



**MANAGEMENT'S DISCUSSION & ANALYSIS**  
**OF FINANCIAL CONDITION AND RESULTS OF**  
**OPERATIONS**

**For the six months ended June 30, 2016**

**Dated August 9, 2016**

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## 1. Introduction

The following management's discussion and analysis ("MD&A") of Baylin Technologies Inc. ("Baylin", the "Company", "we" or "us") as of August 9, 2016 should be read in conjunction with (i) our unaudited interim condensed consolidated financial statements for the three months and six months ended June 30, 2016 and 2015 and (ii) our audited consolidated financial statements for the year ended December 31, 2015 ("Fiscal 2015") and the related notes included therein. These audited consolidated financial statements have been prepared using accounting policies consistent with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). All amounts are expressed in United States dollars unless otherwise indicated. The MD&A unaudited and audited consolidated financial statements were reviewed by our audit committee (the "Audit Committee") and approved by our board of directors (the "Board of Directors").

Additional information relating to the Company, including our most recent Annual Information Form, may be found at [www.sedar.com](http://www.sedar.com).

### Forward-Looking Statements

This MD&A of the financial conditions and results of operations contains forward-looking statements concerning anticipated developments in our operations in future periods, the adequacy of our financial resources and other events or conditions that may occur in the future. Forward-looking statements are frequently, but not always, identified by words such as "expects," "anticipates," "believes," "intends," "estimates," "predicts," "potential," "targeted," "plans," "possible" and similar expressions, or statements that events, conditions or results "will," "may," "could" or "should" occur or be achieved. These forward-looking statements include, without limitation, statements about our market opportunities, strategies, competition, expected activities and expenditures as we pursue our business plan, the adequacy of our available cash resources and other statements about future events or results. Forward-looking statements are statements about the future and are inherently uncertain and actual achievements of the Company or other future events or conditions may differ materially from those reflected in the forward-looking statements due to a variety of risks, uncertainties and other factors, such as business and economic risks and uncertainties. Forward-looking statements are based on certain assumptions and analyses made by the Company in light of the experience and perception of historical trends, current conditions and expected future developments and other factors it believes are appropriate, and are subject to risks and uncertainties. Although we believe that the assumptions underlying these statements are reasonable, they may prove to be incorrect, and we cannot assure that actual results will be consistent with these forward-looking statements. Consequently, all forward-looking statements made in this MD&A on the financial conditions and results of operations or the documents incorporated by reference are qualified by this cautionary statement and there can be no assurance that actual results or developments we anticipate will be realized. Some of these risks, uncertainties and other factors are described in our most recent Annual Information Form under the heading "Risk Factors" available at [www.sedar.com](http://www.sedar.com). For the reasons set forth above, investors should not place undue reliance on forward-looking statements. Unless otherwise stated, the forward-looking statements contained in this MD&A are made as of the date of this MD&A and we assume no obligation to update any forward-looking statements, whether as a result of new information or future events or otherwise, except to the extent required by applicable law.

## 2. Overview

We are a global provider of innovative wireless antenna solutions with over 38 years of experience in designing, manufacturing and supplying antennas. We strive to meet our customers' needs by being their trusted partner from initial design to production. Our antenna solutions are custom engineered to meet the specifications for our customers' mobile, broadband and wireless infrastructure needs. Since our establishment in 1978, our business has grown into an international platform with operations in North America and Asia.

### **3. Overall Performance**

#### **3.1 Material issues for the three months and six months ended June 30, 2016 and 2015:**

- Positive momentum continued into the second quarter of fiscal 2016, building on the much improved first quarter of fiscal 2016.
- Revenue increased by 57%, to \$15.7 million in Q2 2016, from the comparable quarter in fiscal 2015. Strong results were posted in Mobile and Infrastructure product lines, which grew by 222% and 18% respectively. Year-to-date 2016 Revenue was up 75%, to \$31.5 million, from the comparable period in fiscal 2015.
- Gross profit and gross margin both increased in the current quarter to \$4.4 million and 28.1%, respectively; doubling the \$2.2 million generated in the same quarter in fiscal 2015. Gross profit also grew by 3% from the first quarter of fiscal 2016, bringing year-to-date gross profit to \$8.7 million; a 167% increase from the same period in fiscal 2015.
- Operating expenses declined again in both dollar term and as a percentage of Revenue, to \$4.7 million (29.8% of Revenue) when compared to Q1 2016 (\$4.9 million, 31.0%) and Q2 2015 (\$4.9 million, 49.2%).
- Positive EBITDA continued into Q2 2016. At \$0.5 million it increased from \$0.2 million in Q1 of fiscal 2016. This was the second sequential positive quarter, and an improvement over the comparable quarter last year where the EBITDA loss was \$1.7 million. EBITDA for the six months ended June 30, 2016 was \$0.7 million, an improvement from the comparable period in fiscal 2015 where the EBITDA loss was \$5.2 million.
- Invested to facilitate further growth, by continuing to hire more engineers and investing \$0.3 million in capital equipment in the first half of 2016. The second half of 2016 will see the launch of our new product introduction line (NPI) in Tempe, Arizona which will improve time to market for new Infrastructure products.
- Continued to improve liquidity through (i) improved cash conversion cycle, to 36 days in the current quarter, and (ii) entered into a sale and leaseback of our Israel based R&D facility. Sale proceeds are \$1.8 million, and the lease term is for 3 years leasing approximately 50% of the space previously occupied.
- Increased our Cash position to \$8.1 million at end of Q2 2016; an increase of \$1.4 million from March 31, 2016. Debt and lease obligations declined by 57%, to \$2.7 million, in the first six months of 2016.
- Completed the Head office transition with the announcement of PricewaterhouseCoopers LLP (Canada) as the company's new auditors.

#### **3.2 Outlook**

The significant changes made in Fiscal 2015, meant to address the operating losses and negative cash flow incurred in fiscal 2014 and 2015, were meaningful contributing factors to the significantly improved financial results in the first half of fiscal 2016. The second quarter of fiscal 2016 saw a continuation of year-over-year ("YOY") growth in (i) Revenue and gross profit, (ii) gross margin expansion and (iii) reduction in overall operating costs, leading to the first sequential positive EBITDA quarters since our Initial Public Offering in November 2013.

Another significant contributing factor to our improved financial results in the first six months of fiscal 2016 was the improved market position of our Mobile product line with our major customer relative to

a year ago. The momentum created in the latter part of fiscal 2015 carried into the first half of fiscal 2016, primarily due to the continued success this customer is having with its new product launch. As previously noted, due to this customer's product launch being earlier than in prior years and normal seasonality of this business, Mobile shipments in the second half of fiscal 2016 are currently anticipated to be lower than the level shipped in the first half of fiscal 2016.

U.S.-based telecommunication carriers are predicting growth in network capital spending in 2016, and we believe our Infrastructure products are well positioned to benefit from that occurrence. Accordingly we currently anticipate posting stronger Infrastructure shipments in the second half of fiscal 2016 relative to the first half of 2016.

Cost reductions, manufacturing efficiency and product line rationalization will continue in 2016 and we expect these improvements will lead to modest improvement in gross margin in the second half of fiscal 2016 compared with the first half.

The over-arching focus for the Board of Directors and management in fiscal 2016 is to continue the momentum created in the second half of 2015 while prudently managing our liquidity. Exploring new opportunities in the Mobile market, continuing to diversify and expand the Networking customer portfolio and further expanding the Infrastructure product portfolio will be the primary focus. Also, management will explore opportunities to increase its capital resources and liquidity in light of the anticipated growth and consequential requirement to fund increased working capital levels.

### **3.3 Industry & Business Overview**

One of the significant changes that occurred mid-2015 was the focus on Mobile, Wireless Infrastructure and Networking sales structure. Mobile, the largest product line area in terms of Revenue, undertook a major initiative with the establishment of the Vietnam manufacturing plant. Establishing this new plant helped regain market share with our major customer, as evidenced by the growth in the first half of fiscal 2016. During the last three quarters of fiscal 2015 and into fiscal 2016, LDS production capacity increased in order to meet this customer's demand. In order to facilitate this increase, it necessitated transitioning nearly the entire LDS capacity to Vietnam. The Company expects its Mobile customer portfolio to diversify and grow in the short-term following new design wins announced in 2015.

As a result of the Company's strategy of diversifying its revenue base and becoming less reliant on the Mobile product line, and in particular its major customer, the Wireless Infrastructure product line is seen as a major growth opportunity. Overall capital spending in this market was soft in 2014 and the first part of 2015 however we noted increased spending in the latter part of 2015. We anticipate spending by our customers (cellular carriers in particular) to continue to ramp up in 2016. As a result, we believe we are well positioned to win additional market share given the breadth of our product offering and expertise in both indoor and outdoor DAS products. A key focus is the expansion of our product portfolio and gaining additional key customers in the mid to latter part of 2016 and more fully in 2017.

The Networking product line remains positioned as the leading choice in the United States for Tier 1 carrier grade gateways. Over the past two years the Networking product line has also been able to diversify its customer portfolio by securing some significant new customers. We have continued to build a robust product pipeline and grow the product portfolio, though are also managing the product life-cycle of mature products.

### **3.4 Key Performance Indicators**

Key performance indicators ("KPI") that we use to manage our business and evaluate our financial results and operating performance include the following:

**Operations***Revenue growth*

We analyze our sales as one reporting segment. We use indicators to analyze sales such as YOY growth and compound annual growth rate ("CAGR"), and comparison to monthly budgets.

*EBITDA and Adjusted EBITDA*

We use EBITDA and Adjusted EBITDA to measure our financial performance and our ability to generate and sustain earnings and cash flow. EBITDA refers to earnings before interest, net finance expenses, taxes, depreciation and amortization and discontinued operations. Adjusted EBITDA refers to EBITDA adjusted for items of an exceptional nature that are outside of the ordinary course of business. Such items include, but are not limited to, one-time items, certain exceptional, non-recurring share-based compensation, capital gains and losses, restructuring costs, recognition of significant provisions and other significant non-cash transactions (collectively "one-time items"). We do not believe these one-time items reflect the underlying performance of our business. EBITDA and Adjusted EBITDA are non-IFRS performance measures. We believe that in addition to net earnings, EBITDA and Adjusted EBITDA are useful complementary measures to pre-tax profitability and are commonly used by the financial and investment community for valuation purposes.

*Variable contribution*

We use variable contribution (Revenue less material cost and direct variable labour) and variable contribution margin (variable contribution divided by Revenue) to measure the profit available to cover fixed manufacturing costs and operating expenses. Our variable contribution margin can change due to the mix of products sold, the portion of materials and direct labour and the costs thereof, as well as changes in selling prices which occur in the market from time to time.

*Research & Development ("R&D")*

As a leading technology company, we make R&D investments to remain at the forefront of technology as required by our customers and to maintain solutions for the top antenna providers. R&D investments secure our position as an innovative solution provider for our current and potential customers. We monitor our R&D investments according to market requirements and the product categories we aim to enter. We will continue to invest in R&D activities in areas we believe have significant profitable revenue opportunities. Our objective is to accelerate the design and development of the opportunities we believe will provide sustainable profitable growth.

*Sales and marketing and general and administrative ("G&A") expense monitoring*

We incur sales and marketing and G&A costs that are essential to our business growth. These expense levels are monitored regularly against pre-established budgets.

**Financial Position***Liquidity and streaming cash management*

As a global company, we maintain a global cash management system which enables us to fund the operations of our subsidiaries. We maintain credit facilities as required at several of our main operating locations to support our sales, manufacturing, and R&D activities. We see cash flow as an important KPI for the whole organization and the specific locations in particular.

*Working Capital requirements*

We monitor the individual components of working capital (current assets less current liabilities). The KPI's used are customer collection days, vendor payment days and the level of inventory relative to sales. We monitor working capital levels through a cash conversion cycle ("CCC") on a monthly basis to maintain sufficient, but not excessive, working capital for our operations.

*Current Ratio*

Current ratio is a non-IFRS measure that does not have a standardized meaning and may not be comparable to a similar measure disclosed by other issuers. Current ratio is calculated by dividing current assets by current liabilities. Monitoring the current ratio helps to assess our level of current assets available to satisfy current liabilities.

*Capital Expenditures*

Management uses the return on investment model and simple payback to evaluate significant capital expenditures.

**Significant Factors Affecting Results of Operations**

Our results of operations are influenced by a variety of factors, including:

*Revenue*

Revenue is derived from the sales of our antenna products. Financial results are reported as one reportable segment. The Company manufactures and sells a variety of antenna products such as antennas for mobile handsets and smartphones, networking and telemetry devices, land mobile radios, telematics and wireless infrastructure antennas. Revenue is impacted by the timing of our customer's product launches, their project deployment plans, and network expansion investment levels by carriers and independent providers.

*Gross profit*

Our gross profit is impacted by selling prices and sales volumes, product mix and the variable costs of goods sold (being direct materials and direct labour). The Company also commenced lean manufacturing processes in order to optimize and reduce its fixed manufacturing costs going forward.

*R&D Expenses*

R&D expenses consist primarily of salaries, patent fees, product development costs and other related engineering expenses. Our technological design centers are located in Israel, South Korea and the United States. As such, we often incur significant expenditures in the development of a new product without any assurance that our customers' system designers will ultimately select our product for use in their applications. We are often required to anticipate which product designs will generate demand in advance of our customers expressly indicating a need for that particular design. Even if our customers' system designers ultimately select our products, a substantial period of time will elapse before we generate revenue relative to the possibly significant expenses we have initially incurred.

*Sales and Marketing Expenses*

Sales and marketing expenses consist primarily of salaries, advertising, trade shows, travel costs and other promotional activities. The impact of these costs can be material when entering new markets such as the infrastructure market and reaching new customers, requiring significant investments to win new business.

*G&A Expenses*

G&A expenses consist of costs relating to human resources, legal and finance functions, professional fees, insurance and other corporate expenses.

**Non-IFRS Measures**

The following are non-IFRS measures. Accordingly, investors are cautioned not to place undue reliance on them and are also urged to read all IFRS accounting disclosures presented in the unaudited condensed consolidated financial statements for the six months ended June 30, 2016 and the audited consolidated financial statements and accompanying notes for Fiscal 2015. Non-IFRS measures do not have a

standardized meaning and our calculation thereof may not be comparable to similar measures disclosed by other issuers.

#### *EBITDA and Adjusted EBITDA*

EBITDA and Adjusted EBITDA are non-IFRS measures that we use to assess our operating performance. EBITDA and Adjusted EBITDA are reconciled as follows:

#### **Reconciliation to Operating Loss**

('000s)	Three months ended June 30		
	2016	2015	% Change
	\$	\$	
<b>Operating loss</b>	<b>(264)</b>	<b>(2,703)</b>	n/m
Amortization and depreciation	788	1,004	-22.3
<b>EBITDA</b>	<b>524</b>	<b>(1,699)</b>	n/m
Termination costs and other one-time costs	(30)	401	n/m
<b>Adjusted EBITDA</b>	<b>494</b>	<b>(1,298)</b>	n/m

('000s)	Six months ended June 30		
	2016	2015	% Change
	\$	\$	
<b>Operating loss</b>	<b>(893)</b>	<b>(7,092)</b>	n/m
Amortization and depreciation	1,600	1,874	-14.6
<b>EBITDA</b>	<b>707</b>	<b>(5,218)</b>	n/m
Termination costs and other one-time costs	82	1,022	-
<b>Adjusted EBITDA</b>	<b>789</b>	<b>(4,196)</b>	n/m

For the three months ending June 30, 2016, EBITDA was \$0.5 million, a significant turnaround from the EBITDA loss of \$1.7 million in the comparable period in 2015. The positive EBITDA in the current quarter was the second sequential positive quarter, reversing the eight sequential quarterly EBITDA losses incurred in fiscal 2014 and 2015. Increases in Revenue and gross profit in the three months ended June 30, 2016 were the primary contributing factors to the EBITDA improvement.

For the six months ending June 30, 2016, EBITDA was \$0.7 million; a significant turnaround from the EBITDA loss of \$5.2 million in the comparable period in 2015. The factors noted above were also the primary contributing factors to the EBITDA improvement. Adjusted EBITDA for the six months ended June 30, 2016 was \$0.8 million; a substantial improvement from the \$4.2 million Adjusted EBITDA loss in the comparable period a year ago.

#### **4. Selected Financial Information and Discussion of Operations**

The following table sets forth a summary of the results of operations for the fiscal periods indicated:

('000s), except per share amounts	Three months ended		Six months ended		
	June 30		June 30		
	2016	2015	2016	2015	Fiscal 2015
	\$	\$	\$	\$	\$
Revenue	15,661	9,992	31,450	17,947	43,026
Gross Profit	4,407	2,215	8,668	3,244	9,091
Loss before income taxes	(78)	(2,541)	(617)	(8,286)	(14,074)
Income taxes	(233)	(127)	(282)	(132)	(596)
Net Loss	(311)	(2,668)	(899)	(8,418)	(14,670)
Basic and diluted loss per share	(0.02)	(0.14)	(0.05)	(0.45)	(0.78)
EBITDA	524	(1,699)	707	(5,218)	(8,704)
Adjusted EBITDA	494	(1,298)	789	(4,196)	(6,928)
Current assets	29,567	31,712	29,567	31,712	28,346
Total assets	47,575	56,015	47,575	56,015	49,574
Current liabilities	17,030	17,885	17,030	17,885	18,433
Non-current liabilities	1,355	986	1,355	986	983
Total liabilities	18,385	18,871	18,385	18,871	19,416

### Results of Operations for the three and six months ended June 30, 2016 and 2015:

#### Revenue, Cost of Revenue and Gross Margin

('000s)	Three months ended June 30			Six months ended June 30		
	2016	2015	% Change	2016	2015	% Change
	\$	\$		\$	\$	
<b>Revenue</b>	<b>15,661</b>	<b>9,992</b>	<b>56.7</b>	<b>31,450</b>	<b>17,947</b>	<b>75.2</b>
Cost of Revenue	11,254	7,777	44.7	22,782	14,703	54.9
Gross Profit	4,407	2,215	100.0	8,668	3,244	167.2
Gross Margin (%)	28.1	22.2		27.6	18.1	

#### Revenue

Revenue in the three months ended June 30, 2016 and 2015 were \$15.7 million and \$10.0 million, respectively, reflecting an increase of 56.7% YOY. The increase was due primarily to stronger shipments of Mobile products, particularly to our main customer, and to a lesser extent growth in sales of our Infrastructure products. Sales of Networking products in the current quarter were lower than in the comparable prior year quarter due to the timing of customer demand.

Revenue in the six months ended June 30, 2016 and 2015 were \$31.5 million and \$17.9 million, respectively, reflecting an increase of 75.2% YOY. The increase was due primarily to similar factors as noted above.

Our main customer accounted for 52% and 58% of Revenue for Q2, 2016 and Q1 2016, respectively. As previously noted, due to this customer's product launch being earlier than in prior years, Mobile shipments in Q2 of fiscal 2016 were lower than the level shipped in Q1 of fiscal 2016. Also, due to this factor and the normal seasonality of this business, Mobile shipments in the second half of fiscal 2016 are currently anticipated to be lower than the level shipped in the first half of fiscal 2016.

#### Cost of Revenue

Cost of revenue is comprised of variable costs (such as material cost and direct labour) and fixed costs, (such as indirect labour, other manufacturing overheads and depreciation). Variable costs were \$8.3

million (52.8% of Revenue) in Q2 of fiscal 2016, versus \$5.2 million (51.6% of Revenue) in last year's comparable quarter. The increase in variable costs of \$3.1 million was due primarily to higher Revenue, and to a lesser extent the product mix. Fixed costs in Q2 of fiscal 2016 were \$3.0 million (19.1% of Revenue), versus \$2.6 million in the comparable quarter in fiscal 2015 (26.3% of Revenue).

For the six months ended June 30, 2016, variable costs were \$17.3 million (55.1% of Revenue), versus \$9.6 million (53.5% of Revenue) in last year's comparable period. The increase in variable costs of \$7.7 million was due primarily to higher Revenue. Fixed costs in the first half of fiscal 2016 were \$5.4 million (17.3% of Revenue), versus \$5.1 million in the comparable period in fiscal 2015 (28.4% of Revenue). The improved ratio of fixed costs to Revenue was primarily due to the higher production volumes in the first half of fiscal 2016.

### ***Gross Profit***

Gross profit increased to \$4.4 million (28.1% of Revenue) in the three months ended June 30, 2016. This represented an improvement from Q1 of fiscal 2016 (\$4.3 million or 26.9% of Revenue) and the comparable quarter in fiscal 2015 (\$2.2 million or 22.2% of Revenue). The improvement in gross margin (gross profit divided by Revenue) in fiscal 2016 was attributable to the higher production volumes (associated with the increased sales) amortized over a relatively fixed cost base.

Gross profit increased to \$8.7 million (27.6% of Revenue) in the six months ended June 30, 2016. This represented an improvement from the comparable period in fiscal 2015 (\$3.2 million or 18.1% of Revenue). The improvement in gross margin in fiscal 2016 was attributable to the same factors cited above.

### ***R&D Expenses***

	Three months ended June 30			Six months ended June 30		
	2016	2015	% Change	2016	2015	% Change
	\$	\$		\$	\$	
Payrolls	1,432	1,017	40.8	2,808	2,052	36.8
Other development costs	377	392	-3.8	802	872	-8.0
Depreciation	19	118	-83.9	100	220	-54.5
<b>Total</b>	<b>1,828</b>	<b>1,527</b>	<b>19.6</b>	<b>3,700</b>	<b>3,144</b>	<b>17.7</b>
As a percentage of Revenue	11.7	15.3		11.7	17.5	

R&D expenses were \$1.8 million in Q2 fiscal 2016, compared with \$1.5 million in same quarter in fiscal 2015. These expenses were \$3.7 million in the first six months of fiscal 2016, compared with \$3.1 million in same period in fiscal 2015. We increased R&D spending in fiscal 2016, mainly in increased headcount, in order to expand the product pipeline for 2016 and future years.

**Sales and Marketing Expenses**

('000s)	Three months ended June 30			Six months ended June 30		
	2016	2015	% Change	2016	2015	% Change
	\$	\$		\$	\$	
Payrolls	571	800	-28.6	1,221	1,482	-17.6
Other	89	289	-69.2	310	838	-63.0
<b>Total</b>	<b>660</b>	<b>1,089</b>	<b>-37.6</b>	<b>1,532</b>	<b>2,320</b>	<b>-34.0</b>
As a percentage of Revenue	4.2	10.9		4.9	12.9	

Sales and marketing expenses of \$0.7 million declined in the second quarter of fiscal 2016, from \$1.1 million in the same quarter in fiscal 2015. Payroll-related expenses declined YOY due to streamlining senior sales management at the end of Q1 fiscal 2016, though was partially offset by hiring more sales people. Our belief is these investments will yield benefits in driving the Company's growth strategy in new business areas, thereby diversifying our revenue base and penetrating new and growing markets. There were also decreases in tradeshows, travel expenses and other related expenses as part of the Company's cost reduction initiatives.

Sales and marketing expenses of \$1.5 million in the first half of fiscal 2016 declined from \$2.3 million in the same period in fiscal 2015. The decreases were in tradeshows, travel expenses and other related expenses as part of the Company's cost reduction initiatives.

**General and Administrative**

('000s)	Three months ended June 30			Six months ended June 30		
	2016	2015	% Change	2016	2015	% Change
	\$	\$		\$	\$	
Payrolls	928	684	35.7	1,754	2,140	-18.0
Other	1,165	1,468	-20.6	2,420	2,462	-1.7
Depreciation	90	150	-40.0	155	270	-42.6
<b>Total</b>	<b>2,183</b>	<b>2,302</b>	<b>-5.2</b>	<b>4,329</b>	<b>4,872</b>	<b>-11.1</b>
As a percentage of Revenue	13.9	23.0		13.8	27.1	

G&A expenses for the three months ended June 30, 2016 decreased from the three months ended June 30, 2015 by \$0.1 million, whereas these expenses decreased by \$0.5 million in the comparable six month periods, due to the ongoing expense control initiatives.

**Net loss for the period**

('000s), except per share amounts	Three months ended June 30			Six months ended June 30		
	2016	2015	% Change	2016	2015	% Change
	\$	\$		\$	\$	
Loss before taxes	(78)	(2,541)	n/m	(617)	(8,286)	n/m
Income taxes	(233)	(127)	84.3	(282)	(132)	113.6
<b>Loss for the period</b>	<b>(311)</b>	<b>(2,668)</b>	<b>n/m</b>	<b>(899)</b>	<b>(8,481)</b>	<b>n/m</b>
Basic and diluted loss per share:	(0.02)	(0.14)		(0.05)	(0.45)	

Tax expenses increased in the current quarter and half year, from the comparable periods in fiscal 2015 due to the significant increase in the Company's earnings. The company has not recognized yet any significant tax recovery for its carry forward operating losses.

### 5. Summary of Quarterly Results

<b>('000s), except per share amounts</b>				
	<b>Three Months Ended</b>			
	<b>June 30, 2016</b>	<b>March 31, 2016</b>	<b>December 31, 2015</b>	<b>September 30, 2015</b>
	\$	\$	\$	\$
Revenue	15,661	15,789	12,981	12,098
Gross Profit	4,407	4,262	3,122	2,725
EBITDA	524	184	(1,976)	(1,511)
Adjusted EBITDA	494	295	(1,477)	(1,255)
Loss	(311)	(588)	(3,309)	(2,943)
Basic and diluted loss per share	(0.02)	(0.03)	(0.18)	(0.16)

  

<b>('000s), except per share amounts</b>				
	<b>Three Months Ended</b>			
	<b>June 30, 2015</b>	<b>March 31, 2015</b>	<b>December 31, 2014</b>	<b>September 30, 2014</b>
	\$	\$	\$	\$
Revenue	9,992	7,955	9,440	13,431
Gross Profit	2,215	1,029	1,261	3,193
EBITDA	(1,699)	(3,518)	(2,957)	(1,366)
Adjusted EBITDA	(1,298)	(2,898)	(2,957)	(1,366)
Net loss	(2,668)	(5,750)	(4,946)	(2,864)
Basic and diluted loss per share	(0.14)	(0.31)	(0.26)	(0.15)

Fiscal 2015 was characterized as a year of significant transition and change, and as such the Company incurred one-time costs which were essential to effect the reorganization and transition. These expenses included costs for the newly appointed executives and key sales people, as well as pursuing additional business opportunities. These costs were treated as one-time non-ordinary costs and excluded from Adjusted EBITDA. In the first quarter of 2015 the Company incurred one-time costs for the termination of several executives in accordance with their employment contract terms.

Revenue for the three months ended June 30, 2016 continued the YOY growth demonstrated in the latter part of fiscal 2015 and into Q1 of fiscal 2016. While Revenue in Q2 2016 was relatively level with Q1 of 2016 (though a 56.7% increase from the comparable quarter in fiscal 2015), improvements were noted in Gross Profit, Gross Margin %, EBITDA and Adjusted EBITDA.

Revenue for the three months ended March 31, 2016 increased by \$2.8 million or 21.6% from the three months ended December 31, 2015. Gross profit increased by \$1.1 million or 35.9% from the previous quarter, benefitting from the growth in Mobile handset sales arising from the continued increased demand from our major customer.

Revenue for the three months ended December 31, 2015 increased by \$0.9 million or 7.3% from the three months ended September 30, 2015. Gross profit increased by \$0.4 million or 14.6% from the previous quarter. The increase in gross profit was as a result of growth in Mobile handset sales, due to an increase in demand from our major customer.

Revenue for the three months ended September 30, 2015 increased by \$2.1 million or 21.1% from the three months ended June 30, 2015. Gross profit increased by \$0.5 million or 23.0% from the previous quarter. The increase in gross profit was as a result of growth in the mobile handset products due to an increase in demand from our major customer and to growth in the Infrastructure product line.

Revenue for the three months ended June 30, 2015 increased by \$2.0 million or 25.6% from the three months ended March 31, 2015. Gross profit increased by \$1.2 million or 115.3% from the previous quarter. This was as a result of growth in sales to Infrastructure and Network customers, coupled with reductions in variable manufacturing costs.

EBITDA and Adjusted EBITDA in the first and second quarter of fiscal 2016 were positive, reversing quarterly losses since fiscal 2013. EBITDA in Q2 of fiscal 2016 showed a \$0.3 million increase from the prior quarter.

While the Adjusted EBITDA loss in the fourth quarter of 2015 was higher than in the third quarter of 2015, the fourth quarter was negatively affected by duplicative costs related to the head office transition, the ramp up of R&D, hiring sales staff to support the growth in certain products areas, and normal year end compensation accrual true up. During the second and the third quarter of 2015 Adjusted EBITDA was comparatively level, though was characterized by the comprehensive reorganization and cost reduction initiatives, and hiring of new staff through all areas.

## **6. Capital Resources and Liquidity**

Our capital resources are in part used to fund working capital associated with product launches, invest in design proposals for our current customers, and the capital investments required to sustain and expand our business and manufacturing capabilities in order to meet customer demands.

### *Liquidity*

Our approach is to ensure, to the extent possible, that we always have sufficient liquidity to meet our liabilities as they become due. We do so by continuously monitoring cash flow, current ratio and actual expenses, all compared to our current liabilities and budgeted expenses. We monitor our cash flow weekly, and other metrics monthly.

As at June 30, 2016, March 31, 2016 and December 31, 2015, we had cash and cash equivalents totaling \$8.1 million, \$6.7 million and \$11.4 million, respectively. At June 30, 2016 we had access to approximately \$6.9 million credit facilities, of which \$2.7 million was utilized. Our ability to effectively utilize bank credit facilities is dependent on our collateral and in accordance with the requirements of the banks servicing our operational subsidiaries. Bank credits for working capital are secured by our subsidiaries' buildings and account receivables from our customers.

During the three months ended June 30, 2016, cash and cash equivalents increased by \$1.4 million mainly due to (i) receipt of deposit on the sale and leaseback of the land and building in Israel of \$0.7 million (sale and leaseback is anticipated to close in Q3 of fiscal 2016), and (ii) receipt of a Harmonized Sales Tax refund related to the Initial Public Offering in 2013 (\$0.3 million).

In the first quarter of fiscal 2016 the Company entered into a new \$4.0 million revolving credit facility with Hong Kong Shanghai Bank Corporation ("HSBC", and the "HSBC Facility"). Any drawing on the HSBC Facility will be fully collateralized by cash, which is deposited in a restricted account with HSBC ("Restricted Cash"), the only use of which is to repay any borrowings under the HSBC Facility. There were no borrowing under this facility as at June 30, 2016.

In the first quarter of fiscal 2016 the Company repaid a portion of the loan outstanding with the First International Bank of Israel ("FIBI") of \$2.9 million, while the remaining amount was repaid in the second quarter of fiscal 2016.

We anticipate that in fiscal 2016, the Company will utilize a portion of its unrestricted cash to (i) deposit cash into the Restricted Cash account to collateralize any borrowings on the HSBC Facility, and (ii) fund working capital requirements, particularly accounts receivables and inventory in support of the anticipated revenue growth in 2016. The Company projects its unrestricted cash, coupled with available credit facilities, will provide sufficient liquidity for the foreseeable future.

### *Cash provided by (used in) operating activities*

Cash used in operating activities for the six months ended June, 2016 was \$1.5 million, a substantial decrease from the \$4.4 million cash used in operating activities in the six months ended June, 2015. The decreased use of cash period over period was mainly driven by positive EBITDA in the current quarter versus the EBITDA loss in the six months ended June 30, 2015.

*Cash provided by (used in) investing activities*

In the six months ended June 30, 2016 we generated \$1.6 million, whereas the cash used in comparable with the first half of fiscal 2015 was \$0.4 million. The improvement in fiscal 2016 was due to the pending sale of the Israel based R&D facility.

*Cash provided by (used in) financing activities*

In the six months ended June 30, 2016, we used \$3.4 million mainly for the repayment bank loans in Israel.

*Working capital requirements*

Working capital requirements are mainly for materials, production, sales and marketing, R&D, operations and G&A expenses. Working capital can be improved (lowered) by increasing sales, decreasing the cost of materials and decreasing the use of subcontractors. Working capital is also impacted by the change in CCC for changes in our customers' and suppliers' payment terms.

Non-cash working capital increased from \$4.9 million as at December 31, 2015 to \$7.1 million as at June 30, 2016. The increase in working capital was primarily due to (i) increased levels of accounts receivables and inventory though partially offset by (ii) an increase in trade payables due to the higher production volumes in the current quarter.

The current ratio was 1.7:1 and 1.5:1 as of June 30, 2016 and December 31, 2015, respectively. The improvement in current ratio was the result of the factors cited above regarding the increase in working capital, particularly the increases in Accounts Receivables and Inventory.

*Trade receivables, net*

Trade receivables, net were \$11.0 million as at June 30, 2016, compared to \$12.6 million as at March 31, 2016. The decrease was attributable to a more consistent, ongoing focus on reducing overdue balances and tighter customer credit terms.

*Inventory*

Inventory as at June 30, 2016 was \$7.8 million, compared to \$6.2 million as at March 31, 2016. The higher level of inventory was as a result of the normal seasonal inventory build for the second half of fiscal 2016. We anticipate inventory levels to decline over the balance of fiscal 2016.

*Trade and other payables*

Trade payables and other liabilities as at June 30, 2016 were \$14.3 million compared to \$13.8 million as at March 31, 2016. The increase was attributable to the higher production volumes associated with the inventory build as noted above.

*Commitments for capital expenditures*

See "Debt - Finance Lease Obligations and Equipment Loan" below for a discussion of our only commitment for capital expenditure as of June 30, 2016.

**Credit Facilities**

See section "Debt" below for a discussion of our credit facilities as at June 30, 2016.

*Contractual Commitments and Contingencies*

We are not aware of any other liabilities or contingencies, other than those presented under this section that could materially affect our future business.

*Debt*

## Loans and credit from banks:

At June 30, 2016 the Company had credit facilities with banks domiciled in Canada, China and Korea (collectively the "Credit Facilities"). These Credit Facilities are revolving and renewable by the banks for a period up to twelve months. The bank credit we maintain in China is renewable in February, March and August of every year. The bank credit we maintained in Israel, as noted above, was fully repaid in Q2 2016. These credit facilities bear interest at an annual rate of 3.6%-5.9% subject to the currency of the loan and are collateralized by trade receivables, property, plant and equipment.

In Q1 fiscal 2016 the Company entered into a new \$4.0 million revolving credit facility with Hong Kong Shanghai Bank Corporation ("HSBC", the "HSBC Facility"). Any drawing on the HSBC Facility will be fully collateralized by Cash which is deposited in a restricted account with HSBC ("Restricted Cash"), the only use of which is to repay any borrowings under the HSBC Facility.

In Q1 fiscal 2016 the Company repaid a portion of the loan outstanding with the First International Bank of Israel ("FIBI") of \$ 2.9 million. The remaining amount was repaid in Q2 2016.

## Trade and other accounts payables:

As of June 30, 2016, the accounts payable and accrued liabilities were \$14.3 million and will be paid in the ordinary course of business from working capital throughout the second half of Fiscal 2016. As of June 30, 2016, cash and trade receivables amounted to \$8.1 million and \$11.0 million, respectively.

## Finance lease obligations and equipment loan:

In Fiscal 2013, we committed to finance lease obligations and an equipment loan for manufacturing equipment funding in Galtronics Electronics (Wuxi) Co., Ltd. ("Galtronics China") and Galtronics Korea Ltd. ("Galtronics Korea") for specialized manufacturing equipment. The total amount of the finance lease obligations and equipment loan was approximately \$7.2 million for a period of 32 months bearing a weighted average interest rate of 8.0% per annum. As of June 30, 2016, the finance lease obligations were fully discharged.

Other than being subject to covenants in loan agreements, there are no other risks for contractual defaults.

*Limitations on dividend distribution from Galtronics China*

In accordance with applicable Chinese laws, Galtronics China is only permitted to distribute up to 90% of its after-tax earnings. As of March 31, 2016, amounts restricted from distribution, which constitute 10% of Galtronics China's retained earnings, amounted to approximately \$0.8 million.

**7. Contingencies***Commitments*

Galtronics China previously entered into a rental agreement for the premises in China for a five-year period ending in 2016.

Galtronics Korea had entered into rental agreements for three premises in South Korea. As part of the cost reduction initiatives, the Company consolidated the three premises into one effective September 1, 2015, with a rental period that ends in 2017. All amounts related with the consolidations have been recorded in the three months ended June 30, 2015 and include rental fees, warehousing consolidation and write-off of leasehold improvements amounting to \$0.1 million.

Galtronics Israel entered into two rental agreements in Arizona, United States for offices and warehouse space, which agreements will end in 2019 and 2017, respectively.

Galtronics Israel entered into an agreement to sell their land and building for \$1.8 million. As part of that transaction, Galtronics Israel agreed to enter into a 3 year lease for 1,000 square meters, commencing on

closing of the transaction, with annual lease payments of \$0.1 million. Galtronics received \$0.7 million in Q2 of 2016 as a security deposit, with the balance of the funds expected on closing in Q3 fiscal 2016.

On April 2014, the Company entered into a rental agreement for premises in Vietnam for a period of five years. The rental period may be extended for up to five years at the Company's option. The company recently amended the lease to return to the lessor a certain area of its leased premises.

On October 2015 the Company had entered into service agreements with a company controlled by the controlling shareholder, for office space, service of certain employees, administrative support and supplies, computers and communication equipment. The agreement automatically renew until December 31, 2016, with a monthly fee totaling \$0.2 million p.a., which may change from month to month depending on the services the Company requires.

The future minimum lease fees payable as of June 30, 2016 are as follows:

('000s)	\$
First year	668
Second through sixth years	743
<b>Total expenses</b>	<b>1,411</b>

#### *Legal Proceedings*

In 2009 Galtronics Israel ("GTI") received notice, for possible indemnification, by one of its major customers (the "customer"), for a claim filed against the customer in relation to several U.S. patent infringements. A jury rendered a judgment against the customer for approximately \$38 million which was subsequently appealed by the customer. The appeal was formally dismissed on April 21, 2014. During the relevant period subject to the claim, GTI was not the major antennas supplier for the customer. Since the notice for possible indemnification, GTI has not received any demand for payment from the customer and it is not clear whether such a demand will ever be received, and if so, what would be the amount of such demand. Management and its legal counsel are unable to assess the outcome of the claim against the customer and the effect, if any, on the Company. Accordingly, no provision was recorded in respect of this demand.

#### *Stock Option Grants*

##### a. Galtronics Share Option Plan:

On July 22, 2013, Galtronics' board of directors adopted the Galtronics Corporation Ltd. 2013 Share Option Plan (the "2013 Plan"). Under the 2013 Plan, Galtronics may grant options or shares to employees, officers, directors, consultants and other service providers of the Company or affiliated companies. 1,500,000 common shares have been reserved for grants pursuant to the 2013 Plan. Unless otherwise determined by the board of directors, the exercise price of options granted shall be the market price of the shares on the date of grant. The options shall generally vest over a period of four years. The options shall expire eight years after the date of grant.

##### Former Chief Executive Officer Grants:

On August 23, 2013, Galtronics' board of directors resolved to grant the Company's then President and Chief Executive Officer 960,000 fully vested shares for no consideration. The share issuance was subject to the Galtronics' 2013 Share Option Plan. The Company recognized share-based compensation in the amount of approximately \$6.1 million included in G&A expenses in the third quarter of Fiscal 2013.

##### Former Chief Technology Officer ("CTO") Grants:

On October 1, 2013, Galtronics' board of directors resolved to grant the Company's then CTO 75,000 fully vested shares for no consideration. The share issuance was subject to the Galtronics' 2013 Share Option Plan. The Company recognized share-based compensation in the amount of approximately \$0.5 million, which was included in R&D expenses in the fourth quarter Fiscal 2013.

Excluding the above mentioned grants, there are no other grants under the 2013 Plan. All future grants will be made pursuant to the Baylin Stock Option Plan.

b. Baylin Stock Option Plan:

The Company adopted a stock option plan effective as of the date of closing of its IPO (the "Stock Option Plan") pursuant to which stock options may be granted to directors, officers, employees and consultants of the Company or its affiliates. The Stock Option Plan will be administered by the Board of Directors, which may delegate this responsibility to a committee of the Board of Directors.

The number of common shares issued and issuable at any time under all security based compensation arrangements of the Company (including the Stock Option Plan), cannot exceed 10% of the number of common shares that are outstanding from time to time (on a non-diluted basis) and the aggregate number of common shares issued upon exercise of stock options granted under the Stock Option Plan and any other share compensation arrangements to insiders and their associates of the Company within a one-year period may not exceed 10% of the common shares then outstanding (on a non-diluted basis). The maximum number of common shares issuable to insiders and their associates at any time pursuant to all security based compensation arrangements cannot exceed 10% of the common shares issued and outstanding from time to time. The Stock Option Plan is considered an "evergreen" plan, since the number of common shares issuable upon exercise of the stock options shall be available for subsequent grants under the Stock Option Plan and the number of stock options available to grant increases as the number of issued and outstanding common shares increases. The number of common shares issuable to any one participant under all security based compensation arrangements of the Company (including the Stock Option Plan) within a one-year period, cannot exceed 5% of the common shares then outstanding (on a non-diluted basis).

All stock options granted shall have an exercise price determined and approved by the board of directors at the time of grant, which shall not be less than the market value of the common shares at such time.

Unless otherwise determined by the board of directors in its discretion at the time stock options are granted, one third of the stock options vest cumulatively on each anniversary of the applicable grant date. Subject to the discretion of the board of directors and as set out below, stock options expire no later than seven years after the date of grant.

On August 24, 2015 the Company's board of directors resolved to grant the Company's President and Chief Executive Officer 925,000 share options subject to the Stock Option Plan. These options vest as follows: (i) 130,000 share options will vest on August 24, 2016, (ii) 130,000 on August 24, 2017. (iii) 240,000 and 425,000 will vest at the discretion of the board of directors, upon recommendation from the Corporate Governance and Compensation Committee, following final review of the performance of the Company for the fiscal years 2015 and 2016, respectively. The options shall expire 5 years following their grant date. As of December 31, 2015, 240,000 options were fully vested.

In the event of change of control over the Company, all unvested share options will be vested immediately.

As for June 30, 2016 the number of share options outstanding is 925,000, with weighted average exercise price of CAD \$1.51. The remaining weighted average contractual life of the share options is 4.33 years.

The fair value of the share options is estimated at the grant date using a Black & Scholes option pricing model, taking into account the terms and conditions upon which the share options were granted.

Expected volatility of the share prices (%)	44.42-45.29
Risk-free interest rate (%)	0.9
Expected life of share options (years)	2.67-3.25
Share price (CAD)	1.50
Option fair value at the grant date (CAD)	0.44-0.48

c. Directors' Deferred Share Unit Plan:

The Company adopted a deferred share unit plan (the "DSU Plan") dated November 27, 2013, which plan will form part of its long-term incentive compensation arrangements for directors. The number of deferred share units ("DSUs") issuable under the DSU Plan at any time must not exceed 500,000 units.

The DSU Plan provides that directors may elect to receive all or a portion that is no less than fifty percent (50%) of their annual retainers (each, an "Annual Retainer") in DSUs. If no election is made in accordance with the terms of the DSU Plan, a deemed election of 50% shall apply. The portion or percentage of an Annual Retainer to be granted as DSUs, as elected or deemed to be elected in accordance with the terms of the DSU Plan, will be determined on the first business day each month of the fiscal year for which such Annual Retainer is payable, and the number of DSUs to be granted shall be based on each completed month of active employment. The DSU grant shall be settled by issuance of common shares on the date that such participant ceases to be a director of the Company and its subsidiaries.

The following table lists the number of DSU during the current year:

	Number of DSU	Weighted average price in CAD \$
DSUs outstanding as of December 31, 2015	139,423	3.50
DSUs granted during Fiscal 2016	43,722	1.98
DSUs outstanding as of June 30, 2016	183,145	2.71

#### 8. *Off-Balance Sheet Arrangements*

We have not created, and are not party to, any special purpose or off-balance sheet entities for the purpose of raising capital, incurring debt or operating our business. We do not have any relationships or arrangements with entities that are not consolidated into our financial statements that are reasonably likely to materially affect liquidity or the availability of capital resources.

#### 9. *Significant Transactions with Related Parties*

Shared Services Agreement – In September 2012, Galtronics entered into a shared services agreement (the "Shared Services Agreement") with Medimor, a company controlled by an affiliate of our Principal Shareholder, pursuant to which Medimor agreed to lease 500 square meters of office space from the corporate offices of Galtronics at 1 Tsvonit St., Upper Tiberias Industrial Zone. The term of the Shared Services Agreement will continue until terminated by either party and the rent payable by Medimor to Galtronics is NIS 14,200/month (approximately \$4,100/month). Pursuant to the Shared Services

Agreement, Galtronics and Medimor share, on a pro rata basis, certain overhead costs associated with the premises. For Fiscal 2014 and 2015, the amounts Galtronics recorded for shared services transactions granted to Medimor were not material.

President & CEO Agreement - On August 24, 2015, the board of directors appointed Mr. Randy Dewey as President and Chief Executive Officer (the "CEO"). The Company entered into an executive employment agreement with the CEO effective of April 1, 2015 for (i) annual remuneration of CAD \$425,000 base salary, (ii) participation in the Company's group insurance benefits plan available to other senior executives, and be entitled to bonuses in the consideration of stock options as described previously in the Stock option plan section. According with the terms of the agreement the executive will be entitled to Exit Event Bonus (EEB) as a one-time special bonus to be paid to the Executive upon a Change of Control of the Company. The consideration of the EEB will be equal up to two times Base Salary (less required deductions) to be paid in cash or securities of the Company as determined by the Board and immediate vesting of any unvested share options as previously mentioned.

In October 2015 the Company entered into service agreements with a company controlled by its principal shareholder, for office space, service of certain employees, administrative support and supplies, computers and communication equipment. The agreement automatically renewed until December 31, 2016, with a monthly fee totaling \$0.2 million p.a., which may change from month to month depending on the services the Company requires. This agreement was approved by the independent directors.

#### ***10. Critical Accounting Estimates and Accounting Policies***

This discussion and analysis of financial condition and results of operations is based on our consolidated financial statements, which have been prepared in accordance with IFRS as issued by the IASB. Significant accounting policies are described in note 2 to the audited consolidated financial statements.

The preparation of the consolidated financial statements requires management to make judgments, estimates and assumptions that affect the reported amounts of assets, liabilities, revenue and expenses. Significant accounting policies employed by us, including the use of estimates, are presented in the notes to the consolidated financial statements. We periodically evaluate our estimates, which are based on historical experience and on various other assumptions that management believes to be reasonable under the circumstances.

Critical accounting policies are those that are most important to the portrayal of our financial condition and results of operations and require management's subjective or complex judgments, resulting in the need for management to make estimates about the effect of matters that are inherently uncertain. If actual performance should differ from historical experience or if the underlying assumptions were to change, our financial condition and results of operations may be materially impacted.

While significant accounting policies are more fully described in note 2 to our audited consolidated financial statements, we believe that the following accounting policies are the most critical to fully understanding and evaluating our financial condition and results of operations:

##### ***Inventory Valuation***

We evaluate inventory balances on an ongoing basis and record a necessary provision for slow-moving or obsolete inventory.

In performing this review, we consider factors such as forecasted sales, demand requirements, product lifecycles and product development plans, quality issues and current inventory levels. If future demand or market conditions for our products are less favorable than forecasted or if unforeseen technological changes occur, we may be required to record write-downs which would negatively affect gross margins in the period when write-downs are recorded and our operating results and financial position could be adversely affected.

The inventory valuation influences the inventory balance and cost of revenue.

***Post-employment Benefits Liabilities***

We operate defined benefit plans in respect of severance, retirement and other local labor laws relevant to post-employment benefit liabilities in operational sites in Israel and South Korea. A portion of post-retirement benefit plans are financed by contributions to insurance companies and classified as defined contribution plans or as defined benefit plans.

The present value of post-employment benefits liabilities depends on a number of factors that are determined on an actuarial basis using a number of assumptions. The assumptions used in determining the net cost or income for severance pay and plan assets include a discount rate. Any changes in these assumptions will impact the carrying amount of severance pay and plan assets. Other key assumptions inherent to the valuation include employee turnover, inflation and future payroll increases.

These assumptions are based on independent actuarial advice and are updated on an annual basis. Actual circumstances may vary from these assumptions, giving rise to a different severance pay liability.

Post-employment benefits influence current and non-current liabilities and payrolls for all cost categories.

***Share-based compensation transactions***

The cost of equity-settled transactions with employees is measured at the fair value of the equity instruments granted at grant date. The fair value is determined using an acceptable option pricing model.

As for other service providers, the cost of the transactions is measured at the fair value of the goods or services received as consideration for equity instruments. In cases where the fair value of the goods or services received as consideration of equity instruments cannot be measured, they are measured by reference to the fair value of the equity instruments granted.

The cost of equity-settled transactions is recognized in profit or loss, together with a corresponding increase in equity, during the period in which the performance and/or service conditions are satisfied, ending on the date on which the relevant employees become fully entitled to the award (the "vesting period"). The cumulative expense recognized for equity-settled transactions at the end of each reporting period until the vesting date reflects the extent to which the vesting period has expired and the Company's best estimate of the number of equity instruments that will ultimately vest. The expense or income recognized in profit or loss represents the change between the cumulative expense recognized at the end of the reporting period and the cumulative expense recognized at the end of the previous reporting period.

No expense is recognized for awards that do not ultimately vest, except for awards where vesting is conditional upon a market condition, which are treated as vesting irrespective of whether the market condition is satisfied, provided that all other vesting conditions (service and/or performance) are satisfied.

If the Company modifies the conditions on which equity-instruments were granted, an additional expense is recognized for any modification that increases the total fair value of the share-based payment arrangement or is otherwise beneficial to the employee/other service provider at the modification date.

If a grant of an equity instrument is cancelled, it is accounted for as if it had vested on the cancellation date, and any expense not yet recognized for the grant is recognized immediately. However, if a new grant replaces the cancelled grant and is identified as a replacement grant on the grant date, the cancelled and new grants are accounted for as a modification of the original grant, as described above.

***Accounting for Income Taxes***

At the end of each reporting period, we are required to estimate income taxes, deferred income taxes and tax credit assets. There are transactions and calculations for which the ultimate tax determination is uncertain during the ordinary course of business as a result of being determined according to complex tax laws and regulations as well as assessing the probability of future realization of deferred taxes and tax credit assets. Where the effect of these laws and regulations is unclear, we use estimates in

determining the liability for the tax to be paid on past profits, which we recognize in our financial statements. We believe the estimates, assumptions and judgments are reasonable, but this can involve complex issues which may take a number of years to resolve. Where the final tax outcome of these matters is different from the amounts that were initially recorded, such differences will impact the income tax and deferred income tax provisions in the period in which such determination is made.

#### ***Impairment of non-financial assets***

We conduct our annual impairment assessment of property, plant and equipment in the fourth quarter of each year (which corresponds to our annual planning cycle), and whenever events or changes in circumstances indicate that the carrying amount of an asset or Cash Generating Unit ("CGU") may not be recoverable.

We recognize an impairment loss when the carrying amount of an asset or CGU exceeds its recoverable amount, which is measured as the greater of its value-in-use and its fair value less costs to sell. The Company operates as one CGU.

The Company used professional assessors to determine the value of its property, plant and equipment at each of its locations. Following this analysis, the Company determined that the recoverable amounts exceed the carrying amounts as of December 31, 2015 and therefore no impairment was recognized.

#### ***11. Adoption of New Accounting Standards and Disclosure of New Standards in the Period Prior to Their Adoption***

Disclosure of new standards in the period prior to their adoption:

##### **IFRS 15, "Revenue from contracts with customers":**

The IASB published IFRS 15, "Revenue from contracts with customers". IFRS 15 replaces IAS 18 "Revenue" and several other revenue recognition related standards.

The IFRS 15 introduces a five-step model that will apply to revenue earned from contracts with customers:

Step 1: Identify the contract with a customer, including reference to contract combination and accounting for contract modifications.

Step 2: Identify the separate performance obligations in the contract.

Step 3: Determine the transaction price, including reference to variable consideration, financing components that are significant to the contract, non-cash consideration and any consideration payable to the customer.

Step 4: Allocate the transaction price to the separate performance obligations on a relative stand-alone selling price basis using observable information, if it is available, or using estimates and assessments.

Step 5: Recognize revenue when the entity satisfies a performance obligation over time or at a point in time.

IFRS 15 is to be applied retrospectively for annual periods beginning on or after January 1, 2018. Early adoption is permitted. IFRS 15 allows an entity to choose to apply a modified retrospective approach, according to which IFRS 15 will only be applied in the current period presented to existing contracts at the date of initial application. No restatement of the comparative periods will be required as long as the disclosures required by IFRS 15 are included.

The Company is evaluating the possible impact of IFRS 15 but is presently unable to assess its effect, if any, on the financial statements.

##### **IFRS 9, "Financial Instruments":**

In July 2014, the IASB issued the final and complete version of IFRS 9, "Financial Instruments" ("IFRS 9"), which replaces IAS 39, "Financial Instruments: Recognition and Measurement". IFRS 9 mainly

focuses on the classification and measurement of financial assets and it applies to all assets in the scope of IAS 39.

According to IFRS 9, all financial assets are measured at fair value upon initial recognition. In subsequent periods, debt instruments are measured at amortized cost only if both of the following conditions are met:

- The asset is held within a business model whose objective is to hold assets in order to collect the contractual cash flows.
- 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.

Subsequent measurement of all other debt instruments and financial assets should be at fair value. IFRS 9 establishes a distinction between debt instruments to be measured at fair value through profit or loss and debt instruments to be measured at fair value through other comprehensive income.

Financial assets that are equity instruments should be measured in subsequent periods at fair value and the changes recognized in profit or loss or in other comprehensive income (loss), in accordance with the election by the Company on an instrument-by-instrument basis. If equity instruments are held for trading, they should be measured at fair value through profit or loss.

According to IFRS 9, the provisions of IAS 39 will continue to apply to derecognition and to financial liabilities for which the fair value option has not been elected.

According to IFRS 9, changes in fair values of financial liabilities which are attributable to the change in credit risk should be presented in other comprehensive income. All other changes in fair value should be presented in profit or loss.

IFRS 9 also prescribes new hedge accounting requirements.

IFRS 9 is to be applied for annual periods beginning on January 1, 2018. Early adoption is permitted.

The Company is evaluating the possible impact of IFRS 9 but is presently unable to assess its effect, if any, on the financial statements.

Amendments to IAS 7, "Statement of Cash Flows", regarding additional disclosures of financial liabilities:

In January 2016, the IASB issued amendments to IAS 7, "Statement of Cash Flows", ("the amendments") which require providing additional disclosures of financial liabilities. The amendments require presenting the movement between the opening balance and the closing balance of financial liabilities, including changes arising from cash flows from financing activities, changes arising from obtaining or losing control in investees, the effect of changes in foreign exchange rates and changes in fair value.

The amendments are effective for annual periods beginning on or after January 1, 2017. No disclosure is required for comparative figures in previous periods before the effective date of the amendments. Earlier application is permitted.

The Company will include the necessary disclosures in the financial statements when applicable.

IFRS 16, "Leases":

In January 2016, the IASB issued IFRS 16, "Leases", ("the new Standard"). According to the new Standard, a lease is a contract, or part of a contract, that conveys the right to use an asset (the underlying asset) for a period of time in exchange for consideration.

According to the new Standard:

- In respect of all leases, lessees are required to recognize an asset against a liability in the statement of financial position (except in certain cases) similarly to the accounting treatment of finance leases according to the existing IAS 17, "Leases".
- Lessees are required to initially recognize a lease liability for the obligation to make lease payments and a right-of-use asset for the right to use the underlying asset for the lease term. Interest expenses and depreciation expenses will be recognized separately.
- Variable lease payments that are not CPI or interest dependent based on performance or use (such as percentage of turnover) will be recognized as expenditure by the lessees or as income by the lessors as incurred.
- In the event of change in variable lease payments that are CPI-linked, lessees will reevaluate the lease liability and the effect of the change will be carried to the right-of-use asset.
- The new Standard prescribes two exceptions according to which lessees are permitted to make an election, on a lease-by-lease basis, to apply a method similar to current operating lease accounting to leases for which the underlying asset is of low value or leases with a lease term of 12 months or less.
- Lessors' accounting treatment remains substantially unchanged, namely classification of the lease as finance lease or operating lease.
- The new Standard is effective for annual periods beginning on or after January 1, 2019. Earlier application is permitted provided that IFRS 15, "Revenue from Contracts with Customers", is simultaneously applied.
- The new Standard permits lessees to use either a full retrospective or a modified retrospective approach on transition for leases existing at the date of transition, with options to use certain transition reliefs whereby no restatement of comparative figures is required.

The Company is studying the possible effect of the new Standard. At this stage, the Company is unable to quantify the impact on the financial statements.

## ***12. Financial Instruments and Risk Management***

### ***Financial Risk Factors:***

Our activities expose us to various financial risks such as foreign exchange risk, interest rate risk and credit risk and liquidity risk, as discussed below. Our comprehensive risk management plan focuses on activities that reduce to a minimum any possible adverse effects on our consolidated financial performance.

### ***Market risk:***

#### ***Foreign exchange risk:***

The major portion of revenue is earned in USD, as such, the financial statements of the Company are reported in USD. The other portions are earned in other currencies such as Chinese Yuan Renminbi ("RMB") and South Korean Won ("KRW"). However, these portions are USD driven since customers total product costing is USD based. A portion of the operating costs are realized in currencies other than the functional currencies of relevant entities. As a result, we are exposed to currency risk on these operations. Also, additional earnings volatility arises from the translation of monetary assets and liabilities denominated in foreign currencies at the rate of exchange at the end of each reporting period, the impact of which is reported as a foreign exchange gain or loss in finance expenses.

Our objective in managing currency risk is to minimize exposure to currencies other than functional currency. Our policy is to match foreign denominated assets with foreign denominated liabilities.

*Interest rate risk:*

We believe that interest rate risk is low as our short and long-term loans have either fixed rates or variable interest rates determined by reference to the LIBOR. The LIBOR rate fluctuations in Fiscal year 2015 and in Fiscal year 2014 were minor. Based on our experience in Israel and China in the past few years, the interest rate was relatively steady in areas where debt was highly concentrated.

*Credit risk:*

A significant portion of our products are sold to major equipment manufacturers of consumer electronics products. These major customers are located primarily in North America, Europe and East Asia. We perform ongoing credit evaluations of the customers. We have a policy of selling our products to customers with an appropriate credit history.

We extend 30-90 day credit terms to our customers and regularly monitor the credit extended to such customers and their general financial condition but do not require collateral as security for these receivables. We provide an allowance for doubtful accounts based on the factors that affect the credit risk of certain customers, past experience and other information.

We maintain cash and cash equivalents and other financial instruments in various financial institutions. These financial institutions are located in different geographical areas near our subsidiaries. Accord to our policy, the relative credit stability of the various financial institutions is evaluated on a regular basis.

We recognize a significant portion of our revenue from a limited number of customers. The loss of, or a significant reduction in, orders from one or more of our major customers would adversely affect our business, results of operations and financial condition. We recognized an aggregate of 58% and 64% of our revenue from our top three customers for the Fiscal year 2015 and 2014, respectively. In particular, we received 43% and 47% of revenue, directly and indirectly, from Samsung and its subcontractors for the year ended December 31, 2015 and 2014, respectively, and 58% in the first quarter of 2016. The reduction in customer concentration is due to the decreased revenue we experienced from our major customer in the mobile area combined with a diversification of revenue experienced in other business areas. We continue our efforts to reduce the dependency on a limited number of customers by expanding our product portfolio and enlarging our sales and marketing efforts. The top three customers in any given year may not be the same top three customers in a previous or subsequent year.

*Liquidity risk:*

We monitor our liquidity risk through use of quarterly budgets and cash flow projection tools. The objective is to maintain sufficient liquidity by a combination of cash on hand, borrowings under our Credit Facilities, and generating operating cash flow.

### ***13. Outstanding Share Data***

As of May 3, 2015, the Company had 18,733,919 fully paid and non-assessable Common Shares issued and outstanding. There has been no change in the number of fully paid and non-assessable Common Shares issued and outstanding since the Company's initial public offering on November 27, 2013.

### ***14. Internal Controls Over Financial Reporting***

Management is responsible for the design and operating effectiveness of internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of the financial statements in accordance with IFRS. Based on a review of the Company's internal control procedures, management believes its internal controls and procedures are appropriately designed as at March 31, 2016.

No significant changes in the Company's internal control over financial reporting occurred during the three months ended March 31, 2016 that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

**Disclosure Controls and Procedures**

Management is also responsible for the design and effectiveness of disclosure controls and procedures to provide reasonable assurance that material information related to the Company, including its consolidated subsidiaries, is made known to the Company's certifying officers. The Company's Interim President and Chief Executive Officer and Chief Financial Officer have each evaluated the design of the Company's disclosure controls and procedures as at March 31, 2016 and have concluded that these controls and procedures were appropriately designed.

***15. Additional Information***

Additional information relating to the Company, including the most recently filed Annual Information Form, is available on SEDAR at [www.sedar.com](http://www.sedar.com).

***16. Risk Factors***

For a detailed description of risk factors associated with the Company, refer to the "Risk Factors" section of the Company's Annual Information Form filed on SEDAR on March 9, 2016.