## MANAGEMENT'S DISCUSSION AND ANALYSIS

**of**

## First Quarter Report
## April 30, 2011

The following management's discussion and analysis ("MD&A") of the financial condition and results of operations for the quarters ended April 30, 2011 and April 30, 2010 of Discovery Air Inc. ("Discovery Air" or the "Corporation") should be read in conjunction with the unaudited consolidated financial statements and related notes of the Corporation for the three months ended April 30, 2011 and the annual audited consolidated financial statements and related notes for the year ended January 31, 2011, which are available on SEDAR at www.sedar.com. On February 1, 2011, the Corporation adopted International Financial Reporting Standards ("IFRS") for financial reporting purposes using a transition date of February 1, 2010. The interim financial statements for the three months ended April 30, 2011, including required comparative information, have been prepared in accordance with International Financial Reporting Standards 1, *First-time Adoption of International Financial Reporting Standards,* and with International Accounting Standard ("IAS") 34, *Interim Financial Reporting* as issued by the International Accounting Standards Board ("IASB"), and are reported in Canadian dollars. Previously, the Corporation prepared its Interim and Annual Consolidated Financial Statements in accordance with Canadian generally accepted accounting principles. Unless otherwise noted, fiscal 2011 comparative information has been prepared in accordance with IFRS.

***Financial Definitions***

In this MD&A, the following financial terms have the meanings ascribed to them below:

(a) "EBITDA" means earnings before interest, taxes and depreciation;
(b) "EBITDAR" means EBITDA before aircraft lease costs;
(c) "Fiscal 2012" means the fiscal year of the Corporation ending January 31, 2012;
(d) "Fiscal 2011" means the fiscal year of the Corporation ending January 31, 2011;
(e) "Fiscal 2010" means the fiscal year of the Corporation ending January 31, 2010;
(f) "Q1/12", "Q2/12", "Q3/12" and "Q4/12" mean the first, second, third and fourth quarters, respectively, of Fiscal 2012;
(g) "Q1/11", "Q2/11", "Q3/11" and "Q4/11" mean the first, second, third and fourth quarters, respectively, of Fiscal 2011; and
(h) "Q1/10", "Q2/10", "Q3/10" and "Q4/10" mean the first, second, third and fourth quarters, respectively, of Fiscal 2010.

## *Business Profile*

Discovery Air, founded in 2004, is a specialty aviation services company operating across Canada and in select markets internationally. With over 140 aircraft, it is one of the largest aircraft operators in Canada, employing during its peak periods over 600 flight crew, maintainers and support staff working to deliver a variety of air transport and logistics solutions to a wide range of government and business customers. Discovery Air offers fixed-wing and rotary-wing capabilities and aircraft maintenance services, as well as logistics and remote operations management services. These services are provided through the following subsidiaries of the Corporation: Top Aces Inc. ("Top Aces"), which delivers airborne training and special mission services to the Canadian military; Hicks & Lawrence Limited ("Hicks"), a supplier of airborne fire management services to the Ontario government and charter services to government agencies and corporate customers; Discovery Air Technical Services Inc. ("Technical Services"), which provides a range of maintenance, repair, overhaul, modification, engineering and certification services ("MRO"); Great Slave Helicopters Ltd. ("Great Slave"), one of the largest VFR helicopter operators in Canada; Air Tindi Ltd. ("Air Tindi") the largest fixed-wing aircraft charter provider based in Northern Canada; Discovery Mining Services Ltd. ("Discovery Mining"), which supplies all-weather exploration camps as well as expediting and logistics support services; and Discovery Air Innovations Inc. ("Innovations"), the innovation arm of Discovery Air that identifies and captures large, new market opportunities.

## *Selected Financial Information*

| (thousands of dollars, except per share amounts) | Q1/12 (unaudited) | Q1/11 (unaudited) |
|---|---|---|
| **Results of operations** | | |
| Revenue | $ 37,249 | $ 25,815 |
| Expenses | $ 32,457 | $ 23,459 |
| Depreciation of property and equipment and intangible assets | $ 4,503 | $ 4,384 |
| Earnings (loss) before undernoted items | $ 289 | $ (2,028) |
| | | |
| Finance costs | $ 3,752 | $ 3,547 |
| Loss and comprehensive loss | $ (2,586) | $ (3,929) |
| Basic and diluted loss per common share: | $ (0.02) | $ (0.03) |
| | | |
| **Financial position and liquidity** | | |
| Total assets | $ 264,740 | $ 256,532 |
| Total loans and borrowings | $ 139,274 | $ 144,212 |
| Cash used in operations | $ (10,397) | $ (9,538) |
| Working capital | $ (28,752) | $ 11,855 |
| | | |
| **Key non-IFRS performance measures*** | | |
| EBITDAR | $ 6,770 | $ 4,033 |
| EBITDA | $ 4,766 | $ 2,433 |
| EBITDA Margin | 13% | 9% |

* See Non-IFRS measures

## *Segmented information*

Through six operating subsidiaries, Discovery Air offers fixed-wing and rotary-wing capabilities, logistics and remote operations management services and aircraft maintenance and repair and overhaul services. Discovery Air has two reportable business segments: Government Services and Northern Services.

The Corporation's Government Services segment includes three subsidiaries. Top Aces delivers airborne training and special mission services to the Canadian military. Top Aces provides close air support training to the Canadian Army, as well as maritime support, electronic warfare training and target tow services to the Canadian Navy. Top Aces also delivers adversary fighter support, target tow and electronic warfare training support to the Canadian Air Force. Most electronic warfare training is accomplished with military personnel on board Top Aces' aircraft. Hicks is a primary supplier of airborne fire management services to the Ontario government, and also provides charter service to government agencies and corporate customers throughout northern Ontario. Technical Services provides a range of aircraft maintenance, repair and overhaul, modification, engineering and certification services from its Quebec City location.

Discovery Air's Northern Services segment includes three subsidiaries. Great Slave, the second-largest VFR helicopter operator in Canada, has bases throughout northern Canada from which it operates support flights for mining and oil and gas seismic and exploration work, forest fire suppression, aerial construction and precision external load applications and environmental impact surveys. Air Tindi utilizes a varied fleet of fixed-wing aircraft to provide vital air ambulance services and to operate both scheduled and charter cargo and passenger flights to remote areas of northern Canada. Finally, Discovery Mining constructs and rents all-weather exploration camps and provides expediting and logistical support services.

All activities that are not allocated to these two business segments are reported under Corporate Support including Discovery Air Innovations.

## *Seasonality and quarterly fluctuations*

The Corporation's businesses are, to varying degrees, seasonal in nature. Seasonality and other factors can affect the comparability of results from one period to another, particularly from quarter to quarter.

- In Canada, there is normally increased demand for the services provided by the Northern Services segment and Hicks commencing in the spring and continuing through to the end of the summer.
- Top Aces' revenue-generating opportunities are usually significantly higher in the February - June and September - November time periods. Though Top Aces' revenues are relatively predictable over a twelve-month period, they can

vary substantially from month to month depending largely on the customers' training priorities and, on occasion, weather conditions.

- The Corporation attempts to perform most major repairs and refurbishments during the slower periods of revenue-generating activity. As well, repairs and maintenance on aircraft are not required evenly throughout the year and the timing of related expenses within a year may vary from one period to another.
- Weather conditions can have an impact on flight activity from one period to another, especially in the forest fire suppression businesses.

## *Results of operations for Q1/12 and Q1/11*

| (thousands of dollars) | Q1/12 (unaudited) | | | | Q1/11 (unaudited) | | | |
|---|---|---|---|---|---|---|---|---|
| | Northern Services | Government Services | Corporate Support | Total | Northern Services | Government Services | Corporate Support | Total |
| **Revenue** | **$ 18,547** | **$ 18,702** | **$ -** | **$ 37,249** | **$ 15,382** | **$ 10,433** | **$ -** | **$ 25,815** |
| Expenses | 18,447 | 12,204 | 1,806 | 32,457 | 14,454 | 7,359 | 1,646 | 23,459 |
| **Earnings (loss) before undernoted items** | **$ 100** | **$ 6,498** | **$ (1,806)** | **$ 4,792** | **$ 928** | **$ 3,074** | **$ (1,646)** | **$ 2,356** |
| Depreciation of property and equipment and intangible assets | $ 2,380 | $ 2,107 | $ 16 | $ 4,503 | $ 2,576 | $ 1,792 | $ 16 | $ 4,384 |
| Finance costs | | | | 3,752 | | | | 3,547 |
| Loss on sale of property and equipment | | | | 255 | | | | - |
| Share of (earnings) loss of equity accounted investees (net of income tax) | | | | (229) | | | | (77) |
| Income tax provision | | | | (903) | | | | (1,569) |
| **Earnings and comprehensive income** | | | | **(2,586)** | | | | **(3,929)** |
| **EBITDA** | **$ 100** | **$ 6,498** | **$ (1,806)** | **$ 4,766** | **$ 928** | **$ 3,074** | **$ (1,646)** | **$ 2,433** |
| **Capital expenditures** | **$ 2,425** | **$ 5,369** | **$ 18** | **$ 7,812** | **$ 1,341** | **$ 543** | **$ 30** | **$ 1,914** |
| | **As at April 30 2011** | | | | **As at April 30, 2010** | | | |
| **Total assets** | **$ 131,136** | **$ 128,583** | **$ 5,021** | **$ 264,740** | **$ 138,412** | **$ 115,545** | **$ 2,575** | **$ 256,532** |
| **Goodwill** | **$ -** | **$ 37,862** | **$ -** | **$ 37,862** | **$ -** | **$ 37,862** | **$ -** | **$ 37,862** |
| **Intangible assets** | **$ 7,392** | **$ 10,657** | **$ -** | **$ 18,049** | **$ 9,540** | **$ 12,942** | **$ -** | **$ 22,482** |

## *Consolidated results*

### *Revenue and Hours Flown*

Revenue was $37.2 million for Q1/12, compared to $25.8 million for Q1/11, a 44% increase. The Corporation's revenue, which is largely driven by flight hours, is primarily generated from aviation transportation services that are delivered through its subsidiaries. Revenues from non-flight hour sources include revenue of Discovery Mining and of Technical Services, scheduled passenger services to remote communities provided by Air Tindi and the basing, standby and minimum fees that are typical of government contracts, such as those held by Top Aces, Hicks, and, to a lesser extent, Great Slave. Revenue generated from flight hours for Q1/12 was $28.9 million (78% of total revenue), compared to $20.9 million (81% of total revenue) for Q1/11. Hours flown in Q1/12 were 10,106 compared to 8,542 for the prior year, representing an 18% increase. The Northern Services and Government Services segments recorded year-over-year increases in revenue of 21% and 79%, respectively in Q1/12. The Northern Services segment's increase in revenue reflects continuing strong activity from the segment's resource-based customers both in Northern Canada and Peru. The Government Services segment's increase in revenues was a result of increased flight hours in the quarter to support the Canadian military's airborne training and special mission services and the year-over-year incremental revenue contribution from MRO services provided by Technical Services, which began operations in late Fiscal 2011.

The Corporation's Q1/12 revenue reflects a continuing positive increase over the comparative period contribution from all major industry sectors as noted in Fiscal 2011. With increased flight hours generated from the Canadian military in Q1/12, revenue from the government sector represented the largest year-over-year increase in Q1/12. As a percentage, this sector increased by 35% compared to Q1/11. Revenues from the Corporation's mining exploration, mining production and oil and gas sectors combined reflect a 41% increase over the comparative period. The increase in the resource-based sectors was led by strong contribution from the oil and gas sector work in Peru.

*Expenses*
Expenses were $32.5 million for Q1/12, compared to $23.5 million for Q1/11, a 38% increase. Expenses consist of operating fixed and variable expenses, which includes crew and fleet related costs, as well as general and administrative expenses. The increase in expenses was attributable to the following factors:

- increased direct costs associated with higher revenue;
- seasonal ramp up cost associated with preparation for the upcoming peak season activity;
- incremental costs related to Technical Services which began operations in Q2/11;
- increased utilization of leased aircraft; and,
- higher wage rates to remain competitive in the skilled labour market.

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Crew and fleet related costs are the largest operating expense categories. Crew related costs, consisting primarily of wages, benefits, travel and training for pilots and maintenance engineers, totaled $11.2 million for Q1/12, compared to $7.8 million for the prior year, representing a 44% increase. Fleet related costs consist primarily of aircraft lease costs, fuel, maintenance costs and facility costs. Fleet related costs for Q1/12 were $12.5 million compared to $8.4 million for the prior year, representing a 49% increase. While fuel costs represent a significant component of the Corporation's operating expenses, the Corporation recovers substantially all of these and other recoverable costs from its customers. These recoveries are classified as revenue. The historically high level of fuel recovery has greatly mitigated the impact of rising fuel prices on the Corporation's earnings. Depreciation of capitalized overhaul and major inspection costs relate to aircraft components previously included in fleet related costs under CGAAP is now reflected in depreciation under IFRS. General and administrative expenses are mainly wages and benefits of administrative personnel, facility costs, travel costs, insurance costs and other overhead expenses. For Q1/12, these costs were $8.7 million compared to $7.3 million for Q1/11. The 19% increase was largely attributable to staff hiring and increased infrastructure in support of operating activities.

*EBITDA and EBITDAR (see Non-IFRS Measures)*
EBITDA was $4.8 million for Q1/12, compared to $2.4 million for Q1/11. EBITDA margin for Q1/12 was 13% compared to 9% for Q1/11. The favourable year-over-year increases in EBITDA and in EBITDA margin for Q1/12 were largely attributable to increased revenue from higher margin aircraft and related services. Aircraft lease costs were $2.0 million in Q1/12, compared to $1.6 million in Q1/11. In Q1/12, the Corporation utilized more short-term aircraft lease arrangements to meet increased year over year demand.

*Earnings*
In Q1/12, the Corporation recorded a seasonal loss of $2.6 million compared to a loss of $3.9 million for Q1/11. Depreciation expense related to capital assets and intangible assets for Q1/12 was $4.5 million compared to $4.4 million for Q1/11. Finance costs of $3.8 million for Q1/12 were comparable to $3.5 million for Q1/11. The Corporation incurred slightly lower debt related charges in Q1/12; however, the lower financing charges were offset by higher foreign exchange charges. The Corporation's share of equity accounted investees' earnings (net of income tax) was $0.2 million for Q1/12 comparable to $0.1 million in Q1/11. The Corporation recorded a $0.3 million loss on a sale of an aircraft in Q1/12. The Corporation had an income tax recovery of $0.9 million for Q1/12, compared to an income tax recovery of $1.6 million for Q1/11. The Corporation's statutory income tax rate for Q1/12 was approximately 28% compared to 30% for Q1/11. The difference between the Corporation's income tax provision rate and the statutory rate arises from changes in the timing of the reversal of temporary tax and accounting differences and permanent tax differences.

## *Northern Services*

The Northern Services segment generated revenue of $18.5 million on 8,129 flight hours for Q1/12, compared to revenue of $15.4 million on 7,002 flight hours for Q1/11. The 20% increase in revenue and 16% increase in flight hours from Q1/11 were largely attributable to the segment's 41% year-over-year increase in revenues from its mining exploration and production and oil and gas based customers. The segment benefited from a full quarter of operations in Q1/12 in Peru compared to Q1/11 at which time the operation was largely in a startup phase.

The segment incurred expenses totaling $18.4 million for Q1/12, compared to $14.5 million for Q1/11, a 27% increase. While the segment incurred higher aircraft lease and crew related costs in relation to the increased revenues in the quarter the segment also incurred ramp up costs in preparation for the upcoming peak season in Q2/12 and Q3/12. These costs incorporate higher staff count as well as higher wages as dictated by the skilled labour market. Finally, the segment incurred higher aircraft maintenance cost which again consisted primarily of seasonal repair and maintenance work for the upcoming peak season.

The segment recorded EBITDA of $0.1 million for Q1/12, compared to $0.9 million for Q1/11 with the variance attributable to higher operating costs. EBITDAR for Q1/12 was $1.9 million, compared to $2.4 million for Q1/11. The segment incurred higher aircraft lease expense in Q1/12, corresponding to increased flight hours in Q1/12 compared to Q1/11.

## *Government Services*

The Government Services segment generated revenue of $18.7 million on 1,977 flight hours for Q1/12, compared to revenue of $10.4 million on 1,540 flight hours for Q1/11. This represented an 80% increase in revenue and a 35% increase in total flight hours, again largely attributable to higher demand for airborne training and special mission services by the Canadian military and revenues generated from MRO service provided by Technical Services, which began operations in late Fiscal 2011.

The segment incurred expenses totaling $12.2 million for Q1/12, compared to $7.4 million for Q1/11, an increase of 65%. The increase in operating expenses is consistent with the segment's increased revenue level.

The segment generated EBITDA of $6.5 million for Q1/12, compared to EBITDA of $3.1 million for Q1/11. The increase in EBITDA flows directly from increased utilization of the segments higher-rate aircraft and new revenue contribution from Technical Services' MRO services. EBITDAR for Q1/12 was $6.7 million, compared to EBITDAR of $3.2 million for Q1/11.

## *Corporate Support*

Corporate support expenses totaled $1.8 million for Q1/12, compared to $1.7 million for Q1/11.

## *Liquidity and Financial Resources*

The following schedule summarizes the changes in cash flow components for Q1/12 and Q1/11:

| (thousands of dollars) | | Q1/12 | | Q1/11 |
|---|---|---|---|---|
| Operating activities | $ | (10,397) | $ | (9,538) |
| Investing acitivities | | (6,648) | | (1,736) |
| Financing activities | | 13,568 | | 6,555 |
| Net decrease in cash for the year | $ | (3,477) | $ | (4,719) |

The cash position at the end of Q1/12 reflected a net cash outflow of $3.5 million compared to a net cash outflow of $4.7 million in Q1/11. The Corporation had $14.0 million drawn on its operating line of credit as at Q1/12 compared to $7.8 million as at Q1/11. The increased draw reflects the increased seasonal demands for non-capital requirements and investing activities.

*Operating activities*

Q1/12 operating activities generated a net cash outflow of $10.4 million, compared to a net cash outflow of $9.5 million in Q1/11. The lower year-over-year loss of $1.3 million was offset by increased cash outflow from higher seasonal non-cash working capital funding demands ($0.9 million) and adjustments to future income tax related to loss utilization anticipated in the current fiscal year ($1.5 million).

*Investing activities*

The net cash outlay from investing activities for Q1/12 was $6.6 million compared to $1.7 million for Q1/11. Capital expenditures in Q1/12 included two aircraft purchases for a total of $2.0 million and entered into a long term capital lease arrangement related to the MRO facility in Quebec City for $2.7 million, with the remaining $3.5 million related to sustaining capital expenditures and capitalized aircraft overhaul costs. Offsetting the capital expenditures in Q1/12 were proceeds of $1.2 million from the divestiture of an aircraft. Q1/11 net capital expenditures of $1.8 million related to sustaining capital expenditures and capitalized aircraft overhaul costs.

In addition to aircraft overhaul costs related to its existing fleet, the Corporation has committed to the purchase of a fixed wing aircraft for approximately US $1.8 million in Q2/12, a fixed wing aircraft for approximately US $0.9 million in Q3/12 and two fixed wing aircraft for approximately US $3.2 million in Q4/12. The Corporation has provided a $0.3 million non-refundable deposit to be applied to the final purchase price of these aircraft.

*Financing activities*

The Corporation had an outstanding balance of $14.0 million on its operating line of credit as at Q1/12. Consistent with the seasonal nature of the Corporation's business cycle, the Corporation draws on its operating line of credit primarily in the first and second quarters to fund start-up costs associated with seasonal increases in business volumes, as well as to fund increased non-cash working capital; these draws are typically substantially repaid during the third quarter. At the end of Q1/11, the Corporation had an outstanding balance on its operating line of credit of $7.8 million. Netting cash and restricted cash against the outstanding operating line of credit results in a net indebtedness balance of $9.4 million as at the end of Q1/12 compared to $4.3 million at the end of Q1/11. In addition to funding operational activities, the Corporation also drew on the operating line of credit to facilitate short term financing of aircraft purchases totaling $2.0 million during Q1/12.

The Corporation obtained new financing of $2.9 million, which related substantially to a new finance lease arrangement of Technical Services' hangar facility in Quebec City. The Corporation made scheduled debt repayments of $3.3 million during Q1/12. The Corporation did not undertake any significant new long-term financing in Q1/11 and made scheduled repayments of $1.3 million.

*Working capital and cash position*

At the end of Q1/12, the Corporation had a negative working capital position of $28.8 million and a current ratio of 0.7 compared to a negative working capital position of $10.3 million and a current ratio of 0.8 at the end of Fiscal 2011. Given the seasonal nature of the Corporation's businesses, a more meaningful comparison would be of the working capital position as at the end of Q1/12 and Q1/11. As at the end of Q1/11, the working capital position was $11.9 million with a current ratio of 1.4. The year–over-year decrease in the working capital balance and current ratio is attributable to the Corporation's $28.2 million convertible debentures and $13.2 million related party debt being classified as "current portion of long-term debt". Had the convertible debentures and related party debt not been classified as current, the Corporation would have had a working capital position of $13.3 million and a current ratio of 1.3 as at the end of Q1/12. Excluding the impact of the classification of these debts instruments as current, the Q1/12 working capital level reflects a stronger position attributable to the year-over-year increase in operating activities.

The Corporation is aware of the following balance sheet conditions, income items or cash flow items that could materially impact liquidity in the foreseeable future:

- a reversal in the resource sector recovery, resulting in lower levels of business activity in the Corporation's Northern Services segment;
- the Government Services segment not being awarded DND's new long-term contract; the Corporation is currently awaiting an RFP and anticipates that it will be released in August 2011; and,
- capital expenditures related to aircraft purchases or fleet maintenance that are higher than expected.

While the Corporation believes it will have sufficient liquidity to meet its current and future operating requirements based on its existing working capital position, cash generated from operations and the operating credit facilities it maintains, this belief could change if any or all of the above factors materialize. The Corporation's management continues to monitor other factors that could adversely impact its working capital and cash position.
The Corporation's operating line of credit is used to fund any short-term financing requirements which arise as a result of the seasonality of the Corporation's revenue and cash flow patterns. Except as noted above in "Investing Activities", the Corporation has not committed to any expenditures that would significantly change its working capital requirements for the foreseeable future. For further information on the Corporation's operating line of credit, see "Subsequent Events" below. Each significant, non-maintenance related capital expenditure is assessed to gain reasonable assurance that the capital expenditure will, at a minimum, be matched by projected revenues or cost savings generated by the expenditure.

*Debt financing*

The Corporation maintained $139.3 million in term debt obligations as at the end of Q1/12 compared to $139.3 million as at the end of Q4/11. The Corporation was in compliance with all covenants established by its lenders as at April 30, 2011. The Corporation's current portion of loans and borrowings balance of $51.1 million at the end of Q1/12 includes the $28.2 million principal amount of debentures maturing in December 2011 and $13.2 million of debt extinguishment committed to by the Corporation in early Q2/12. For further information on changes in the Corporation's term debt obligations, see "Subsequent Events" below.

## *Shareholders' Equity*

Shareholders' equity decreased by the amount of the Q1/12 net loss which is consistent with the Corporation's low first quarter results. Share capital was unchanged in Q1/12 while contributed surplus increased by $16,000 related to stock options issued in prior periods.

At April 30, 2011, there were 134,461,555 Class A common shares and 742,604 Class B common shares outstanding. At the same date, there were 4,357,300 common share options outstanding and no common share purchase warrants outstanding. During Q3/11, the Corporation granted 1,500,000 stock options under a new employee stock option plan approved by the shareholders in June 2010. No other activity has occurred under this plan to date. The Corporation maintains 2,857,300 outstanding stock options issued under an employee stock option plan created in January 2006. This plan was terminated in June 2008, eliminating any additional grants under this plan. During Q1/12, 33,500 stock options expired related to the January 2006 plan.

## *Related Party Transactions*

At April 30, 2011, the Corporation had long-term debt including accrued interest totalling $13.4 million (January 31, 2011 - $13.6 million) owing primarily to current and former officers and directors of the Corporation or its subsidiaries and who were former owners of the subsidiaries. As discussed in debt financing and subsequent events, this debt was extinguished on May 2, 2011. For the three month period ended April 30, 2011, interest expense on this debt totalled $143,000 (April 30, 2010 - $84,000).

## *Off-Balance Sheet Arrangements*

The Corporation has no off-balance sheet arrangements that management is aware of other than those disclosed in note 14 of the Corporation's annual audited consolidated financial statements for the year ended January 31, 2011.

## *Risk Factors*

The Corporation is subject to a number of risks and uncertainties and is affected by a number of factors outside of the control of its management. Details are provided in the "Risk Factors" section of the Corporation's management's discussion and analysis for the year ended January 31, 2011, which can be found on SEDAR at www.sedar.com.

## *Changes in Accounting Policies*

Refer to notes 13 and 14 of the Corporation's interim condensed consolidated financial statements for a detailed discussion of the Corporation's transition to IFRS.

## *Recently Issued Standards*

A number of new standards, and amendments to standards and interpretations, are not yet effective for the year ending January 31, 2012, and have not been applied in preparing the interim financial statements. Management is currently reviewing the standards to determine the impact on the interim financial statements.

*IFRS 9 Financial Instruments*

The IASB issued IFRS 9 Financial Instruments in November 2009 and subsequently added to the scope of the standard in October 2010. The standard introduces new requirements for the classification and measurement of financial assets and liabilities and is applicable for annual periods beginning on or after January 1, 2013. The Corporation has not early adopted IFRS 9 Financial Instruments, and has yet to assess its full impact.

*IFRS 10 Consolidated Financial Statements*

In May 2011, the IASB issued IFRS 10 Consolidated Financial Statements, which is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. The Corporation intends to adopt IFRS 10 in its financial statements for the annual period beginning on February 1, 2013. The Corporation has not yet determined the impact of adoption of IFRS 10.

*IFRS 11 Joint Arrangements*

In May 2011, the IASB issued IFRS 11 Joint Arrangements. The standard introduces new requirements for entities which had previously accounted for joint ventures using proportionate consolidation. The Company intends to adopt IFRS 11 in its financial statements for the annual period beginning on February 1, 2013, when the standard becomes effective. The Corporation does not expect IFRS 11 to have a material impact on the Corporation's financial statements.

*IFRS 12 Disclosure of Interests in Other Entities*

In May 2011, the IASB issued IFRS 12 Disclosure of Interests in Other Entities, which is effective for annual periods beginning on or after January 1, 2013. IFRS 12 contains the disclosure requirements for entities that have interests in subsidiaries, joint arrangements, associates and/or unconsolidated structured entities. The Company intends to adopt IFRS 12 in its financial statements for the annual period beginning on February 1, 2013. While the Corporation has not yet determined the impact of adoption of IFRS 12, it is expected that the amendment of IFRS 12 will increase the current level of disclosure of interests in other entities.

*IFRS 13 Fair Value Measurement*

The IASB issued IFRS 13 Fair Value Measurement in May 2010, which is effective prospectively for annual periods beginning on or after January 1, 2013. The standard replaces the fair value measurement guidance contained in individual IFRSs with a single source of fair value measurement guidance and defines fair value as the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, i.e., an exit price. The standard also establishes a framework for measuring fair value and sets out disclosure requirements for fair value measurements to provide information that enables financial statement users to assess the methods and inputs used to develop fair value measurements and, for recurring fair value measurements that use significant unobservable inputs, the effect of the measurements on income or loss or other comprehensive income. The Company intends to adopt IFRS 13 prospectively in its financial statements for the annual period beginning on February 1, 2013. The extent of the impact of adoption of IFRS 13 has not yet been determined.

*Amendments to IAS 28 Investments in Associates and Joint Ventures*

In May 2011, the IASB issued Amendments to IAS 28 Investments in Associates and Joint Ventures, which is effective for annual periods beginning on or after January 1, 2013, with early adoption permitted. The standard requires that the interest retained when there is a cessation of significant influence or joint control triggered not be remeasured. The Company intends to adopt the amendments in its financial statements for the annual period beginning on February 1, 2013. The extent of the impact of adoption of the amendments has not yet been determined.

## *Use of Accounting Estimates*

In preparing the interim financial statements, various accounting estimates are made in applying the Corporation's accounting policies. These estimates require significant judgment on the part of management and are considered critical as they are important to the Corporation's financial condition and results. There have been no changes to the Corporations significant accounting estimates disclosed in the Corporation's fiscal 2011 MD&A.

## *NON-IFRS MEASURES*

References to "EBITDA" are to earnings before interest and financing charges, income taxes and depreciation. References to "EBITDAR" is EBITDA before aircraft lease cost. The EBITDA margin and EBITDAR margin are EBITDA and EBITDAR as a percentage of revenue. Management believes EBITDA and EBITDAR to be important measures, as they exclude the effects of long-term investment decisions from the performance of the Corporation's day-to-day operations. Management believes these measurements are useful to measure a company's ability to service debt and to meet other payment obligations or as a valuation measurement.

Prior to Fiscal 2012, the Corporation's EBITDA and EBITDAR included the depreciation of rotable and overhauled components which were treated as operating expenses. Starting in Fiscal 2012 with the conversion to IFRS, depreciation of rotable and overhauled components is included as part of depreciation, which is not, therefore included in the calculation of EBITDA and EBITDAR.

The following table reflects the impact to IFRS EBITDA and EBITDAR:

| (thousands of dollars) | Q1 2012 | Q1 2011 |
|---|---|---|
| Loss | $ (2,586) | $ (3,929) |
| Income tax recovery | (903) | (1,569) |
| Financing charges | 3,752 | 3,547 |
| Depreciation of property and equipment and intangible assets | 4,503 | 4,384 |
| EBITDA | $ 4,766 | $ 2,433 |
| Aircraft lease expenses | 2,004 | 1,600 |
| EBITDAR | $ 6,770 | $ 4,033 |

The EBITDA margin and EBITDAR margin are EBITDA and EBITDAR as a percentage of revenue.

## *Segmented breakdown of EBITDA and EBITDAR*

| (thousands of dollars) | Q1/12 (unaudited) | | | | Q1/11 (unaudited) | | | |
|---|---|---|---|---|---|---|---|---|
| | Northern Services | Government Services | Corporate Support | Total | Northern Services | Government Services | Corporate Support | Total |
| Revenue | $ 18,547 | $ 18,702 | $ - | $ 37,249 | $ 15,382 | $ 10,433 | $ - | $ 25,815 |
| Expenses | 18,447 | 12,204 | 1,806 | 32,457 | 14,454 | 7,359 | 1,646 | 23,459 |
| Loss on sale of property and equipment | | | | 255 | | | | - |
| Share of (earnings) loss of equity accounted investees (net of income tax) | | | | (229) | | | | (77) |
| **EBITDA** | **$ 100** | **$ 6,498** | **$ (1,806)** | **$ 4,766** | **$ 928** | **$ 3,074** | **$ (1,646)** | **$ 2,433** |
| Aircraft lease expenses | 1,805 | 199 | - | 2,004 | 1,425 | 175 | - | 1,600 |
| **EBITDAR** | **$ 1,905** | **$ 6,697** | **$ (1,806)** | **$ 6,770** | **$ 2,353** | **$ 3,249** | **$ (1,646)** | **$ 4,033** |

## *SUMMARY OF QUARTERLY RESULTS*

| (thousands of dollars, except per share amounts) | **2012 - IFRS (unaudited)** | **2011 - IFRS (unaudited)** | | | | **2010 - GAAP (unaudited)** | | |
|---|---|---|---|---|---|---|---|---|
| | **IFRS Q1 Apr 30** | **IFRS Q4** | **IFRS Q3** | **IFRS Q2** | **IFRS Q1 Apr 30** | **CGAAP Q4** | **CGAAP Q3** | **CGAAP Q2** |
| **Results of operations:** | | | | | | | | |
| Total revenue | $ 37,249 | $ 23,746 | $ 44,066 | $ 57,658 | $ 25,815 | $ 17,749 | $ 34,125 | $ 45,733 |
| EBITDA | $ 4,766 | $ (98) | $ 14,220 | $ 26,078 | $ 2,433 | $ (2,296) | $ 9,933 | $ 18,831 |
| Earnings (loss) | $ (2,586) | $ (6,236) | $ 3,775 | $ 11,576 | $ (3,929) | $ (4,837) | $ 1,668 | $ 8,004 |
| Basic and diluted earnings (loss) per share | $ (0.02) | $ (0.05) | $ 0.03 | $ 0.09 | $ (0.03) | $ (0.04) | $ 0.01 | $ 0.06 |

The business of the Corporation follows a seasonal pattern with the lowest revenue occurring from November to April. Therefore, the Corporation's results vary from quarter to quarter and results for an interim period are not necessarily indicative of results that may be expected for a full year.

## *SUBSEQUENT EVENTS*

On May 2, 2011, the Corporation completed a transaction to repay related party debts and accrued interest totalling $13.4 million through a cash payment of $3.1 million and the issuance of 10,352,000 Class A common shares. Based on the market value of the Class A common shares at the date of settlement ($0.43 per share), the Corporation expects to record a pre-tax gain on the extinguishment of the related party debts of approximately $5.8 million in its second quarter.

On May 12, 2011, the Corporation closed a $30.0 million issuance of new convertible unsecured subordinated debentures (the "New Debentures") at a price of $1,000 per debenture. On May 27, 2011, the Corporation also closed the issuance of an overallotment option on the original issue, for an additional $4.5 million aggregate principal amount of New Debentures. On June 16, 2011, the Corporation used the net proceeds of issuance of the New Debentures to fully repay the Corporation's $28.8 million 8.75% Convertible Unsecured Subordinated Debentures due December 31, 2011 and accrued interest payable thereon. The Corporation intends to use the remaining funds from the issuance of the New Debentures to fund working capital and general corporate purposes.

The Corporation and its Lender agreed to extend the maturity date of the Corporation's existing operating line of credit from June 9, 2011 to July 29, 2011 in order to complete documentation of the annual renewal of this facility. The renewal is for another one year term, with minor modifications to certain terms and conditions and with a reduction in the annual interest rate from 18% to 13%. The aircraft term loan provided by the same Lender will also be renewed for another 1 year term at 13% per annum.

## *DISCLOSURE CONTROLS AND INTERNAL CONTROLS*

The change from CGAAP to IFRS has resulted in various accounting process changes within the various operating units, specifically related to the Corporation's property, plant and equipment and consolidation. While there were no control deficiencies identified during the current quarter, the Corporation's management will continue to monitor the internal controls over financial reporting ("ICFR") to ensure that IFRS has not been materially affected as a result of transitioning to IFRS. There were no other changes during the period that materially affected or are reasonably likely to materially affect the Corporation's ICFR and disclosure controls and procedures.

## *FORWARD-LOOKING STATEMENTS*

Forward-looking information and statements are included in this management's discussion and analysis. Forward-looking information and statements include, but are not limited to, statements concerning possible or assumed future financial and operating results set out in this document, the Corporation's strengths, strategies and priorities and the Corporation's assessment of the economic and business outlook for the Corporation and the Corporation's industry. Generally, but not always, forward-looking information can be identified by the use of forward-looking terminology such as "may", "could", "should", "would", "expect", "believe", "plan", "estimate", "outlook", "forecast", "anticipate", "foresee", "continue" or the negative of these terms or variations of them or similar terminology. More particularly, and without limitation, this management's discussion and analysis contains forward-looking statements relating to: the seasonality of the Corporation's business; its Objective and business development; the impact of the current economic conditions on the results of its operations and/or financial condition; management's outlook for the future; management's ability to reduce costs and/or contain them at the existing levels; management's ability to continue to manage working capital effectively; the impact of weather conditions on the results of the Corporation's operations and/or financial condition; the cost of relocating its corporate office; its ability to utilize planned and/or existing fleet capacity; its ability to continue to meet lender covenants and other terms and conditions of its credit agreements; plans and/or requirements to make new capital investments; and, its plans, decisions and the impacts resulting from the implementation of IFRS.

All forward-looking information and statements presented in this document are based on reasonable assumptions, estimates and analysis that take into account management's experience and perception of trends and interpretation of external factors, such as economic conditions. By their very nature, forward-looking statements involve inherent risks and uncertainties, both general and specific, and risks exist that predictions, forecasts, projections and other forward-looking statements will not be achieved. Readers are cautioned not to place undue reliance on these forward-looking statements as a number of important factors could cause actual results to differ materially from the plans, objectives, expectations, estimates and intentions expressed in such forward-looking statements. These factors include, but are not limited to: the Corporation's ability to secure operating contracts; the strength of the Canadian economy in general and the strength of the local economies within Canada in which the Corporation conducts operations; the effects of changes in interest rates; the effects of competition in the markets in which the Corporation operates; inflation; capital market fluctuations, including the availability of equity and/or debt capital to the Corporation; the impact of changes in the laws and regulations regulating aviation services; changes in tax laws; technological changes; unexpected judicial or regulatory proceedings and decisions; weather conditions in the geographical regions in which the Corporation operates; and the Corporation's anticipation of and success in managing the risks implied by the foregoing.

The foregoing list of important factors is not exhaustive. When relying on forward-looking information and statements to make decisions, investors and others should carefully consider the foregoing factors and other uncertainties and potential events.

Additional information relating to the Corporation, including the Corporation's Annual Information Form, can be found on SEDAR at www.sedar.com.

**Dated: July 13, 2011**