operations.

The assessment of the Company's ability to execute its strategy of reducing operating costs, and ability to mitigate the risk of the COVID-19 virus involves significant judgement. Estimates and assumptions regarding future operating costs, revenue and profitability levels and general business and customer conditions are continually evaluated and are based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances.

**Impact of COVID-19**

In March 2020, the World Health Organization ("WHO") declared coronavirus ("COVID-19") a global pandemic. Governments worldwide enacted emergency measures including travel bans, social distancing measures and mandatory quarantine requirements. The measures have negatively impacted the global economy and adversely impacted the aviation industry worldwide particularly in the commercial airline industry. Based on management's best estimate, the significant decrease in air travel resulting from the COVID-19 pandemic is adversely affecting Avcorp's customers and their demand for the Company's products. The situation remains dynamic and the ultimate duration and magnitude of the impact on the economy and the financial effect on the Company remains unknown at this time.

The Company has implemented measures to align its cost structure and maximize cash preservation during the current market conditions, including headcount reductions to ensure that it emerges from the current crisis on solid footing. The Company also applied and received the Canada Emergency Wage Subsidy for its Canadian operations and support as part of Paycheck Protection Plan for its U.S. operations. On a consolidated basis, the COVID-19 pandemic had a material negative impact on free cash flow for the full year due to lower revenue.

**2. Basis of Preparation and Measurement**

The consolidated financial statements of the Company have been prepared in accordance with International Financial Reporting Standards ("IFRS").

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

**Amendments to IAS 1: Classification of Liabilities as Current or Non-Current**

In January 2020, the IASB issued Classification of Liabilities as Current or Non-current (Amendments to IAS 1). The amendments aim to promote consistency in applying the requirements by helping companies determine whether, in the statement of financial position, debt and other liabilities with an uncertain settlement date should be classified as current (due or potentially due to be settled within one year) or non-current. The amendments include clarifying the classification requirements for debt a company might settle by converting it into equity. The amendments are effective for annual reporting periods beginning on or after January 1, 2023, with earlier application permitted. The Company is currently assessing the impact and the timing to adopt this amendment.

**Amendments to IAS 37: Onerous Contracts – Costs of Fulfilling a contract**

In May 2020, the IASB issued amendments to IAS 37 to specify which costs an entity needs to include when assessing whether a contract is onerous or loss-making.

The amendments apply a "directly related cost approach". The costs that relate directly to a contract to provide goods or services include both incremental costs and an allocation of costs directly related to contract activities. General and administrative costs do not relate directly to a contract and are excluded unless they are explicitly chargeable to the counterparty under the contract.

The amendments are effective for annual reporting periods beginning on or after 1 January 2022, with earlier application permitted. The Company is currently assessing the impact and the timing to adopt this amendment.

### 3. Significant Accounting Policies

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

#### **Basis of consolidation**

The financial statements of the Company consolidate the accounts of Avcorp Industries Inc. and its subsidiaries Comtek Advanced Structures Ltd., Avcorp US Holdings Inc., and Avcorp Composite Fabrication Inc. (the "Group"). All material intercompany transactions, balances and unrealized gains and losses from intercompany transactions are eliminated on consolidation.

The consolidated financial statements comprise the financial statements of the Group and its subsidiaries as at December 31, 2020. Control is achieved when the Group is exposed, or has rights, to variable returns from its involvement with the investee and has the ability to affect those returns through its power over the investee. Specifically, the Group controls an investee if, and only if, the Group has:

- Power over the investee (i.e. existing rights that give it the current ability to direct the relevant activities of the investee);
- Exposure, or rights, to variable returns from its involvement with the investee; and
- The ability to use its power over the investee to affect its returns.

Generally, there is a presumption that a majority of voting rights result in control. Consolidation of a subsidiary begins when the Group obtains control over the subsidiary and ceases when the Group loses control of the subsidiary. Assets, liabilities, income and expenses of a subsidiary acquired or disposed of during the year are included in the consolidated financial statements from the date the Group gains control until the date the Group ceases to control the subsidiary.

When necessary, adjustments are made to the financial statements of subsidiaries to bring their accounting policies into line with the Group's accounting policies. All intra-group assets and liabilities, equity, income, expenses and cash flows relating to transactions between members of the Group are eliminated in full on consolidation.

#### **Business combinations**

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the aggregate of the consideration transferred, which is measured at acquisition date fair value. Acquisition-related costs are expensed as incurred and included in administrative expenses.

#### **Foreign currency translation**

- Functional and presentation currency: Foreign currency items included in the consolidated financial statements of each consolidated entity in the Avcorp Industries Inc. group are measured using the currency of the primary economic environment in which the entity operates (the "functional currency"). The consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency. The functional currency of the Company's subsidiaries, Comtek, is also determined to be Canadian dollars. The functional currency of the Company's subsidiaries, Avcorp US Holdings Inc., and ACF is determined to be US dollars.
- On consolidation, the assets and liabilities of foreign operations are translated into Canadian dollars at the rate of exchange prevailing at the reporting date and their statements of income are translated at average exchange rates prevailing during the period. The exchange differences arising on translation for consolidation are recognized in other comprehensive income ("OCI"). On disposal of a foreign operation, the component of OCI relating to that particular foreign operation is reclassified to consolidated income.
- Any goodwill arising on the acquisition of a foreign operation and any fair value adjustments to the carrying amounts of assets and liabilities arising on the acquisition are treated as assets and liabilities of the foreign operation and translated at the spot rate of exchange at the reporting date.
- Transactions and balances: Foreign currency transactions are translated into the functional currency using the exchange rates prevailing at the dates of the transactions. Generally, foreign exchange gains and losses resulting from the settlement of foreign currency transactions and from the translation at period-end exchange rates of monetary assets and liabilities denominated in currencies other than an operation's functional currency are recognized in the consolidated statements of income.

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

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**Fair value measurement**

Fair value is defined as the exchange price that would be received for an asset or paid to transfer a liability in the principal or most advantageous market for the asset or liability in an orderly transaction between market participants on the measurement date. When determining fair value measurements for assets and liabilities required to be recorded at fair value, the Company considers the principal or most advantageous market in which it would transact and also considers assumptions that market participants would use when pricing an asset or liability. The fair value hierarchy has three levels of inputs that may be used to measure fair value: Level 1—Unadjusted quoted prices in active markets for identical assets or liabilities; Level 2—Unadjusted quoted prices in active markets for similar assets or liabilities, or unadjusted quoted prices for identical or similar assets or liabilities in markets that are not active, or inputs other than quoted prices that are observable for the asset or liability; and Level 3—Unobservable inputs for the asset or liability.

**Financial instruments**

## a) Financial assets

Financial assets include, in particular, cash, accounts receivables and equity investments.

Financial assets are classified, at initial recognition, as subsequently measured at amortized cost, fair value through other comprehensive income, and fair value through profit or loss. The classification of financial assets at initial recognition depends on the financial asset's contractual cash flow characteristics. With the exception of accounts receivables that do not contain a significant financing component or for which the Company has applied the practical expedient, the Company initially measures a financial asset at its fair value plus, in the case of a financial asset not at fair value through profit or loss, transaction costs. Accounts receivables that do not contain a significant financing component or for which the Company has applied the practical expedient are measured at the transaction price determined under IFRS 15. Refer to the accounting policies for Revenue from contracts with customers.

The Company measures financial assets at amortized cost if the financial asset is held within a business model with the objective to hold financial assets in order to collect contractual cash flows and the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding. Financial assets at amortized cost are subsequently measured using the effective interest method and are subject to impairment. Gains and losses are recognized in profit or loss when the asset is derecognized, modified or impaired.

The Company's financial assets at amortized cost includes accounts receivables.

The Company recognizes an allowance for expected credit losses (ECLs) for all debt instruments not held at fair value through profit or loss. ECLs are based on the difference between the contractual cash flows due in accordance with the contract and all the cash flows that the Company expects to receive, discounted at an approximation of the original effective interest rate. The expected cash flows will include cash flows from the sale of collateral held or other credit enhancements that are integral to the contractual terms. For accounts receivables and contract assets, the Company applies a simplified approach in calculating ECLs. Therefore, the Company does not track changes in credit risk, but instead recognizes a loss allowance based on lifetime ECLs at each reporting date.

The Company has established a provision matrix that is based on its historical credit loss experience, adjusted for forward-looking factors specific to the debtors and the economic environment. The provision for ECL rates is based on days past due for groupings of various customer segments that have similar loss patterns (i.e., by customer type and rating). The assessment of the correlation between historical credit loss pattern, forecast economic conditions and ECLs is a significant estimate. The amount of ECLs is sensitive to changes in circumstances and of forecast economic conditions. The Company's historical credit loss experience and forecast of economic conditions may also not be representative of customer's actual default in the future.

Equity investments in non-listed companies are classified and measured as equity instruments at fair value through profit or loss.

## b) Financial liabilities

Financial liabilities often entitle the holder to return the instrument to the issuer in return for cash or another financial asset. These include the bank indebtedness, accounts payables, finance lease liabilities, customer advance, guarantee fee, and term debt.

Financial liabilities are measured at their fair value at the time of acquisition, which is normally equivalent to the net loan proceeds. Transaction costs directly attributable to the acquisition are deducted from the amount of all financial liabilities that are not measured at fair value through profit or loss subsequent to initial recognition. If a financial liability is interest free or bears interest at below the market rate, it is recognized based on market interest rate for a similar financial liability. The financial liability initially recognized at fair value is amortized subsequent to initial recognition using the effective interest method.

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

**Inventories**

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

**Property, Plant and Equipment**

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

An estimation is made of the useful life of property, plant and equipment. The useful life is measured in terms of years of production, and depreciated on a straight line basis.

|                                |                          |
|--------------------------------|--------------------------|
| Computer hardware and software | 2 - 10 years             |
| Machinery and equipment        | 5 - 15 years             |
| Leasehold improvements         | end of leases up to 2028 |

The Company allocates the amount initially recognized in respect of an item of property, plant and equipment to its significant parts and depreciates separately each such part. The useful lives of the assets are reviewed annually and adjusted if appropriate. The amortization expense in property, plant and equipment is recognized in the consolidated statement of loss in the expense category that is consistent with the function of the property, plant, and equipment.

**Intangible Assets**

Intangible assets acquired separately are measured on initial recognition at cost. The cost of intangible assets acquired in a business combination is their fair value at the date of acquisition. Following initial recognition, intangible assets are carried at cost less any accumulated amortization and accumulated impairment losses. Internally generated intangibles, excluding capitalized development costs, are not capitalized and the related expenditure is reflected in profit or loss in the period in which the expenditure is incurred.

Intangible assets with finite lives are amortized over the useful economic life and assessed for impairment whenever there is an indication that the intangible asset may be impaired. The amortization period and the amortization method for an intangible asset with a finite useful life are reviewed at least at the end of each reporting period. Changes in the expected useful life or the expected pattern of consumption of future economic benefits embodied in the asset are considered to modify the amortization period or method, as appropriate, and are treated as changes in accounting estimates. The amortization expense on intangible assets with finite lives is recognized in the profit or loss in the expense category that is consistent with the function of the intangible assets.

**Research and development costs**

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

**Segment Reporting**

Management has determined the operating segments based on information regularly reviewed for the purposes of decision making, allocating resources, and assessing performance by the Company’s chief operating decision maker; the Chief Executive Officer (CEO). The Company evaluates the financial performance of its operating segments primarily based on operating income or loss.

**Impairment of non-financial assets**

The Company assesses at each reporting date, whether there is an indication that an asset may be impaired. If any indication exists, or when annual impairment testing for an asset is required, the Company estimates the asset’s recoverable amount. An asset’s recoverable amount is the higher of an asset’s or cash generating units (“CGU”) fair value less costs of disposal and its value in use. The Company’s CGUs are ASI, Comtek, and ACF. The recoverable amount is determined for an individual asset, unless the asset does not generate cash inflows that are largely independent of those from other assets or groups of assets.

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

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When the carrying amount of an asset or CGU exceeds its recoverable amount, the asset is considered impaired and is written down to its recoverable amount.

In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. In determining fair value less costs of disposal, recent market transactions are taken into account. If no such transactions can be identified, an appropriate valuation model is used. These calculations are corroborated by valuation multiples, quoted share prices for publicly traded companies or other available fair value indicators.

The Company bases its impairment calculation on detailed budgets and forecast calculations, which are prepared separately for each of the Company's CGUs to which the individual assets are allocated. These budgets and forecast calculations generally cover a period of five years. A long-term growth rate is calculated and applied to project future cash flows after the fifth year.

An assessment is made at each reporting date to determine whether there is an indication that previously recognized impairment losses no longer exist or have decreased. If such indication exists, the Company estimates the asset's or CGU's recoverable amount. A previously recognized impairment loss is reversed only if there has been a change in the assumptions used to determine the asset's recoverable amount since the last impairment loss was recognized. The reversal is limited so that the carrying amount of the asset does not exceed its recoverable amount, nor exceed the carrying amount that would have been determined, net of depreciation, had no impairment loss been recognized for the asset in prior years. Such reversal is recognized in the statement of profit or loss unless the asset is carried at a revalued amount, in which case, the reversal is treated as a revaluation increase.

**Employee benefits**

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

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

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

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

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

**Revenue**

The Company's major revenue streams arise from the production and supply of major airframe structures and aircraft parts to aircraft manufacturers, the repair of aircraft components, aircraft product design and production tooling design and manufacture.

Revenue is recognized either at a point in time or over time, as the Company satisfies performance obligations by transferring the promised goods or services to its customers. An asset is transferred as the customer obtains control of the asset. If a performance obligation is not satisfied over time, the Company satisfies the performance obligation at a point in time.

The Company transfers control of a good or service over time and, therefore, satisfies a performance obligation and recognizes revenue over time, if one of the following criteria is met:

- the customer simultaneously receives and consumes the benefits provided by the Company's performance as the Company performs;
- the Company's performance creates or enhances an asset (for example, work in progress) that the customer controls as the asset is created or enhanced; or
- the Company's performance does not create an asset with an alternative use to the Company and the Company has an enforceable right to payment for performance completed to date.

The Company transfers control of the goods over time as evidenced either by contractual termination clauses or by our rights to payment for work performed to date plus a reasonable profit to deliver products that do not have an alternative use to the Company. The Company uses the input method to measure the satisfaction of performance obligations over time. The inputs are labour hours expended and cost of materials consumed relative to the total expected inputs to the satisfaction of that performance obligation.

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

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Determining whether a contract transfers control of the goods over time requires management to consider the terms of the contract, as well as any laws that apply to the contract, and make judgements as to (1) whether the asset created by the Company's performance does not have an alternative use to the Company if the Company is either restricted contractually from readily directing the asset for another use during the creation or enhancement of that asset or limited practically from readily directing the asset in its completed state for another use and (2) evaluating whether it has an enforceable right to payment for performance completed to date.

The Company transfers control of the goods at a point in time when the goods are delivered to the customers.

Revenue is measured based on the price specified in the sales contract.

Contract Assets include unbilled amounts typically resulting from sales under purchase orders and long-term contracts when over time method of revenue recognition is utilized and revenue recognized exceeds the amount billed to the customer, and right to payment is not just subject to passage of time. Amounts may not exceed their net realizable value. Contract assets are current in nature.

Contract liabilities consist of advance payments and billings in excess of revenue recognized. Advance payments and billings in excess of revenue recognized are classified as current or non-current based on the timing of when revenue is expected to be recognized. This period of contract liabilities realization can extend, dependent on the amortization of the related costs, over one or more fiscal years. Certain program inventories have been funded by a customer, whereby the associated contract liability will be recorded as revenue upon delivery of units of production.

The Company's customer contracts with the U.S. government are subject to the Federal Acquisition Regulation ("FAR") and are competitively priced based on estimated costs of providing the contractual goods or services. The U.S. Government or the prime contractor may cancel any contract at any time through a termination for convenience or for cause. Many of our contracts have terms that create an enforceable right to payment for performance completed to date in the event of a termination for convenience. Variable consideration is estimated as the most likely amount to which we expect to be entitled and is recognized to the extent it is probable that a significant reversal will not occur when the uncertainty associated with the variable consideration is subsequently resolved.

**Cost of sales**

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

**Income tax****a) Current income tax**

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

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

**b) Deferred income tax**

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

Deferred income tax liabilities are not recognized for taxable temporary differences associated with investments in subsidiaries, when the timing of the reversal of the temporary differences can be controlled and it is probable that the temporary differences will not reverse in the foreseeable future.

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

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

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

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

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

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

**Capital Stock**

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

**Earnings per share**

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

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

**Lease****Right-of-use assets**

The Company recognizes right-of-use assets at the commencement date of the lease. Right-of-use assets are measured at cost, less any accumulated depreciation and impairment losses, and adjusted for any re-measurement of lease liabilities. The cost of right-of-use assets includes the amount of lease liabilities recognized, initial direct costs incurred, and lease payments made at or before the commencement date less any lease incentives received. Unless the Company is reasonably certain to obtain ownership of the leased asset at the end of the lease term, the recognized right-of-use assets are depreciated on a straight-line basis over the shorter of its estimated useful life and the lease term. Right-of-use assets are subject to impairment.

**Lease liabilities**

At the commencement date of the lease, the Company recognizes lease liabilities measured at the present value of lease payments to be made over the lease term. The lease payments include fixed payments (including in-substance fixed payments) less any lease incentives receivable, variable lease payments that depend on an index or a rate, and amounts expected to be paid under residual value guarantees. The lease payments also include the exercise price of a purchase option reasonably certain to be exercised by the Company and payments of penalties for terminating a lease, if the lease term reflects the Company exercising the option to terminate. The variable lease payments that do not depend on an index or a rate are recognized as expense in the period on which the event or condition that triggers the payment occurs.

In calculating the present value of lease payments, the Company uses the incremental borrowing rate at the lease commencement date if the interest rate implicit in the lease is not readily determinable. The incremental borrowing rate is the rate of interest that the Company would have to pay to borrow over a similar term, and with a similar security, the funds necessary to obtain an asset of a similar value to the lease asset in a similar economic environment. After the commencement date, the amount of lease liabilities is increased to reflect the accretion of interest and reduced for the lease payments made. In addition, the carrying amount of lease liabilities is re-measured if there is a modification, a change in the lease term, a change in the in-substance fixed lease payments or a change in the assessment to purchase the underlying asset.

**Short-term leases and leases of low-value assets**

The Company applies the short-term lease recognition exemption to its short-term leases that have a lease term of 12 months or less from the commencement date and do not contain a purchase option. It also applies the lease of low-value assets recognition exemption to leases of assets that are considered of low value. Lease payments on short-term leases and leases of low-value assets are recognized as expense on a straight-line basis over the lease term.

**Significant judgement in determining the lease term of contracts with renewal options**

The Company determines the lease term as the non-cancellable term of the lease, together with any periods covered by an option to extend the lease if it is reasonably certain to be exercised, or any periods covered by an option to terminate the lease, if it is reasonably certain not to be exercised. The Company considers all relevant factors that create an economic incentive for it to exercise the renewal. After the commencement date, the Company reassesses the lease term if there is a significant event or change in circumstances that is within its control and affects its ability to exercise (or not to exercise) the option to renew.



**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

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**Government grants**

The Company recognized government grant income related to the Canada Emergency Wage Subsidy and the U.S. Small Business Administration Paycheck Protection Program loan when there is reasonable assurance that the Company will comply with eligibility requirements and the grants will be received. The Company has recognized deferred government grant on wages capitalized as inventory. The deferred government grant will be recognized as income upon sale of the inventory.

**4. Critical Accounting Estimates and Judgements**

The preparation of consolidated financial statements in conformity with IFRS requires management to make estimates and judgments that affect the amounts which are reported in the consolidated financial statements during the reporting period. Estimates and other judgments are evaluated at each reporting date and are based on management's experience and other factors, including expectations about future events that are believed to be reasonable under the circumstances. Any changes in estimates and assumptions could have a material impact on the assets and liabilities at the date of the statement of financial position. The Company reviews its estimates and assumptions on an ongoing basis and uses the most current information available and exercises careful judgement in making these estimates and assumptions.

- **Functional currency:** The functional currency for the Company and its subsidiaries is the currency of the primary economic environment in which each operates. The Company has determined that the functional currency for the Company and all its subsidiaries except for Avcorp US Holdings Inc. and ACF is the Canadian dollar. The functional currency for Avcorp US Holdings Inc. and ACF is the US dollar. The determination of functional currency may require certain judgements to determine the primary economic environment. The Company reconsiders the functional currency used when there is a change in events and conditions which determined the primary economic environment.
- **Impairments:** The recoverable amount of intangible assets, development costs and property, plant and equipment are based on estimates and assumptions regarding the expected market outlook and cash flows from each of the Company's CGU. Assumptions, judgments and estimates about future values are complex and often subjective. They can be affected by a variety of factors, including external factors such as industry and economic trends, and internal factors such as changes in the Company's business strategy or internal forecasts. Although the Company believes the assumptions, judgments and estimates made in the past have been reasonable and appropriate, different assumptions, judgments and estimates could materially affect the Company's reported financial results.
- **Going concern and debt classification:** Management assesses the Company's ability to continue as a going concern at each reporting date, using quantitative and qualitative information available. Management also determines the appropriate classification of its debt arrangements based on terms of the various agreements based on the Company's financial condition. 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.
- **Capitalization of development costs:** When capitalizing development costs the Company must assess the technical and commercial feasibility of the projects and estimate the useful lives of resulting products. Determining whether future economic benefits will flow from the assets and therefore the estimates and assumptions associated with these calculations are instrumental in (i) deciding whether project costs can be capitalized, and (ii) accurately calculating the useful life of the projects for the Company. A change in estimate of the amortization period occurred for a contract that received a termination of convenience, an accelerated amortization of \$7,469,000 was recognized in the year ended December 31, 2020.
- **Inventories are valued at the lower of cost and net realizable value.** The costs of inventory involve estimates in determining the allocation of fixed and variable production overhead. These estimates involved include determination of normal production capacity and nature of expenses to be allocated.
- **On a periodic basis the Company reviews its plant capacity and estimates the portion of its under-utilized overhead expenditures.** The Company has expensed \$8,346,000 of overhead costs during the current year (December 31, 2019: \$7,004,000) in respect of unutilized plant capacity. These amounts are included in the Consolidated Statements of Loss and Comprehensive Loss as costs of sales.
- **The Company has entered into production contracts in the ordinary course of its business.** The unavoidable cost of meeting the obligations under certain of these contracts exceeds the associated expected future net benefits; consequently, an onerous contract provision has been recognized. The calculation of this provision involves the use of estimates including, but not limited to, program gross margin, and the effect of learning curves of production and the timing of achieving certain operational efficiencies. These actual results can vary significantly from these estimates with consequent variability in the amounts of the provision recorded. The onerous contract provision is calculated by taking the expected future costs that will be incurred under the contract and deducting any estimated revenues. The onerous contract provision is primarily due to a high cost structure and learning curves of production that cannot be recovered through current pricing of the associated contracts. The total onerous contract provision for the year ended December 31, 2020 is \$565,000 (December 31, 2019: \$251,000).

**Notes to Consolidated Financial Statements  
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*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

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- While a formal claim has not been levied by the customer, the Company has provisioned for a claim asserted by a customer in the amount of \$7,130,000 (USD \$5,600,000) as at December 31, 2020 (December 31, 2019: \$7,273,000 (USD \$5,600,000)). Subsequent to year end on March 12, 2021, the Company has amended and restated the accommodation agreement with customer and Panta B.V. Canada providing a mutual release and settlement on all claims.
- Values of right of use assets and lease liabilities require judgement in determining lease terms such as extension option and discount rate used. In the case where incremental borrowing rate is used, the Company estimates the incremental borrowing rate based on the lease term, collateral assumptions, and the economic environment in which the lease is denominated.
- The Company has provisioned USD \$1,350,000 (December 31, 2019: USD \$1,350,000) for a legal action due to certain employment practices at the Gardena facility.
- Upon termination for convenience for customer contracts subject to the Federal Acquisition Regulation ("FAR"), the Company must assess the contractual provisions that permit termination and the related contractual remedies available to recover all or a portion of our incurred costs and fees for work performed. Variable consideration is recognized as estimated revenue to the extent it is probable that a significant reversal in the amount of revenue recognized will not occur when the uncertainty associated with the variable consideration is subsequently resolved. Management estimated the variable consideration using actual costs, an estimate of reasonable profit margin determined in accordance with the contractual provisions and historical experience, and delay cost estimated under the contractual entitlement subject to FAR. Although the Company believes its estimates and assumptions made are consistent with the terms and conditions of the contract, the actual settlement amount determined at a future date could materially affect the Company's reported financial results.
- The Company has determined that it will meet the eligibility requirements for the Canada Emergency Wage Subsidies not yet received and has estimated the amounts recognized as other income and deferred government grant to be \$2,031,000 and \$657,000 respectively in the current year.
- The Company has determined that it will meet the eligibility requirements for partial forgiveness of the U.S. Small Business Administration Paycheck Protection Program loan and has recognized \$4,601,000 (USD \$3,430,000) in other income in the current year.

## Notes to Consolidated Financial Statements For the year ended December 31, 2020

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

### 5. Expenses by Nature

The Consolidated Statements of Loss and Comprehensive Loss presents expenses by function. Accordingly, amortization and depreciation is not presented as a separate line on the statement (with the exception of office equipment), but is included within cost of sales to the extent that it relates to manufacturing machinery and equipment, right of use assets or leasehold improvements.

Expenses by nature:

|  | 2020            | 2019     |
|--|-----------------|----------|
| Raw materials, purchased parts and consumables     | <b>\$65,028</b> | \$84,377 |
| Salary, wages, and benefits                        | <b>59,117</b>   | 68,816   |
| Amortization of development costs                  | <b>8,955</b>    | 1,786    |
| Depreciation                                       | <b>8,338</b>    | 8,218    |
| Contract services & consulting                     | <b>3,606</b>    | 4,605    |
| Utilities  | <b>3,491</b>    | 3,592    |
| Transportation                                     | <b>1,926</b>    | 2,273    |
| Office equipment rental and maintenance            | <b>1,867</b>    | 1,837    |
| Other expenses and conversion costs into inventory | <b>1,537</b>    | 1,481    |
| Rent   | <b>1,514</b>    | 1,893    |
| Legal and audit fees                               | <b>1,509</b>    | 2,382    |
| Amortization of intangible assets                  | <b>1,197</b>    | 1,184    |
| Plant equipment rental and maintenance             | <b>900</b>      | 892      |
| Insurance  | <b>664</b>      | 606      |
| Change in onerous contracts provision              | <b>308</b>      | (1,665)  |
| Travel costs                                       | <b>203</b>      | 733      |
| Office supplies                                    | <b>171</b>      | 188      |
| Royalties  | <b>159</b>      | 193      |
| Bad debt recovery                                  | <b>(257)</b>    | (172)    |
|  | <b>160,233</b>  | 183,219  |

### 6. Capital Risk Management

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

The Company includes capital stock in its definition of capital, as shown in the Company's consolidated statements of financial position.

The Company's primary objective in its management of capital is to ensure that it has sufficient financial resources to fund ongoing operations and new program investment. In order to secure this capital, the Company may attempt to raise funds via issuance of debt and equity, or by securing strategic partners.

The Company's loan agreement with a Canadian Chartered Bank restricts the declaration or payment of any dividend.

### 7. Financial Risk Management

The Company is exposed to certain financial risks including market risk, currency risk, credit risk, liquidity risk, interest rate risk and price risk. The note presents information about the Company's risk to each of these risks; its objectives, policies and processes for measuring and managing risk.

#### a) Market Risk

Market risk is the risk that changes in the market prices, such as foreign exchange rates and interest rates, will affect the Company's income or the value of its holdings of financial instruments. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes. The Company may utilize derivative instruments in the management of its foreign currency and interest rate exposures.

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

b) Currency Risk

Currency risk arises because the amount of the local currency receivable or payable for transactions denominated in foreign currencies may vary due to changes in exchange rate ("transaction exposures") and because the non-Canadian dollar denominated financial statements of the Company's subsidiaries may vary on consolidation into the reporting currency of Canadian dollars ("translation exposures").

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 components in US dollars at prices that are usually established at the order date. 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 for the year ended December 31, 2020 is \$364,000 (December 31, 2019: \$843,000 gain).

The Company had the following US dollar denominated balances:

| <b>AS AT DECEMBER 31</b> | <b>2020</b>       | 2019       |
|--------------------------|-------------------|------------|
| Bank cash position       | <b>USD\$3,285</b> | USD\$2,639 |
| Accounts receivable      | <b>6,393</b>      | 9,824      |
| Accounts payable         | <b>3,726</b>      | 6,948      |
| Customer advance         | <b>4,643</b>      | 4,643      |
| Bank indebtedness        | <b>60,037</b>     | 65,184     |
| Term loan                | <b>10,322</b>     | 4,273      |

With other variables unchanged, each \$0.10 strengthening (weakening) of the CAD against the USD would result in an increase (decrease) of approximately \$6,905,000 in net income for the year ended December 31, 2020 as a result of holding a net liability position in USD as at December 31, 2020.

As at December 31, 2019, a \$0.10 strengthening (weakening) of the CAD against the USD would result in an increase (decrease) of approximately \$6,859,000 in net income for the year ended December 31, 2019 as a result of holding a net liability position in USD as at December 31, 2019.

c) 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 Defence, Space & Security ("BDS"), Bombardier Aerospace ("Bombardier"), BAE Systems (Operations) Limited ("BAE"), Lockheed Martin ("LM"), and Subaru Corporation ("Subaru"). The maximum exposure to credit risk is represented by the amount of accounts receivable in the consolidated statements of financial position.

As at the consolidated statements of financial position date 89.6% (December 31, 2019: 85.6%) of the Company's trade accounts receivable are attributable to these customers.

The Company is exposed to credit risk if counterparties to its trade receivables are unable to meet their obligations. The concentration of credit risk from its customers is minimized because the Company has an original equipment manufacturer and tier one aerospace customer base as at December 31, 2020. The customers are predominately large, well-capitalized, and long-established entities with a low risk of non-payment. The Company regularly monitors its credit risk and credit exposure.

The following table provides the change in allowance for doubtful accounts for trade receivables:

| <b>FOR THE YEAR ENDED DECEMBER 31</b> | <b>2020</b>  | 2019    |
|---------------------------------------|--------------|---------|
| Balance as at January 1               | <b>\$355</b> | \$1,780 |
| Additions                             | <b>36</b>    | 336     |
| Use                                   | <b>(42)</b>  | (16)    |
| Collection                            | <b>(320)</b> | (1,745) |
| Balance as at December 31             | <b>29</b>    | 355     |

## Notes to Consolidated Financial Statements For the year ended December 31, 2020

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

The following table provides aged trade receivables:

| <b>AS AT DECEMBER 31</b> | <b>2020</b>    | 2019            |
|--------------------------|----------------|-----------------|
| Current                  | <b>\$9,531</b> | <b>\$10,221</b> |
| 31 – 60 days             | <b>1,379</b>   | <b>3,507</b>    |
| 61 – 90 days             | <b>1,400</b>   | <b>2,055</b>    |
| Over 90 days             | <b>1,499</b>   | <b>1,137</b>    |
| Total                    | <b>13,809</b>  | <b>16,920</b>   |

### d) 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.

Accounts payable and accrued liabilities are all due within the next twelve months. Term debt repayments are as outlined in note 20.

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

|                                       | <b>December 31, 2020</b>  |                           |                    |                     |
|---------------------------------------|---------------------------|---------------------------|--------------------|---------------------|
|                                       | <b>Less than 3 months</b> | <b>3 months to 1 year</b> | <b>1 – 5 years</b> | <b>Over 5 years</b> |
| Bank indebtedness (note 16)           | \$76,708                  | \$-                       | \$-                | \$-                 |
| Term debt (note 20)                   | 1,205                     | 15,663                    | 13,413             | 5,755               |
| Trade payables (note 18)              | 10,980                    | -                         | -                  | -                   |
| Payroll related liabilities (note 18) | 5,242                     | -                         | -                  | -                   |
| Customer advance (note 17)            | 5,911                     | -                         | -                  | -                   |
| Guarantee fee (note 16)               | -                         | 8,178                     | -                  | -                   |
| Accrued interest (note 18)            | 159                       | -                         | -                  | -                   |
| Other accruals (note 18)              | 216                       | -                         | -                  | -                   |

|                                       | December 31, 2019         |                           |                    |                     |
|---------------------------------------|---------------------------|---------------------------|--------------------|---------------------|
|                                       | <b>Less than 3 months</b> | <b>3 months to 1 year</b> | <b>1 – 5 years</b> | <b>Over 5 years</b> |
| Bank indebtedness (note 16)           | \$85,470                  | \$-                       | \$-                | \$-                 |
| Term debt (note 20)                   | 593                       | 2,175                     | 19,556             | 7,292               |
| Trade payables (note 18)              | 23,201                    | -                         | -                  | -                   |
| Payroll related liabilities (note 18) | 4,952                     | -                         | -                  | -                   |
| Customer advance (note 17)            | 6,030                     | -                         | -                  | -                   |
| Guarantee fee (note 16)               | -                         | -                         | 5,277              | -                   |
| Accrued interest (note 18)            | 356                       | -                         | -                  | -                   |
| Other accruals (note 18)              | 176                       | -                         | -                  | -                   |

### e) Interest Rate Risk

The Company is exposed to interest rate risk on the utilized portion of its operating line of credit.

Interest rate for advances made up to the maximum of the allowable borrowing base of USD \$23,000,000 revolving loan less USD \$2,300,000:

- Royal Bank Prime ("RBP") plus 1.50% per annum
- Royal Bank US Base Rate ("RBUSTR") plus 1.50% per annum
- Banker's Acceptance ("BA") Equivalent Rate plus 3.00% per annum

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

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- LIBOR Rate plus 3.00% per annum

Interest rate for advances made on the additional USD \$45,000,000 borrowing capacity up to USD \$68,000,000.

- RBP plus 0.00% per annum
- RBUSTR plus 0.00% per annum
- BA Equivalent Rate plus 0.875% per annum
- LIBOR Rate plus 0.875% per annum

Drawdown under the USD \$45,000,000 additional borrowing capacity is supported by a Guarantee provided by a Guarantor. Panta Holdings B.V. provided guarantee to the Guarantor in the maximum payment of USD \$10,000,000 if the bank draws on the Guarantee in whole or in part.

The Company will provide the Guarantor, as consideration for the Guarantee, a fee equal to 5.375% of the weighted average outstanding balance of the guaranteed portion over each full twelve (12) month period commencing on the funding date plus, for the partial year thereafter, 5.375% of the weighted average outstanding balance of the guaranteed portion multiplied by the number of days in the partial year divided by three hundred sixty (360). The fee will be payable on the maturity date. Subsequent to year end on March 12, 2021, the Company has amended and restated the accommodation agreement with a customer and Panta B.V. Canada waiving all rights to the Guarantee Fee (note 34).

The maximum operating line of credit availability is \$83,649,000 (USD \$65,700,000) of which \$76,439,000 (USD \$60,037,000) is utilized as at December 31, 2020 (December 31, 2019: \$84,661,000 (USD \$65,184,000)). The Company lowers interest rate costs by managing utilization of the operating lines of credit to the lowest amount practical. For the year ended December 31, 2020, with other variables unchanged, a 1% change in the base borrowing rate would have an \$764,000 (December 31, 2019: \$847,000) impact on net earnings and cash flow. Based on net collateral provided to its bank, the Company is able to draw up to an additional \$1,762,000 (USD \$1,384,000) on its operating line of credit as at December 31, 2020 (December 31, 2019: \$335,000 (USD \$258,000)). As at the date of this report the Company is able to draw up to an additional \$20,000 (USD \$16,000) (note 16) on its operating line of credit.

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

f) Price Risk

Certain of the Company's sales contracts contain derivative financial instruments to reduce exposure to price risk associated with its revenues. The price adjustment clause within these sales contracts was not recorded as it does not produce a significant amount to be recorded.

g) Financial Assets and Liabilities by Category

Categories of financial instruments

Under IFRS 9, financial instruments are classified into one of the following categories: financial assets at fair value through other comprehensive income and fair value through profit and loss, financial liabilities at fair value through profit or loss, and other financial liabilities and financial assets at amortized cost.

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**
*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

As at December 31, 2020 and December 31, 2019, the Company's financial assets and liabilities are categorized as follows:

**AS AT DECEMBER 31**

|                              | 2020           |         | 2019           |         |
|------------------------------|----------------|---------|----------------|---------|
|                              | Amortized cost | Total   | Amortized cost | Total   |
| <b>Financial Assets</b>      |                |         |                |         |
| Cash                         | \$7,044        | \$7,044 | \$4,316        | \$4,316 |
| Accounts receivable          | 14,436         | 14,436  | 17,625         | 17,625  |
| <b>Financial Liabilities</b> |                |         |                |         |
| Bank indebtedness            | 76,708         | 76,708  | 85,470         | 85,470  |
| Accounts payable             | 27,932         | 27,932  | 38,178         | 38,178  |
| Term debt                    | 36,036         | 36,036  | 29,616         | 29,616  |
| Customer advance             | 5,911          | 5,911   | 6,030          | 6,030   |
| Guarantee fee                | 8,178          | 8,178   | 5,277          | 5,277   |

**8. Fair Value Measurement**

As at December 31, 2020 and December 31, 2019, the fair values of cash, accounts receivable, accounts payable, and bank indebtedness approximated their carrying values because of the short-term nature of these instruments.

**AS AT DECEMBER 31**

|                              | 2020           |            | 2019           |            |
|------------------------------|----------------|------------|----------------|------------|
|                              | Carrying value | Fair value | Carrying value | Fair value |
| <b>Financial liabilities</b> |                |            |                |            |
| Term debt (level 2)          | 36,036         | 36,036     | 29,616         | 29,616     |
| Customer advance (level 2)   | 5,911          | 5,911      | 6,030          | 6,030      |
| Guarantee fee (level 2)      | 8,178          | 8,178      | 5,277          | 5,277      |

**Fair value hierarchy**

The Company's financial assets recorded at fair value on the consolidated statements of financial position have been categorized into three categories based on a fair value hierarchy. Fair value of assets and liabilities included in Level 1 are determined by reference to quoted prices in active markets for identical assets and liabilities. Assets and liabilities in Level 2 include valuations using inputs other than the quoted prices for which all significant inputs are based on observable market data, either directly or indirectly. Level 3 valuations are based on inputs that are not based on observable market data.

The fair value hierarchy requires the use of observable market inputs whenever such inputs exist. A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

**9. Accounts Receivable**
**AS AT DECEMBER 31**

|                     | 2020          | 2019          |
|---------------------|---------------|---------------|
| Trade receivables   | \$13,809      | \$16,920      |
| Input tax credits   | 545           | 623           |
| Accrued receivables | 82            | 82            |
|                     | <b>14,436</b> | <b>17,625</b> |

The average trade receivables days outstanding is 33 days as at December 31, 2020 (December 31, 2019: 37 days).

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

The accounts receivables are pledged as security under the Company's operating line of credit (note 16).

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

**AS AT DECEMBER 31**

|                 | <b>2020</b>       | 2019        |
|-----------------|-------------------|-------------|
| US dollar       | <b>USD\$6,813</b> | USD\$10,935 |
| Canadian dollar | <b>5,761</b>      | 3,423       |

**10. Contract Assets**

Contract assets include unbilled amounts typically resulting from sales under purchase orders and long-term contracts when over time method of revenue recognition is utilized and revenue recognized exceeds the amount billed to the customer, and right to payment is not just subject to the passage of time. Amounts may not exceed their net realizable value. Contract Assets are released when the customer is invoiced and is recorded to accounts receivable. Contract assets also include variable consideration recognized upon contract modifications, determined using the most likely amount expected to be entitled. Contract assets are current in nature.

A significant portion of the contract assets are pledged as security under the Company's operating line of credit (note 16).

**AS AT DECEMBER 31**

|                | <b>2020</b>     | 2019     |
|----------------|-----------------|----------|
| Contract asset | <b>\$34,325</b> | \$26,162 |

**11. Inventories**

**AS AT DECEMBER 31**

|                        | <b>2020</b>    | 2019    |
|------------------------|----------------|---------|
| Raw materials          | <b>\$8,296</b> | \$9,222 |
| Work-in-progress       | <b>5,160</b>   | 7,203   |
| Finished products      | <b>216</b>     | 571     |
| Inventory obsolescence | <b>(4,015)</b> | (4,063) |
|                        | <b>9,657</b>   | 12,933  |

The amount of inventory expensed in cost of sales during the year ended December 31, 2020 amounted to \$125,428,000 (December 31, 2019: \$152,192,000).

During the year ended December 31, 2020, \$108,000 (December 31, 2019, \$431,000) was recognized as a reversal of expense for inventories carried at net realizable value. This is recognized in cost of sales. Certain program inventories have been funded by a customer, whereby the associated contract liabilities will be recorded as revenue upon delivery of units of production.

The inventories are pledged as security under the Company's operating line of credit (note 16).



**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**
*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*
**12. Prepayments and Other Assets**
**AS AT DECEMBER 31**

|  | 2020         | 2019  |
|--|--------------|-------|
| Deposits on material purchases               | <b>\$646</b> | \$543 |
| Prepaid insurance                            | <b>3,437</b> | 3,229 |
| Prepaid IT security maintenance and licenses | <b>459</b>   | 190   |
| Prepaid property tax                         | <b>287</b>   | 537   |
| Prepaid other                                | <b>156</b>   | 375   |
|  | <b>4,985</b> | 4,874 |
| Less: Current portion                        | <b>2,108</b> | 2,136 |
| Non-current portion                          | <b>2,877</b> | 2,738 |

**13. Development Costs**

Development costs represent hard and soft tooling, and prototype design costs incurred for various customer programs. Customers have funded non-recurring costs incurred during the introduction of new production programs. These costs are deferred as development costs and are amortized to income in conjunction with the associated production activities, upon commencement of production, on a units-of-production basis over the expected life of the programs. A change in estimate of the amortization period occurred for a contract that received a termination of convenience, this accelerated \$7,469,000 of amortization in the year ended December 31, 2020.

**FOR THE YEAR ENDED DECEMBER 31**

|                  | 2020            | 2019     |
|------------------|-----------------|----------|
| Opening balance  | <b>\$14,075</b> | \$11,755 |
| Additions        | <b>3,929</b>    | 4,116    |
| Amortization     | <b>(8,955)</b>  | (1,786)  |
| Foreign exchange | <b>(4)</b>      | (10)     |
|                  | <b>9,045</b>    | 14,075   |

**FOR THE YEAR ENDED DECEMBER 31**

|                          | 2020            | 2019     |
|--------------------------|-----------------|----------|
| Cost                     | <b>\$30,982</b> | \$27,057 |
| Accumulated amortization | <b>(21,937)</b> | (12,982) |
| Net book amount          | <b>9,045</b>    | 14,075   |

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**
*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*
**14. Property, Plant and Equipment**

|                                      | <b>Building</b> | <b>Machinery and equipment</b> | <b>Computer hardware and software</b> | <b>Leasehold improvements</b> | <b>Total</b>  |
|--------------------------------------|-----------------|--------------------------------|---------------------------------------|-------------------------------|---------------|
| <b>Year ended December 31, 2019</b>  |                 |                                |                                       |                               |               |
| Opening net book amount              | 12,205          | 25,885                         | 2,185                                 | 1,230                         | 41,505        |
| Additions                            | 12,759          | 740                            | 867                                   | 73                            | 14,439        |
| Disposals – cost                     | -               | (587)                          | -                                     | -                             | (587)         |
| Disposals – accumulated depreciation | -               | 377                            | -                                     | -                             | 377           |
| Depreciation charge                  | (3,414)         | (3,967)                        | (615)                                 | (222)                         | (8,218)       |
| Currency translation adjustment      | (225)           | (832)                          | (101)                                 | (30)                          | (1,188)       |
| <b>Closing net book amount</b>       | <b>21,325</b>   | <b>21,616</b>                  | <b>2,336</b>                          | <b>1,051</b>                  | <b>46,328</b> |
| <b>At December 31, 2019</b>          |                 |                                |                                       |                               |               |
| Cost                                 | 24,694          | 59,409                         | 10,709                                | 2,992                         | 97,804        |
| Accumulated depreciation             | (3,369)         | (37,793)                       | (8,373)                               | (1,941)                       | (51,476)      |
| <b>Net book amount</b>               | <b>21,325</b>   | <b>21,616</b>                  | <b>2,336</b>                          | <b>1,051</b>                  | <b>46,328</b> |
| <b>Year ended December 31, 2020</b>  |                 |                                |                                       |                               |               |
| Opening net book amount              | 21,325          | 21,616                         | 2,336                                 | 1,051                         | 46,328        |
| Additions                            | 63              | 928                            | 156                                   | 1,062                         | 2,209         |
| Disposals – cost                     | -               | (1,701)                        | -                                     | (95)                          | (1,796)       |
| Disposals – accumulated depreciation | -               | 574                            | -                                     | 35                            | 609           |
| Depreciation charge                  | (3,515)         | (3,962)                        | (638)                                 | (223)                         | (8,338)       |
| Transfers                            | -               | (139)                          | 47                                    | 92                            | -             |
| Currency translation adjustment      | (153)           | (120)                          | (25)                                  | (11)                          | (309)         |
| <b>Closing net book amount</b>       | <b>17,720</b>   | <b>17,196</b>                  | <b>1,876</b>                          | <b>1,911</b>                  | <b>38,703</b> |
| <b>At December 31, 2020</b>          |                 |                                |                                       |                               |               |
| Cost                                 | 24,511          | 57,994                         | 10,860                                | 4,029                         | 97,394        |
| Accumulated depreciation             | (6,791)         | (40,798)                       | (8,984)                               | (2,118)                       | (58,691)      |
| <b>Net book amount</b>               | <b>17,720</b>   | <b>17,196</b>                  | <b>1,876</b>                          | <b>1,911</b>                  | <b>38,703</b> |

The Company has \$52,000 in commitments at December 31, 2020 (December 31, 2019: \$318,000) to purchase Property, Plant and Equipment in 2021.

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**
*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

The Company leases various assets including buildings, equipment, and computer hardware and software. The following table summarizes the changes in right-of-use assets within Property, plant and equipment:

|                                      | <b>Building</b> | <b>Machinery and equipment</b> | <b>Computer hardware and software</b> | <b>Total</b>  |
|--------------------------------------|-----------------|--------------------------------|---------------------------------------|---------------|
| <b>January 1, 2019</b>               | 12,205          | 1,101                          | 449                                   | 13,755        |
| Additions                            | 12,759          | -                              | 776                                   | 13,535        |
| Depreciation charge                  | (3,471)         | (238)                          | (209)                                 | (3,918)       |
| Currency translation adjustment      | (168)           | (82)                           | (2)                                   | (252)         |
| <b>At December 31, 2019</b>          | <b>21,325</b>   | <b>781</b>                     | <b>1,014</b>                          | <b>23,120</b> |
| <b>January 1, 2020</b>               | 21,325          | 781                            | 1,014                                 | 23,120        |
| Additions                            | 63              | 265                            | 112                                   | 440           |
| Disposals - cost                     | -               | (215)                          | -                                     | (215)         |
| Disposals - accumulated depreciation | -               | 59                             | -                                     | 59            |
| Depreciation charge                  | (3,515)         | (261)                          | (257)                                 | (4,033)       |
| Currency translation adjustment      | (153)           | 57                             | (2)                                   | (98)          |
| <b>At December 31, 2020</b>          | <b>17,720</b>   | <b>686</b>                     | <b>867</b>                            | <b>19,273</b> |

On January 25, 2019, the Company and its subsidiary Avcorp Composite Fabrication Inc. (the "Avcorp Parties") entered into an agreement with HITCO Carbon Composites, Inc., SGL Carbon, LLC, and SGL Carbon SE (the "SGL parties") and a customer to settle all claims related to alleged deficiencies in HITCO's non-destructive inspection processes, a mutual release amount the Avcorp Parties, SGL Parties and a customer and other business matters including a lease renewal (note 26). The Gardena Facility's lease was renewed resulting in the addition of \$12,759,000 to the right-of-use assets. Subsequent to year end on February 25, 2021, the Company and SGL Composites Inc. amended the Gardena Facility's lease agreement effective January 1, 2021 (note 34).

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**
*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*
**15. Intangibles**

|                                     | Lease | Customer<br>contract –<br>re-complete | Developed<br>Software | Total   |
|-------------------------------------|-------|---------------------------------------|-----------------------|---------|
| <b>Year ended December 31, 2019</b> |       |                                       |                       |         |
| Opening net book amount             | -     | 2,238                                 | 899                   | 3,137   |
| Amortization charge                 | -     | (1,088)                               | (96)                  | (1,184) |
| Currency translation adjustment     | -     | (85)                                  | (41)                  | (126)   |
| <b>Closing net book amount</b>      | -     | 1,065                                 | 762                   | 1,827   |
| <b>At December 31, 2019</b>         |       |                                       |                       |         |
| Cost                                | 702   | 5,325                                 | 941                   | 6,968   |
| Accumulated depreciation            | (702) | (4,260)                               | (179)                 | (5,141) |
| <b>Net book amount</b>              | -     | 1,065                                 | 762                   | 1,827   |
| <b>Year ended December 31, 2020</b> |       |                                       |                       |         |
| Opening net book amount             | -     | 1,065                                 | 762                   | 1,827   |
| Amortization charge                 | -     | (1,100)                               | (97)                  | (1,197) |
| Currency translation adjustment     | -     | 35                                    | (10)                  | 25      |
| <b>Closing net book amount</b>      | -     | -                                     | 655                   | 655     |
| <b>At December 31, 2020</b>         |       |                                       |                       |         |
| Cost                                | 688   | 5,219                                 | 922                   | 6,829   |
| Accumulated depreciation            | (688) | (5,219)                               | (267)                 | (6,174) |
| <b>Net book amount</b>              | -     | -                                     | 655                   | 655     |

**16. Bank Indebtedness**

On November 15, 2019, the Company entered into a loan agreement to expand its operating credit facility with a Canadian Chartered Bank. This loan agreement amends, re-states and replaces the loan agreements entered into on September 27, 2012 and subsequently on May 26, 2017. The loan agreement extends the maturity to June 30, 2021. The Company is currently in discussions to extend the maturity date.

- Maximum availability under the Loan agreement cannot exceed USD \$68,000,000 less USD \$2,300,000 until June 30, 2021. USD \$45,000,000 borrowing capacity under the loan agreement is supported by a customer of the Company (the "Guarantor") by way of a guarantee (the "Guarantee"). On November 15, 2019, Panta Holdings B.V., the holding company of Panta Canada B.V. which is Avcorp's majority shareholder, entered into a guarantee agreement with the Guarantor. Pursuant to the guarantee agreement, Panta Holdings B.V. provided guarantee to the Guarantor in the maximum payment of USD \$10,000,000 if the bank draws on the Guarantee in whole or in part.
- Interest rate for advances made up to the maximum of the allowable borrowing base of USD \$23,000,000 revolving loan less USD \$2,300,000:
  - Royal Bank Prime ("RBP") plus 1.50% per annum
  - Royal Bank US Base Rate ("RBUSBR") plus 1.50% per annum
  - Banker's Acceptance ("BA") Equivalent Rate plus 3.00% per annum
  - LIBOR Rate plus 3.00% per annum
- Interest rate for advances made on the additional USD \$45,000,000 borrowing capacity up to USD \$68,000,000.
  - RBP plus 0.00% per annum
  - RBUSBR plus 0.00% per annum
  - BA Equivalent Rate plus 0.875% per annum
  - LIBOR Rate plus 0.875% per annum

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

- Pursuant to the terms of the amending loan agreement, the Company is required to meet certain financial covenants beginning in Q1 2020. In the event that the Company fails to meet the covenants, Panta Holdings B.V. and Panta Canada B.V. shall be entitled to make cash injections for a fiscal quarter by way of loan or equity investment in Avcorp. Such injections will be considered a positive addition to the calculation of the financial metrics for the purposes of determining compliance with the covenants. In addition, the Company will have a cure period measured cumulatively for the failed quarter and the subsequent quarter. There is uncertainty as to the ability of the Company to meet its financial covenants without the additional financial support from Panta Holdings B.V. and Panta Canada B.V.
  - The Company cannot provide assurance it will be able to meet the financial metrics going forward and may seek a waiver or amendment to the loan agreement if an event of default is to occur.
- On February 6, 2020, the Company entered into an amendment to its existing loan agreement with a Canadian Chartered Bank whereby the following amendments were made:
  - The threshold of the financial covenants for the first and second fiscal quarters for the 2020 fiscal year were amended in favor of the Company.
- On April 27, 2020 through to October 30, 2020, the Company entered into multiple extensions to the amendment above to its existing loan agreement with a Canadian Chartered Bank whereby the following amendment was made:
  - The maximum availability under the Loan agreement cannot exceed USD \$68,000,000 less USD \$1,000,000 until December 31, 2020 and thereafter less USD \$2,300,000.

The loan agreement is subject to the existing security agreements with a Canadian Chartered Bank and with its Guarantor. This debt facility is secured by a charge and specific registration over all of the assets of the Company.

The Company will provide the Guarantor, as consideration for the Guarantee, a fee equal to 5.375% of the weighted average outstanding balance of the guaranteed portion over each full twelve (12) month period commencing on the funding date plus, for the partial year thereafter, 5.375% of the weighted average outstanding balance of the guaranteed portion multiplied by the number of days in the partial year divided by three hundred sixty (360). The fee will be payable on the maturity date of the outstanding loan balance. Subsequent to year end on Mar 12, 2021, the Company has amended and restated the accommodation agreement with a customer and Panta B.V. Canada waiving all rights to the Guarantee Fee (note 34).

The Company ended the year with bank operating line utilization of \$76,439,000 (USD \$60,037,000) offset by \$7,044,000 cash compared to utilization of \$84,661,000 (USD \$65,184,000) with \$4,316,000 cash on hand as at December 31, 2019. The balance of the net loss and related adjustments on modification of bank indebtedness as a result of executing an amending agreement in 2019 was \$269,000 as at December 31, 2020 (December 31, 2019 \$809,000). Based on net collateral provided to its bank, the Company is able to draw up to an additional \$1,762,000 (USD \$1,384,000) on its operating line of credit as at December 31, 2020 (December 31, 2019: \$335,000 (USD \$258,000)).

**FOR THE YEAR ENDED DECEMBER 31**

|  | <b>2020</b>     | 2019     |
|--|-----------------|----------|
| Opening balance                                      | <b>\$85,470</b> | \$85,840 |
| Drawdowns on bank indebtedness                       | <b>653</b>      | 20,844   |
| (Amortization)/Recognition of loan modification loss | <b>(540)</b>    | 906      |
| Repayment of loans                                   | <b>(7,368)</b>  | (18,010) |
| Foreign exchange gain                                | <b>(1,507)</b>  | (4,110)  |
| Ending balance                                       | <b>76,708</b>   | 85,470   |

The carrying amount of accounts receivable pledged as security under the Company’s operating line of credit as at December 31, 2020 is \$8,605,000 (December 31, 2019: \$13,121,000). The inventory and contract asset pledged as security under the Company’s operating line of credit as at December 31, 2020 is \$20,306,000 (December 31, 2019: \$22,185,000).

**17. Customer advance**

On December 18, 2015, in conjunction with the acquisition of Hitco, the Company assumed a customer advance for pre-funded product deliveries. The customer advance is re-paid as the Company delivers to the customer. In the event that cancellation, termination, or assignment of the statement of work occurs earlier than December 31, 2018, the customer shall have the right to recover from the Company within 120 days of such an event the unamortized portion of the cash advance; such event occurred during the third quarter 2018. The customer advance is subject to an access and security agreement along with a general security agreement entered into with the Company’s bank and a customer.

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**
*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

Uncertainties exist as to the ultimate outcome of a formal contract termination. While the Company believes that it has fulfilled all of its obligations under the contract, it is possible claims may be levied against the Company. The Company has assessed such possible claims as not probable.

The Company amortized into revenue \$Nil of the customer advance during the year ended December 31, 2020. The remaining unamortized customer advance has been recorded at its face value to reflect the amount due and is non-interest bearing. The face value of the unamortized portion of the customer advance as at December 31, 2020 is USD \$4,643,000 (December 31, 2019 is USD \$4,643,000).

Subsequent to year end on March 12, 2021, the Company has amended and restated the accommodation agreement with a customer and Panta B.V. Canada settling and waiving all rights to the customer advance (note 34).

**FOR THE YEAR ENDED DECEMBER 31**

|                  | 2020           | 2019    |
|------------------|----------------|---------|
| Opening balance  | <b>\$6,030</b> | \$6,334 |
| Foreign exchange | <b>(119)</b>   | (304)   |
|                  | <b>5,911</b>   | 6,030   |

**18. Accounts Payable and Accrued Liabilities**
**AS AT DECEMBER 31**

|                                   | 2020            | 2019     |
|-----------------------------------|-----------------|----------|
| Trade payables                    | <b>\$10,980</b> | \$23,201 |
| Claims provision (note 26 and 34) | <b>10,859</b>   | 9,027    |
| Payroll-related liabilities       | <b>5,242</b>    | 4,952    |
| Restoration provision             | <b>476</b>      | 466      |
| Accrued interest                  | <b>159</b>      | 356      |
| Other                             | <b>216</b>      | 176      |
|                                   | <b>27,932</b>   | 38,178   |

**19. Contract Liability**
**FOR THE YEAR ENDED DECEMBER 31**

|                       | 2020            | 2019     |
|-----------------------|-----------------|----------|
| Opening balance       | <b>\$6,793</b>  | \$4,999  |
| Additions             | <b>46,550</b>   | 16,399   |
| Realized              | <b>(38,652)</b> | (14,605) |
|                       | <b>14,691</b>   | 6,793    |
| Less: Current portion | <b>11,502</b>   | 2,036    |
| Non-current portion   | <b>3,189</b>    | 4,757    |

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.

## Notes to Consolidated Financial Statements For the year ended December 31, 2020

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

### 20. Term Debt

#### AS AT DECEMBER 31

|                       | 2020            | 2019     |
|-----------------------|-----------------|----------|
| Lease liabilities(a)  | <b>\$18,243</b> | \$20,493 |
| Panta loans (b)       | <b>13,142</b>   | 5,550    |
| SADI loans (c)        | <b>3,734</b>    | 3,573    |
| PPP loans (d)         | <b>917</b>      | -        |
|                       | <b>36,036</b>   | 29,616   |
| Less: Current portion | <b>16,868</b>   | 2,768    |
| Non-current portion   | <b>19,168</b>   | 26,848   |

#### a) Lease Liabilities

There are various lease liabilities that have a weighted average interest rate of 9.0% per annum (2019: 9.0%). The leases are secured by way of a charge against specific assets. The leases are repayable in installments over periods up to 10 years.

The table below categorizes the lease liability into relevant maturity periods based on the remaining periods from the consolidated statement of financial position date to the maturity date.

|                 | December 31, 2020 |                        |                |
|-----------------|-------------------|------------------------|----------------|
|                 | Within 1 Year     | Between 1 – 5<br>Years | Over 5 Years   |
| Lease liability | <b>\$2,619</b>    | <b>\$11,639</b>        | <b>\$3,985</b> |

|                 | December 31, 2019 |                        |              |
|-----------------|-------------------|------------------------|--------------|
|                 | Within 1 Year     | Between 1 – 5<br>Years | Over 5 Years |
| Lease liability | \$2,415           | \$12,598               | \$5,480      |

#### b) Panta Loan

On August 24, 2018, Avcorp entered into a non-revolving term loan agreement ("2018 Panta loan") with Panta Canada B.V. ("Panta") in the principal amount of USD \$3,500,000.

On November 15, 2019, the Company entered into a standby credit facility agreement ("2019 Panta Loan") with Panta Canada B.V. which amended and restated the 2018 Panta Loan, as well as securing an additional \$4,566,000 (USD \$3,500,000). The Company had drawn the full amount on this 2019 Panta Loan in December 2019 and January 2020.

On March 2, 2020, the Company entered into an amendment to the 2019 Panta Loan securing an additional and drawing \$2,686,000 (USD \$2,000,000). As at December 31, 2020 the Company is able to draw up to an additional \$Nil on the standby credit facility.

Panta Canada B.V. is Avcorp's majority shareholder owning approximately 71.2% of the issued and outstanding common shares. 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 Avcorp, is the sole shareholder of Panta Holdings B.V.

- The loan is subordinated to existing security agreements, except that in the event that Avcorp sells its wholly-owned subsidiary, Comtek Advanced Structures Ltd., Avcorp shall pay to Panta an amount up to the indebtedness then outstanding under the loan, subject to any priority payment required by the bank indebtedness and provided there does not then exist an event of default under the Senior Loan Agreement.
- The loan bears interest at the aggregate rate of interest, expressed as an annual rate, of the U.S. Base Rate of Royal Bank of Canada ("RBUSTR") plus a margin of 5.375% per annum which shall accrue and not be compounded until the maturity date. If either an event of default occurs and is continuing or the indebtedness is not repaid in full on the maturity date, the interest rate in such period shall increase to the rate of 15% per annum and all outstanding indebtedness, including unpaid interest, shall continue to accrue interest at such increased rate of interest from and after the maturity date until paid in full.

## Notes to Consolidated Financial Statements For the year ended December 31, 2020

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

- The maturity date is the earlier of: (i) the date upon which, for any reason, the outstanding principal balance of the operating credit facility established under the Senior Loan Agreement becomes due and owing; (ii) June 30, 2023; and (iii) the date on which there is an acceleration of the loan as a result of a written demand by Panta following the occurrence and during the continuance of an uncured event of default. The Panta Loan has been deemed current in nature due to the maturity date of June 30, 2021 of the operating credit facility.
- Upon the happening of any event of default, Panta may at its option: (i) declare that the indebtedness has become immediately due and payable; and (ii) declare that the indebtedness has become immediately due and payable and elect to convert all or part of the indebtedness into common shares of Avcorp at an exercise price equivalent to the then market price at the time of conversion which shall not exceed \$0.15 per common share.

| <b>FOR THE YEAR ENDED DECEMBER 31</b> | <b>2020</b>    | 2019    |
|---------------------------------------|----------------|---------|
| Opening balance                       | <b>\$5,550</b> | \$4,956 |
| Add: Draw down                        | <b>6,924</b>   | 328     |
| Add: Accrued interest                 | <b>1,079</b>   | 518     |
| Less: Foreign exchange gain           | <b>(411)</b>   | (252)   |
|                                       | <b>13,142</b>  | 5,550   |

Subsequent to year end on March 12, 2021, the Company has amended and restated the accommodation agreement with a customer and Panta B.V. Canada providing an additional aggregate USD \$13,000,000 by way of a non-revolving standby loan facility and equipment loan ("Panta 2021") (note 34).

### c) SADI Loans

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;
- Annual repayments are to occur over a 15-year term, commencing four months following the 2018 fiscal year end with subsequent annual repayments to be paid within four months following the Company's then fiscal year ends;
- In September 2020 the Company received a 9 months deferral of repayment obligations from the Government of Canada for the scheduled payment in 2020 and all the subsequent annual payments in response to COVID-19; and
- Amounts repayable are unsecured.

\$3,734,000 was drawn on this facility as at December 31, 2020 (December 31, 2019: \$3,573,000). The amounts owing, when due, are repayable to the Industrial Technologies Office.

|                       | <b>December 31, 2020</b> | December 31, 2019 |
|-----------------------|--------------------------|-------------------|
| Opening balance       | <b>\$3,573</b>           | \$2,902           |
| Add: Accrued interest | <b>161</b>               | 155               |
| Add: Contributions    | -                        | 868               |
| Less: Repayments      | -                        | (352)             |
| Ending Balance        | <b>3,734</b>             | 3,573             |

### d) Paycheck Protection Program Loan

On April 28, 2020, the Company received a loan in the amount of USD \$4,123,000 from a U.S. Chartered Bank through the U.S. Small Business Administration Paycheck Protection Program ("PPP Loan"). The loan has a term of 2 years. The loan bears interest at a fixed rate of 1% per annum. The Company has determined that \$4,601,000 (USD \$3,430,000) met the forgiveness criteria and the amount is included in other income. On March 9, 2021, the Company submitted the application for review to receive this forgiveness.



## Notes to Consolidated Financial Statements For the year ended December 31, 2020

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

| <b>FOR THE YEAR ENDED DECEMBER 31</b> | <b>December 31, 2020</b> | December 31, 2019 |
|---------------------------------------|--------------------------|-------------------|
| Opening balance                       | \$-                      | \$-               |
| Add: Accrued interest                 | 37                       | -                 |
| Add: Contributions                    | 5,529                    | -                 |
| Less: Loan forgiveness                | (4,601)                  | -                 |
| Less: Foreign exchange gain           | (48)                     | -                 |
| Ending Balance                        | <b>917</b>               | -                 |

### 21. Onerous Contract Provision

The Company entered into production contracts in the ordinary course of business. The unavoidable costs of meeting the obligations under certain of these contracts exceed the associated expected future net benefits; consequently, an onerous contract provision has been recognized. The calculation of this provision involves the use of estimates. The onerous contract provision is calculated by taking the expected future costs that will be incurred under the contracts and deducting any estimated revenues. The onerous contract provision for the year ended December 31, 2020 is \$565,000 (December 31, 2019: \$251,000).

| <b>FOR THE YEAR ENDED DECEMBER 31</b> | <b>2020</b> | 2019    |
|---------------------------------------|-------------|---------|
| Opening balance                       | \$251       | \$1,930 |
| Additions                             | 565         | 178     |
| Amortization                          | (257)       | (1,843) |
| Foreign exchange                      | 6           | (14)    |
| Balance                               | <b>565</b>  | 251     |
| Less: Current portion                 | <b>282</b>  | 251     |
| Non-current portion                   | <b>283</b>  | -       |

### 22. Obligations, Commitments and Contingent Liabilities

The Company has \$52,000 in commitments at December 31, 2020 (December 31, 2019: \$318,000) to purchase property, plant and equipment in 2021.

As at December 31, 2020, including the above, the Company had a total of \$35,238,000 of committed contractual operational purchase order obligations outstanding (December 31, 2019: \$70,622,000).

### 23. Capital Stock

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 368,118,620 common shares issued at December 31, 2020.

Common shares issued or reserved:

|   | <b>Number of shares</b> | <b>Amount</b> |
|---|-------------------------|---------------|
| December 31, 2018   | 368,118,620             | 86,219        |
| Share issue   |                         |               |
| Exercise of stock warrants                                      | -                       | -             |
| Transfer from contributed surplus on exercise of stock warrants | -                       | -             |
| December 31, 2019   | 368,118,620             | 86,219        |
| Share issue   |                         |               |
| Exercise of stock warrants                                      | -                       | -             |
| Transfer from contributed surplus on exercise of stock warrants | -                       | -             |
| December 31, 2020   | <b>368,118,620</b>      | <b>86,219</b> |

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

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

- a) The Company's incentive stock option plan is administered by the Board of Directors. It is a rolling share option plan wherein 10% of the issued and outstanding common shares at the time an option is granted are reserved for issuance.

A summary of the Company's stock options issued as of December 31, 2020 and December 31, 2019, and changes during the periods ending on those dates, are presented below:

| FOR THE YEAR ENDED DECEMBER 31  | 2020        |                                 | 2019       |                                 |
|---------------------------------|-------------|---------------------------------|------------|---------------------------------|
|                                 | Options     | Weighted average exercise price | Options    | Weighted average exercise price |
| Outstanding – Beginning of year | 11,443,000  | \$0.067                         | 11,443,000 | \$0.067                         |
| Granted                         | -           | -                               | -          | -                               |
| Expired                         | (6,002,000) | 0.085                           | -          | -                               |
| Exercised                       | -           | -                               | -          | -                               |
| Forfeited                       | -           | -                               | -          | -                               |
| Outstanding – End of year       | 5,441,000   | 0.048                           | 11,443,000 | 0.067                           |

The following table summarizes stock options which are exercisable as at December 31, 2020:

|         | Number    | Weighted average remaining contractual life (years) | Weighted average exercise price |
|---------|-----------|---|---------------------------------|
| \$0.052 | 3,566,000 | 3.74  | \$0.052                         |

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

| FOR THE YEAR ENDED DECEMBER 31             | 2020    | 2019    |
|--|---------|---------|
| Beginning of year                          | \$5,446 | \$5,370 |
| Stock-based compensation expense (note 24) | 32      | 76      |
| End of year                                | 5,478   | 5,446   |

**24. Stock Based Compensation**

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

No stock option was granted in the year ended December 31, 2020 and 2019.

The amount of stock-based compensation expense, for options granted in prior periods, amortized to earnings during the year ended December 31, 2020 was \$32,000 (2019: \$76,000). Stock-based compensation expense has been included in the Consolidated Statements of Income (Loss) and Comprehensive Income (Loss) as administrative and general expenses.

**25. Defined Contribution Plan**

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

| FOR THE YEAR ENDED DECEMBER 31 | 2020    | 2019    |
|--------------------------------|---------|---------|
| Defined contribution plan      | \$1,409 | \$1,423 |

The Company's contribution to the plan is calculated on a percentage of employee wages. The range of percentages is 1.5% to 9.5%. The plan is available to all employees. Defined contribution plan expenses have been included in the Consolidated Statements of Income (Loss) and Comprehensive Income (Loss) as administrative and general expenses and cost of sales.

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**
*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*
**26. Net Claims**

On January 25, 2019, the Company and its subsidiary Avcorp Composite Fabrication Inc. (the "Avcorp Parties") entered into an agreement with HITCO Carbon Composites, Inc., SGL Carbon, LLC, and SGL Carbon SE (the "SGL parties") and a customer to settle all claims related to alleged deficiencies in HITCO's non-destructive inspection processes and other business matters including a lease renewal and collection of a previously provisioned account receivable in exchange for gross consideration of USD \$12,000,000 from the SGL parties to Avcorp and mutual releases among the Avcorp Parties, SGL Parties and a customer related to the acquisition. The net cash payment received totaled USD \$10,810,000. The net claim settlement resulted in a gain of \$19,759,000, including a lease renewal and collection of previously provisioned accounts receivable.

The Company has provisioned USD \$1,350,000 for a legal action in the second quarter of 2019 due to certain employment practices at its Gardena facility.

While a formal claim has not been levied by the customer, the Company has provisioned for a claim asserted by a customer in the amount of \$7,130,000 (USD \$5,600,000) as at December 31, 2020. Subsequent to year end on March 12, 2021, the Company has amended and restated the accommodation agreement with customer and Panta B.V. Canada providing a mutual release and settlement on all claims. (note 34)

**27. Other Income and Losses**

The Canada Emergency Wage Subsidy from the Canadian Government for the year ended December 31, 2020 of \$6,796,000 were included in the Consolidated Statements of Income (Loss) as other income, \$657,000 was capitalized as deferred income which would be recognized as other income when the related inventory are sold by the Company. There are no unfulfilled conditions or other contingencies attaching to these grants. The Company recorded \$2,688,000 as a government grant receivable as at December 31, 2020, which the Company expected to receive subsequent to year end.

On April 28, 2020, the Company received a loan in the amount of USD \$4,123,000 from a U.S. Chartered Bank through the U.S. Small Business Administration Paycheck Protection Program ("PPP Loan"). The loan has a term of 2 years. The loan bears interest at a fixed rate of 1% per annum. As at December 31, 2020, the Company has determined that \$4,601,000 (USD \$3,430,000) met the forgiveness criteria and the amount is included as other income. On March 9, 2021, the Company submitted the application for review to receive this forgiveness.

| <b>FOR THE YEAR ENDED DECEMBER 31</b> | <b>2020</b>   | 2019  |
|---------------------------------------|---------------|-------|
| Canada Emergency Wage Subsidy         | <b>6,796</b>  | -     |
| Government loan forgiven              | <b>4,601</b>  | -     |
| Fair value losses in investment       | -             | (649) |
| Others                                | <b>245</b>    | -     |
|                                       | <b>11,642</b> | (649) |

**28. Finance Costs**

| <b>FOR THE YEAR ENDED DECEMBER 31</b>                 | <b>2020</b>    | 2019    |
|---|----------------|---------|
| Interest on lease liabilities                         | <b>\$1,797</b> | \$1,961 |
| Interest on other term debt                           | <b>198</b>     | 156     |
| Interest on bank indebtedness                         | <b>5,064</b>   | 5,355   |
| (Amortization) Modification loss on bank indebtedness | <b>(540)</b>   | 906     |
| Interest on related party debt                        | <b>1,079</b>   | 518     |
| Non-cash financing cost accretion                     | <b>10</b>      | 11      |
| Interest on contract liabilities                      | <b>119</b>     | 34      |
| Interest expense                                      | <b>7,727</b>   | 8,941   |
| Interest income                                       | <b>(122)</b>   | (17)    |
| Net interest expense                                  | <b>7,605</b>   | 8,924   |

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

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

**29. Supplementary Cash Flow Information**

| <b>FOR THE YEAR ENDED DECEMBER 31</b>    | <b>2020</b>  | 2019  |
|--|--------------|-------|
| Equipment acquired under lease liability | <b>\$440</b> | \$674 |

**30. Income Tax**

The provision for income tax (recovery) expense is based on the combined Canadian federal and provincial annual income tax rate expected for the full financial year of 27%.

IAS 12, Income Taxes, states that the tax effects of changes in tax laws must be recognized in the period in which the law is enacted or substantively enacted. IAS 12 further requires deferred income tax assets and liabilities to be measured at the enacted or substantively enacted tax rate expected to apply when temporary differences are to be realized or settled. Thus, at the date of enactment, the Company's deferred income taxes were re-measured based upon the new tax rate. The change in deferred income taxes is generally recorded as a non-cash re-measurement adjustment to earnings.

Deferred income tax assets are recognized for deductible temporary differences, unused tax losses, and unused tax credits to the extent that the realization of the related tax benefit through future taxable profits is probable. The Company did not recognize deferred income tax assets of \$33,488,000 (2019: \$30,830,000) in respect of losses amounting to \$75,676,000 (2019: \$69,781,000) which include foreign losses of \$40,329,000 (2019: \$37,429,000) that will expire beginning in 2035 through 2040 (except U.S. Net Operating Losses from fiscal 2018 onwards of \$24,401,000 that carryforward indefinitely), unclaimed research and development costs of \$9,940,000 (2019: \$11,173,000) and capital losses of \$830,000 (2019: \$830,000) with no expiry, investment tax credits of \$1,109,000 (2019: \$1,109,000) which expire beginning in 2022 through 2037, and deductible temporary differences of \$35,255,000 (2019: \$29,428,000).

Income tax expense reported differs from the amount computed by applying the combined Canadian federal and provincial income tax rates, applicable to Avcorp Industries Inc., to the income (loss) before taxes due to the following:

| <b>FOR THE YEAR ENDED DECEMBER 31</b>            | <b>2020</b>      | 2019      |
|--|------------------|-----------|
| Canadian federal and provincial income tax rates | <b>27.00%</b>    | 27.00%    |
| Income tax recovery at statutory rate            | <b>\$(1,816)</b> | \$(2,515) |
| Change in unrecognized temporary differences     | <b>2,972</b>     | 2,412     |
| Tax rate differences                             | <b>(42)</b>      | (82)      |
| Permanent differences on loan forgiveness        | <b>(1,286)</b>   | -         |
| Other permanent differences                      | <b>172</b>       | 185       |
| Tax expense (recovery)                           | <b>-</b>         | -         |

**31. Related Party Transactions**

a) Periodically, consulting services are provided by certain directors. Fees paid to certain directors, or companies with which they have beneficial ownership, during the year ended December 31, 2020 are included in the Consolidated statements of Loss and Comprehensive Loss as administrative and general expenses and amount to \$Nil (December 31, 2019: \$3,000). Fees payable to certain directors or Companies with which they have beneficial ownership, as at December 31, 2020 are \$Nil (December 31, 2019: \$Nil).

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.

| <b>FOR THE YEAR ENDED DECEMBER 31</b>           | <b>2020</b>    | 2019    |
|---|----------------|---------|
| Salaries and other short-term employee benefits | <b>\$1,746</b> | \$2,002 |
| Contributions to defined contribution plan      | <b>91</b>      | 82      |
| Option-based awards                             | <b>32</b>      | 76      |
|   | <b>1,869</b>   | 2,160   |

c) Loans to related parties

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

The balance of loans receivable from key management as at December 31, 2020 is \$5,000 (December 31, 2019: \$5,000). These loans are unsecured and payable on demand.

Other related party transactions are disclosed elsewhere in these consolidated financial statements (note 20).

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

**32. Earnings per share**

Weighted average number of common shares for basic earnings per share as at December 31, 2020 is 368,118,620 (December 31, 2019: 368,118,620). Effect of dilution was not applicable in both years.

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

**33. Economic Dependence and Segmented Information**

The Company reports financial performance based on three reportable segments as detailed below. The Company's Chief Operating Decision Maker ("CODM") utilizes Operating Income Loss as a primary measure of profitability to evaluate performance of its segments and allocate resources:

- The Avcorp Structures & Integration ("ASI") segment, which is dedicated to metallic and composite aerostructures assembly and integration.
- The Comtek Advanced Structures Ltd. ("Comtek") segment, within which 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. Corporate includes general corporate administrative costs and any other costs not identifiable with one of the Company's segments.

The Company's Board of Directors 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 operating profit or loss and is measured consistently with operating profit or loss in the Consolidated Statements of Income and Comprehensive Income.

Sales to five major customers for the year ended December 31, 2020, which comprise several programs and contracts, accounted for approximately 92.3% (December 31, 2019: 91.8%) of sales.

| FOR THE YEAR ENDED DECEMBER 31 | 2020     |            | 2019     |            |
|--------------------------------|----------|------------|----------|------------|
|                                | Revenue  | % of Total | Revenue  | % of Total |
| BAE Systems                    | \$31,332 | 20.8       | \$18,181 | 11.0       |
| Boeing <sup>1</sup>            | 48,237   | 31.9       | 50,351   | 30.6       |
| Bombardier                     | 12,998   | 8.6        | 18,535   | 11.2       |
| Lockheed Martin                | 30,444   | 20.2       | 35,812   | 21.8       |
| Subaru Corporation             | 16,311   | 10.8       | 28,306   | 17.2       |
| Other                          | 11,640   | 7.7        | 13,585   | 8.2        |
| Total                          | 150,962  | 100.0      | 164,770  | 100.0      |

1. Includes Boeing program partner revenue consisting of industry tier-one suppliers to Boeing

a) The Company's sales are distributed amongst the following geographical locations based on location of customers:

## Notes to Consolidated Financial Statements For the year ended December 31, 2020

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

### FOR THE YEAR ENDED DECEMBER 31

|              | 2020           |              | 2019           |              |
|--------------|----------------|--------------|----------------|--------------|
|              | Revenue        | % of Total   | Revenue        | % of Total   |
| Canada       | \$19,801       | 13.1         | \$26,081       | 15.8         |
| USA          | 81,317         | 53.9         | 87,624         | 53.2         |
| Europe       | 32,134         | 21.3         | 20,032         | 12.2         |
| Asia         | 17,462         | 11.6         | 30,706         | 18.6         |
| Australia    | 186            | 0.1          | 257            | 0.2          |
| Other        | 62             | 0.0          | 70             | 0.0          |
| <b>Total</b> | <b>150,962</b> | <b>100.0</b> | <b>164,770</b> | <b>100.0</b> |

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

### AS AT DECEMBER 31

|              | 2020           | 2019           |
|--------------|----------------|----------------|
| Canada       | \$84,644       | \$82,233       |
| USA          | 36,894         | 45,907         |
| <b>Total</b> | <b>121,538</b> | <b>128,140</b> |

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.

- c) The Company's sales are distributed amongst commercial and defence markets:

### FOR THE YEAR ENDED DECEMBER 31

|              | 2020           |              | 2019           |              |
|--------------|----------------|--------------|----------------|--------------|
|              | Revenue        | % of Total   | Revenue        | % of Total   |
| Commercial   | \$63,179       | 41.9         | \$102,437      | 62.2         |
| Defence      | 87,783         | 58.1         | 62,333         | 37.8         |
| <b>Total</b> | <b>150,962</b> | <b>100.0</b> | <b>164,770</b> | <b>100.0</b> |

- d) The Company's revenue is recognized either at a point in time or over time. For the year ended December 31, 2020, revenue earned at a point in time is \$26,700,000 (December 31, 2019: \$42,671,000). Revenue earned over time is \$124,262,000 for the year ended December 31, 2020 (December 31, 2019: \$122,099,000).
- e) 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.

### FOR THE YEAR ENDED DECEMBER 31, 2020

|                                     | Total        | ASI           | Comtek       | ACF            | Corporate      |
|-------------------------------------|--------------|---------------|--------------|----------------|----------------|
| Revenue                             | \$150,962    | 86,756        | \$16,509     | \$47,697       | \$-            |
| Cost of sales                       | 142,729      | 75,868        | 13,941       | 52,920         | -              |
| Gross profit (loss)                 | 8,233        | 10,888        | 2,568        | (5,223)        | -              |
| Administrative and general expenses | 16,717       | 5,779         | 2,288        | 4,247          | 4,403          |
| Depreciation and amortization       | 787          | 314           | 60           | 413            | -              |
| Other income                        | (11,642)     | (5,523)       | (1,273)      | (4,846)        | -              |
| <b>Operating income (loss)</b>      | <b>2,371</b> | <b>10,318</b> | <b>1,493</b> | <b>(5,037)</b> | <b>(4,403)</b> |

# Avcorp Industries Inc.

annual report 2020

## Notes to Consolidated Financial Statements For the year ended December 31, 2020

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

### FOR THE YEAR ENDED DECEMBER 31, 2019

|                                     | Total     | ASI      | Comtek   | ACF      | Corporate |
|-------------------------------------|-----------|----------|----------|----------|-----------|
| Revenue                             | \$164,770 | \$78,099 | \$20,455 | \$66,216 | \$-       |
| Cost of sales                       | 160,982   | 76,206   | 16,910   | 67,866   | -         |
| Gross profit (loss)                 | 3,788     | 1,893    | 3,545    | (1,650)  | -         |
| Administrative and general expenses | 21,467    | 5,130    | 2,632    | 6,460    | 7,245     |
| Depreciation and amortization       | 770       | 328      | 63       | 379      | -         |
| Net (gain) loss on claims           | (17,974)  | -        | -        | 1,785    | (19,759)  |
| Other loss                          | 649       | -        | -        | -        | 649       |
| Operating income (loss)             | (1,124)   | (3,565)  | 850      | (10,274) | 11,865    |

### AS AT DECEMBER 31

|                                   | 2020         |            | 2019         |            |
|-----------------------------------|--------------|------------|--------------|------------|
|                                   | Total Assets | % of Total | Total Assets | % of Total |
| Avcorp Industries Inc.            | \$72,163     | 59.3       | \$69,638     | 54.4       |
| Comtek Advanced Structures Ltd.   | 12,345       | 10.2       | 12,460       | 9.7        |
| Avcorp Composite Fabrication Inc. | 36,894       | 30.4       | 45,907       | 35.8       |
| Corporate                         | 136          | 0.1        | 135          | 0.1        |
| Total                             | 121,538      | 100.0      | 128,140      | 100.0      |

### AS AT DECEMBER 31

|                                   | 2020                       |   | 2019                       |   |
|-----------------------------------|----------------------------|---|----------------------------|---|
|                                   | Development Cost Additions | Property, Plant and Equipment Additions | Development Cost Additions | Property, Plant and Equipment Additions |
| Avcorp Industries Inc.            | \$3,599                    | \$1,651                                 | \$3,934                    | \$1,067                                 |
| Comtek Advanced Structures Ltd.   | 175                        | 118                                     | 100                        | 239                                     |
| Avcorp Composite Fabrication Inc. | 155                        | 440                                     | 82                         | 13,133                                  |
| Total                             | 3,929                      | 2,209                                   | 4,116                      | 14,439                                  |

### AS AT DECEMBER 31

|                                   | 2020              |            | 2019              |            |
|-----------------------------------|-------------------|------------|-------------------|------------|
|                                   | Total Liabilities | % of Total | Total Liabilities | % of Total |
| Avcorp Industries Inc.            | \$41,361          | 24.2       | \$37,783          | 22.0       |
| Comtek Advanced Structures Ltd.   | 3,037             | 1.8        | 3,909             | 2.3        |
| Avcorp Composite Fabrication Inc. | 19,630            | 11.5       | 24,156            | 14.1       |
| Corporate                         | 106,650           | 62.5       | 105,767           | 61.6       |
| Total                             | 170,678           | 100.0      | 171,615           | 100.0      |

## 34. Subsequent Events

- The Company received Canada Emergency Wage Subsidies of \$712,000 in February and March 2021 and applied for an additional \$2,415,000.
- On February 25, 2021, the Company amended the Avcorp Composite Fabrication Inc.'s Gardena facility lease agreement effective January 1, 2021 to vacate certain buildings and renegotiated new lease terms. The amended terms of the lease reduced lease payments, reduced shared operating cost, and ends on December 31, 2022 with an option to extend for three months.
- On March 12, 2021, the Company entered into a multiparty amended and restated the Accommodation Agreement with each of a customer, and Panta Canada B.V. whereby, inter alia;

**Notes to Consolidated Financial Statements  
For the year ended December 31, 2020**

*(all figures in tables are expressed in thousands of Canadian dollars, except per share amounts)*

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- Panta Canada B.V. has agreed to provide a USD \$10,000,000 non-revolving standby loan facility and a USD \$3,000,000 equipment loan for an aggregate availability of USD \$13,000,000; and
  - The elimination of unamortized cash advance, mutual release and forgiveness of certain historic and future guarantee fees payable to the customer. As at December 31, 2020, the guarantee fee is \$8,178,000 (USD \$6,423,000), the customer advance is \$5,911,000 (USD \$4,643,000) and the legal claim is \$7,130,000 (USD \$5,600,000).
- d) On March 15, 2021, the Company received a USD \$2,000,000 second wave Small Business Administration Paycheck Protection Program Loan.
- e) On March 19, 2021, the Company approved the grant of an aggregate of 17,350,000 incentive stock options under the Company's 2007 Stock Option Plan to Directors, Officers and Employees. The options will have a five year term and will have an exercise price determined by the market price effective the close of markets March 22,2021.



## notes

## AVCORP INDUSTRIES INC.

### BOARD OF DIRECTORS AND OFFICERS

David Levi <sup>(1)(2)</sup>  
CHAIRMAN OF THE BOARD  
Executive Chairman  
GrowthWorks Capital Ltd.  
Vancouver, British Columbia

Elizabeth Otis <sup>(1)(2)</sup>  
DIRECTOR  
Tucson, Arizona

Jaap Rosen Jacobson <sup>(2\*)</sup>  
DIRECTOR  
President  
Panta Holdings B.V.  
Mijdrecht, The Netherlands

Ken Robertson <sup>(1\*)</sup>  
DIRECTOR  
Vancouver, British Columbia

Amandeep Kaler  
DIRECTOR  
Group CEO, Avcorp Industries Inc.  
Surrey, British Columbia

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

\*Designates the Committee Chair

### MANAGEMENT

Amandeep Kaler  
Group Chief Executive Officer  
Surrey, British Columbia

Jessica Gill  
Group Vice President, Human Resources  
Surrey, British Columbia

Amish Patel  
Group Vice President, Finance  
North Vancouver, British Columbia

Robin Lovell  
President  
Comtek Advanced Structures Ltd.  
Oakville, Ontario

Tony Kelsey  
General Manager  
Avcorp Composite Fabrication Inc.  
Jurupa Valley, California

Mike Elvidge  
General Manager  
Avcorp Industries Inc.  
Surrey, British Columbia

### DIRECTORY

#### Legal Counsel

McMillan LLP  
Barristers & Solicitors  
Vancouver, British Columbia

#### Auditors

Ernst & Young LLP  
Chartered Professional Accountants  
Vancouver, British Columbia

#### Shares Listed

Toronto Stock Exchange  
Symbol AVP

#### Registrar and Transfer Agent

AST Trust Company (Canada)  
Vancouver, British Columbia

#### Bank

Royal Bank of Canada  
Richmond, British Columbia

#### Avcorp Industries Inc.

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