# Dynetek Industries Ltd. Announces Second Quarter 2008 Results

**Calgary, Alberta, Canada – August ●, 14, 2008** – Dynetek Industries Ltd. (TSX:DNK), a leader in the design, manufacturing and marketing of proprietary fuel storage cylinders and systems for compressed natural gas (CNG) and hydrogen, today reported results for the three months and six months ended June 30, 2008. The full unaudited consolidated financial statements and MD&A have been filed on SEDAR at www.sedar.com and on Dynetek's website at www.dynetek.com.

## Financial Highlights

(tabular amounts in thousands of Canadian dollars, except share capital and per share data)
(unaudited)

| | Three months ended June 30 | | Six months ended June 30 | |
|---|---|---|---|---|
| | **2008** | 2007 | **2008** | 2007 |
| Total Revenue | **5,015** | 8,135 | **9,464** | 18,645 |
| Net income (loss) before taxes | **(1,480)** | (34) | **(2,540)** | 213 |
| Net income (loss) before taxes per common share (basic and fully diluted) | **(0.07)** | nil | **(0.12)** | 0.01 |
| Net income (loss) | **(1,480)** | (2,309) | **(2,540)** | (2,142) |
| Net income (loss) per common share (basic and fully diluted) | **(0.07)** | (0.11) | **(0.12)** | (0.10) |
| EBITDA [1] | **(795)** | 784 | **(1,494)** | 1,694 |
| Capital expenditures | **70** | 443 | **148** | 731 |
| Cash and cash equivalents | **4,154** | 1,600 | **4,154** | 1,600 |
| Non-cash working capital [1] | **11,146** | 11,003 | **11,146** | 11,003 |
| Working capital[1] | **15,300** | 12,603 | **15,300** | 12,603 |
| Cash flow (deficiency) from operations | **(1,713)** | (1,126) | **(2,365)** | 993 |
| Total assets | **41,417** | 44,500 | **41,417** | 44,500 |
| Long-term debt and capital leases | **7,259** | 1,544 | **7,259** | 1,544 |
| Common shares outstanding | **20,936,500** | 20,940,576 | **20,936,500** | 20,940,576 |
| Weighted average common shares outstanding | **20,936,500** | 20,940,576 | **20,936,500** | 20,940,576 |

(1) EBITDA, non-cash working capital and working capital are non-GAAP financial measures. Dynetek defines EBITDA as earnings before interest, taxes, stock based compensation, non-cash foreign exchange, depreciation, and amortization. Dynetek defines non-cash working capital as current assets less cash and current liabilities. Dynetek defines working capital as current assets less current liabilities. Dynetek believes that these non-GAAP financial measures provide investors and analysts with useful information so that they can better understand the financial results and perform a better analysis of Dynetek's growth and profitability potential.

## OPERATIONAL HIGHLIGHTS

In the Outlook section of the MD&A for the year ended December 31, 2007, Dynetek indicated that it expected to incur a loss and negative EBITDA[1] in Q1 and Q2 2008, due to the slowdown in the demand for its products resulting from the postponement of public bus manufacturing in Europe.

In the first six months of 2008, Dynetek achieved total revenues of $9.5 million, a decrease of 49% compared to $18.6 million for the same period of 2007. Cylinder and system sales for the six months ended June 30, 2008 were $6.8 million, a decrease of 55% compared to $15.2 million for the same period of 2007. For the six months ended June 30, 2008 the Company achieved research and development revenue of $2.6 million, a decrease of 19% compared to $3.2 million for the same period of 2007. In the second quarter of 2008, Dynetek achieved total revenues of $5.0 million (2007 - $8.1 million) with cylinder and system sales of $3.5 million (2007 - $5.8 million) and research and development revenue of $1.4 million (2007 - $2.3 million). The Company recorded cash flow deficiency from operations of ($2.4) million for the six months ended June 30, 2008, compared to cash flow from operations of $1.0 million for the same period of 2007. Cash flow deficiency from operations for the three months ended June 30, 2008 was ($1.7) million compared to cash flow deficiency of ($1.1) million for the same period of 2007. The Company had negative EBITDA[1] of ($1.5) million for the six months ended June 30, 2008, compared to positive EBITDA[1] of $1.7 million for the six months ended June 30, 2007. The Company had negative EBITDA[1] of ($0.8) million for the second quarter ended June 30, 2008, compared to positive EBITDA[1] of $0.8 million for

same period of 2007. Dynetek reported a loss of ($2.6) million for the six months ended June 30, 2008, compared to a net loss of ($2.1) million for the comparable period of 2007. The Company had a loss of ($1.5) million for the second quarter ended June 30, 2008 compared to a loss of ($2.3) million for the same period of 2007. As at July 30, 2008 the Company had a confirmed revenue backlog of $21.2 CAD for cylinder and system sales and research and development projects for delivery within the next twelve months.

The Company continues to focus its compressed natural gas cylinder and system sales in areas such as California and Europe. Dynetek's proprietary technology provides advantages such as less weight, more compressed natural gas on board and less operating costs, being the value proposition we offer our customers that our competitors cannot provide. In the first six months of 2008, Dynetek's European operations achieved cylinder and system sales of $4.5 million (2007 - $9.1 million). In the three months ended June 30, 2008, Dynetek's European operations achieved cylinder and system sales of $2.1 million (2007 - $3.3 million). The cylinder and system sales from the Canadian operations for the six months ended June 30, 2008 were $2.3 million (2007 - $6.1 million). The cylinder and system sales from the Canadian operations for the three months ended June 30, 2008 were $1.5 million (2007 - $2.5 million).

Dynetek's research and development team continues to focus its efforts on compressed hydrogen and related storage requirements. During the first six months of 2008 the Company continued to work with NRCan and 9 different OEMs, including Ford, Hyundai, Volkswagen, Daimler and Nissan, to design, manufacture and deliver the hydrogen storage solution on 13 confidential development programs.

In May 2008, the Company received approval from U.S. Department of Transportation (DOT) of their 450 Bar ( 6527 PSI) cylinder for use in Dynetek "BT450" Tube Trailer Systems. The traditional method of bulk gas hauling is with steel tube trailers with typical operating pressure of 3000psi. Dynetek's new high-pressure cylinders and systems which will operate at 6500psi, will enable direct refueling of Hydrogen vehicles from our specially designed "BT450" modules. Dynetek has received an order from Air Liquide to provide cylinders for the construction of a "BT450" Tube Trailer system, which will be used to refuel the Hydrogen bus fleet being deployed by BC Transit for the 2010 Winter Games in Whistler, British Columbia.

In June 2008, Dynetek Europe GmbH received a CNG complete system order from a major bus manufacturer in Europe. These systems, which are to be delivered from June 2008 until February 2009, represent revenue of approximately $10 million (CDN). Dynetek will provide a complete system solution offering a lower overall system weight with increased fuel on board the vehicle than our competitors.

In the first six months of 2008 Dynetek continued to provide deliverables under the milestones for the contract with Magna Steyr in connection with Daimler's automotive fuel cell program. The program involves the development, certification and supply of 700bar compressed hydrogen fuel storage systems, including related engineering, to Magna Steyr in connection with Daimler's fuel cell program.

## OUTLOOK

The Company remains committed to continuing to grow its CNG and Hydrogen revenue streams globally through targeted marketing initiatives.

In 2008, the Company expects to increase its focus on revenue growth opportunities worldwide in the CNG market for bus and heavy-duty truck applications and for bulk hauling of larger quantities of compressed gas. Major economic and environmental factors worldwide are contributing to high-growth in natural gas demand for vehicles as follows:

- The high growth rate in demand for natural gas stems from the comparative advantages of natural gas compared to diesel, gasoline and bio-fuels;
- Natural gas is cleaner with less toxic emissions than diesel or gasoline and is currently less costly;
- A growing natural gas infrastructure. Continuing investment in infrastructure is adding to the number of compressed natural gas refueling centers; and
- CNG will continue to develop as a transportation fuel as it currently is less costly than oil based fuels which are also becoming supply constrained in developing economies.

The above trends and related market opportunities are expected to create a positive intermediate and longer-term outlook for Dynetek. The largest demand for CNG vehicles is in countries where low cost solutions are required. The Company is currently reviewing strategies to grow the compressed gas system revenue and is evaluating additional product

development and sales in order to penetrate price sensitive markets that are actively developing CNG as a transportation fuel. To accomplish this product development and market penetration, the Company will also be evaluating strategic alliances, new joint ventures, new partners and customers, licensing arrangements, new manufacturing techniques and additional product offerings. The Company is committed to change where appropriate to attain its goals of revenue growth and net income.

In the area of bulk hauling, the Company's prime focus will be in markets with access to an abundance of natural gas, where storage technology and pipeline infrastructure are lacking. The Company has already obtained US Department of Transportation (DOT) and Transport Canada (TC) certification for its 223bar bulk hauling system and in 2008, the Company has received DOT approval to sell its 450 bar bulk systems in the US which should help it with penetrating the mobile bulk hauling storage market in 2008 and beyond.

Dynetek expects to incur a loss and negative EBITDA in Q3 of 2008 due to a slowdown in the demand for its products, specifically a postponement of public transit bus manufacturing in Europe. In June 2008 the Company announced Dynetek Europe GmbH has received a CNG complete system order from a major bus manufacturer in Europe and the systems are to be delivered from June 2008 until February 2009, representing revenue of approximately $10 million (CDN). Currently Dynetek is seeing an increase in customer enquiries and expects to see an increase in bid submissions in Q3 2008. The Company will continue to manage its costs responsibly and improve production efficiencies where possible. During the second quarter, the Company reduced production and research and development staff to core levels, reduced executive compensation and continues to review supplier alternatives.

The Company will continue to develop its hydrogen storage technologies to assist in commercializing the hydrogen economy. This includes working with OEMs to implement their hydrogen vehicle strategies and sales to energy-related companies that require mobile refueling units, stationary storage for refueling, and bulk hauling of hydrogen.

In 2008 Dynetek expects to substantially complete the contract with Magna Steyr in connection with Daimler’s automotive fuel cell program. In 2007 Dynetek saw an increase in activity in the hydrogen vehicle market and continues to work with Natural Resources Canada (NRCan) and 9 different Original Equipment Manufacturers (OEMs), including Ford, Hyundai, Daimler, Volkswagen and Nissan, to design, manufacture and deliver hydrogen storage solutions on 13 different confidential development programs.

**ABOUT DYNETEK**

Dynetek Industries Ltd. designs, produces and markets one of the lightest and most advanced fuel storage and refueling systems for compressed natural gas, low emission vehicles and compressed hydrogen, zero-emission fuel cell vehicles. Dynetek is recognized around the world for its solutions-of-choice to the alternate fuel vehicle sector, evidenced by strategic relationships with major manufacturers around the globe. Dynetek is listed on the Toronto Stock Exchange, symbol: DNK

**FORWARD LOOKING STATEMENTS**

*In addition to historical information, this news release contains forward-looking statements and should be read in conjunction with the financial statements and related notes for the year ended December 31, 2007 and quarterly interim financial statements for 2008. Forward-looking statements are based upon current assumptions, expectations and estimates that involve a number of risks and uncertainties and actual results could differ materially from those discussed in the forward-looking statements. Readers are encouraged to review the section in the Management’s Discussion and Analysis titled ‘Principal Risks and Uncertainties’ for a discussion of factors that could affect Dynetek’s future operations and financial results. Forward-looking statements are based upon management's assumptions, expectations and estimates at the time the statements are made. Dynetek does not update forward-looking statements should circumstances or management's assumptions, expectations or estimates change, except where required by securities laws.*

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## MANAGEMENT'S DISCUSSION AND ANALYSIS

*The following sets out management's discussion and analysis of Dynetek's financial position as at June 30, 2008 and December 31, 2007 and results of operations for the three and six months ended June 30, 2008 and 2007 and is based on information available as at August 14, 2008. The interim management's discussion and analysis (MD&A) updates Dynetek's 2007 annual MD&A, to which readers are referred. No update is provided where an item is not material or where there has been no material change from the discussion in Dynetek's annual MD&A.*

### Non-GAAP Financial Measures

Dynetek Industries Ltd. ('the Company") reports its financial results in accordance with generally accepted accounting principles (GAAP). It also occasionally uses certain non-GAAP financial measures, such as EBITDA, working capital and non-cash working capital. Dynetek defines EBITDA as earnings before interest, taxes, stock based compensation, non-cash foreign exchange, depreciation, and amortization. Dynetek defines working capital as current assets less current liabilities. Dynetek defines non-cash working capital as current assets less cash and current liabilities. These non-GAAP financial measures are always clearly indicated. The Company believes that these non-GAAP financial measures provide investors and analysts with useful information so that they can better understand the financial results and perform a better analysis of the Company's growth and profitability potential. Since non-GAAP financial measures do not have a standardized definition, they may differ from the non-GAAP financial measures used by other companies. The Company strongly encourages investors to review its financial statements and other publicly filed reports in their entirety and not rely on a single non-GAAP financial measure.

## FORWARD LOOKING STATEMENTS

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| Weighted average common shares outstanding | **20,936,500** | 20,940,576 | **20,936,500** | 20,940,576 |

(1) EBITDA, non-cash working capital and working capital are non-GAAP financial measures that are defined and discussed in the Non-GAAP Financial Measures section of the Management's Discussion and Analysis.

**Cylinder and system sales** for the six months ended June 30, 2008 were $6.8 million, down 55% from $15.2 million for the same period of 2007. Cylinder and system sales for the three months ended June 30, 2008 were $3.5 million, down $2.3 million or 40% for the same period in 2007. In the first six months of 2008 Dynetek was unable to maintain the same levels in sales as in the same period of 2007 due to the slowdown in tender activities by and deliveries to the European Bus

Market and a reduction of sales into the US heavy-duty truck market. In the first six months of 2008, Dynetek's European operations achieved cylinder and system sales of $4.5 million (2007 - $9.1 million). In the three months ended June 30, 2008, Dynetek's European operations achieved cylinder and system sales of $2.1 million (2007 - $3.3 million). The cylinder and system sales from the Canadian operations for the six months ended June 30, 2008 were $2.3 million (2007 - $6.1 million). The cylinder and system sales from the Canadian operations for the three months ended June 30, 2008 were $1.5 million (2007 - $2.5 million).

**Research and development income** for the six months ended June 30, 2008 was $2.6 million, down 19% or $0.6 million from the same period in 2007. Research and development income for the three months ended June 30, 2008 was $1.4 million, down 39% or $0.9 million from the same period in 2007. During the six months and three months ended June 30, 2008 the research and development revenue was lower than the same period of 2007 due to lower revenues being recognized from the Magna Steyr purchase order involving the design, certification and supply of 700 bar compressed hydrogen fuel storage systems. The reduction was partially offset by additional research and development projects with OEMs that began in the period. During the first six months of 2008, Dynetek continued to be involved with Natural Resources Canada (NRCan) and 9 different Original Equipment Manufacturers (OEMs), including Ford, Hyundai, Daimler, Volkswagen and Nissan, to design, manufacture and deliver the hydrogen storage solution on 13 confidential development programs. Revenues received from the OEMs regarding these projects are recorded on billing milestones outlined in the contracts and, therefore, timing differences occur between when costs are incurred and funding is received. Non-repayable cost shared monies received from NRCan are recorded as revenue in the period it is invoiced. During the first six months of 2008, Dynetek continued to provide deliverables under the milestones for the Magna Steyr contract relating to the Daimler Chrysler fuel cell program.

**Investment and other income** for the six months ended June 30, 2008 was $66,000, compared to $0.3 million for the same period in 2007. Investment and other income for the three months ended June 30, 2008 was $55,000, compared to $38,000 for the same period in 2007. The six month decrease reflects a one-time sale of shares of a private company in the first quarter of 2007. The three month increase reflects the interest income earned on cash in bank.

**Cost of goods sold** was $6.0 million for the six months ended June 30, 2008 compared to $12.4 million for the same period in 2007. Corresponding contribution margins for the six months ended June 30, 2008 were $0.8 million, or 12% of sales compared to $2.8 million or 18% of sales for the same period of 2007. Cost of goods sold was $3.2 million for the three months ended June 30, 2008 compared to $4.8 million for the same period in 2007. Corresponding contribution margins for the three months ended June 30, 2008 were $0.3 million, or 9% of sales compared to $1.0 million or 17% of sales for the same period of 2007. The margin reduction for the three and six months ended June 30, 2008 compared to the same period of 2007 is due to the reduced sales in the period and selling at reduced margins in order to maintain sales, resulting in less revenue to cover fixed costs.

**General and administrative expense** was $1.7 million for the six months ended June 30, 2008 compared to $1.9 million for the same period of 2007. General and administrative expense was $0.9 million for the three months ended June 30, 2008 compared to $1.0 million for the same period of 2007. The three and six month decreases are the result of lower administrative costs in the Dynetek Europe operations reflecting expenses associated with the move of Dynetek Europe's office and plant in 2007. General and administration expense as a percentage of revenue for the six months ended June 30, 2008 was 18% compared to 10% for the same period of 2007. General and administration expense as a percentage of revenue for the three months ended June 30, 2008 was 18% compared to 12% for the same period of 2007. As a percentage of revenue, the three and six month increases reflect the reduction in sales for the three and six months ended June 30, 2008 as compared to the same period of 2007.

**Research and product development expense** was $2.5 million for the six months ended June 30, 2008 compared to $1.8 million for the same period in 2007. Research and product development expense was $1.3 million for the three months ended June 30, 2008 compared to $1.2 million for the same period in 2007. The increase in expenses for the three and six month periods ended June 30, 2008 are the result of the deliverables made in the periods for the Magna project having lower margins than the deliverables made in the comparative periods of 2007. Also, there were severance amounts paid to certain research and development employees in 2008 that did not occur in the comparative period of 2007. Research and development expense consists of materials, labor and costs of benefits and overhead related to research and development activity.

The majority of Dynetek's research and development programs are co-funded with major OEMs and government (NRCan). The funding from the OEMs for the research and development programs is recorded as research and development revenue based on billing milestones outlined in the contracts. This can result in timing differences between when costs are incurred

and funding is received. The government funding is recorded either as research and development income or loans. The cost shared monies received from NRCan, which is non-repayable, are recorded as research and development revenue in the period it is invoiced and the repayable government cost shared monies are recorded as a loan. During the first six months of 2008, Dynetek continued to provide deliverables under the milestones for the Magna Steyr contract relating to the Daimler Chrysler fuel cell program.

**Marketing expense** was $0.7 million for the six months ended June 30, 2008, which is comparable to the same period of 2007. Marketing expense was $0.4 million for the three months ended June 30, 2008, which is comparable to the same period of 2007. Marketing expense increased to 7% of revenue for the six months ended June 30, 2008 compared to 4% for the same period of 2007. Marketing expense increased to 8% of revenue for the three months ended June 30, 2008 compared to 5% for the same period of 2007. The three and six month increases in marketing expense as a percentage of sales reflects the reduction in sales in the periods.

**Interest Expense** was $0.2 million for the six months ended June 30, 2008 compared to $0.1 million for the same period of 2007. Interest Expense was $0.1 million for the three months ended June 30, 2008, compared to $33,000 for the same period of 2007. The increase in interest expense for the three and six month periods ended June 30, 2008 are reflective of the $5.0 million CAD mortgage obtained in March 2008 that did not exist in the comparative period of 2007. The 2008 interest expense also included transaction costs of $33,000 relating to the mortgage obtained during the period.

**Depreciation** was $0.8 million for the six months ended June 30, 2008, which is comparable to the same period of 2007. Depreciation was $0.4 million for the three months ended June 30, 2008, which is comparable to the same period of 2007.

**Amortization** was $0.5 million for the six months ended June 30, 2008, which is comparable to the same period of 2007. Amortization was $0.3 million for the three months ended June 30, 2008, which is comparable to the same period of 2007. Items included in amortization expense include process and development costs, patents and deferred start-up costs for the European operation.

**Foreign exchange** for the six months ended June 30, 2008 was a gain of $0.4 million compared to a loss of $0.1 million in the same period of 2007. Foreign exchange for three months ended June 30, 2008 was a gain of $0.1 million compared to a loss of $0.1 million in the same period of 2007. Dynetek's Canadian operations invoices the majority of its revenue in US dollars and the European operation invoices in Euros. The Company reports its results in Canadian dollars but the revenues are generated in US dollars, Euros and Canadian dollars. The foreign exchange gain in the three and six months of 2008 is a result of a strengthening of the U.S. dollar and the Euro against the Canadian dollar resulting in a positive impact on the foreign denominated accounts receivable and cash when translating into Canadian dollars for financial reporting purposes and the settlement of accounts receivable transactions during the period.

**Stock based compensation** for six months ended June 30, 2008 was $42,000 compared to $56,000 in the same period of 2007. Stock based compensation for three months ended June 30, 2008 was $21,000 compared to $28,000 in the same period of 2007. The reduction of stock based compensation for the three and six month periods ended June 30, 2008 is due to a reduction in options issued.

**Future income tax** for six months ended June 30, 2008 was $nil compared to $2.4 million for the same period of 2007. Future income tax for the three months ended June 30, 2008 was $nil compared to $2.3 million for the same period of 2007. During the second quarter of 2007 the Company considered the future income tax asset impaired due to the deferral of sales for the European bus markets into 2008 and reduced the future income tax asset value to $nil.

**Net Loss** for the six months ended June 30, 2008 was ($2.5) million or ($0.12) per common share compared to a net loss of ($2.1) million or ($0.10) per common share for the comparable period of 2007. Net Loss for the three months ended June 30, 2008 was ($1.5) million or ($0.07) per common share compared to net loss of ($2.3) million or ($0.11) per common share for the comparable period of 2007.The net loss for the three and six months ended June 30, 2008 is substantially the result of reduction of sales due to the slow down in the European bus market and reduced sales into the US heavy-duty truck market.

## Summary of Quarterly Results

The following table shows selected unaudited financial information for the past nine quarters ending June 30, 2008. The information has been obtained from our quarterly unaudited financial statements, which have been prepared in accordance with Canadian GAAP and, in the opinion of management, have been prepared using accounting policies consistent with the Company's audited financial statements as at December 31, 2007 and include all adjustments necessary for the fair presentation of the results of the interim periods. We expect our operating results to vary significantly from quarter to quarter and they should not be relied upon to predict future information.

| (thousands of Canadian dollars except per share data) (unaudited) | June 30 2006 | Sept 30 2006 | Dec. 31 2006 | Mar. 31 2007 | June 30 2007 | Sept 30 2007 | Dec 31 2007 | Mar 31 2008 | June 30 2008 |
|---|---|---|---|---|---|---|---|---|---|
| **Revenues** | | | | | | | | | |
| Cylinder and system sales | 8,090 | 8,275 | 11,334 | 9,322 | 5,838 | 8,481 | 5,367 | 3,242 | 3,517 |
| Research & development income | 644 | 376 | 771 | 918 | 2,259 | 1,322 | 1,150 | 1,196 | 1,443 |
| Investment & other income | 38 | 13 | 14 | 270 | 38 | 33 | 32 | 11 | 55 |
| | 8,772 | 8,664 | 12,119 | 10,510 | 8,135 | 9,836 | 6,549 | 4,449 | 5,015 |
| **Operating expenses** | | | | | | | | | |
| Cost of goods sold | 6,307 | 6,393 | 9,513 | 7,630 | 4,817 | 6,581 | 4,318 | 2,776 | 3,247 |
| Marketing & general and admin. | 1,384 | 1,387 | 1,802 | 1,312 | 1,350 | 1,489 | 1,457 | 1,186 | 1,251 |
| Research & product development | 515 | 567 | 650 | 658 | 1,184 | 1,391 | 1,426 | 1,186 | 1,312 |
| | 8,206 | 8,347 | 11,965 | 9,600 | 7,351 | 9,461 | 7,201 | 5,148 | 5,810 |
| **Earnings before interest, taxes, stock based compensation, non-cash foreign exchange, depreciation & amortization** [1] | 566 | 317 | 154 | 910 | 784 | 375 | (652) | (699) | (795) |
| Interest | - | 22 | 62 | 68 | 33 | 58 | 60 | 68 | 108 |
| Taxes | - | - | 150 | 80 | 2,275 | - | - | - | - |
| Stock based compensation | 51 | 54 | 56 | 28 | 28 | 29 | 197 | 21 | 21 |
| Foreign exchange (gain) loss | 146 | 6 | 75 | (1) | 115 | 34 | 162 | (347) | (93) |
| Depreciation & amortization | 518 | 546 | 1,018 | 568 | 642 | 666 | 1,082 | 619 | 649 |
| | 715 | 628 | 1,361 | 743 | 3,093 | 787 | 1,501 | (361) | 685 |
| **Net income (loss)** | (149) | (311) | (1,207) | 167 | (2,309) | (412) | (2,153) | (1,060) | (1,480) |
| **Net Income (loss) per share** | | | | | | | | | |
| Basic and fully diluted | (0.01) | (0.02) | (0.05) | 0.01 | (0.11) | (0.02) | (0.10) | (0.05) | (0.07) |

(1) EBITDA is a non-GAAP financial measure that is defined and discussed in the Non-GAAP Financial Measures section of the Management's Discussion and Analysis.

## Intangible Assets and Deferred Costs - Expenditures

(thousands of Canadian dollars)
(unaudited)

| | Three months ended June 30 | | Six months ended June 30 | |
|---|---|---|---|---|
| | **2008** | 2007 | **2008** | 2007 |
| Patents | **8** | 10 | **12** | 16 |
| Certification costs | **77** | 153 | **287** | 423 |
| Deferred Costs | **-** | 17 | **-** | 62 |
| | **85** | 180 | **299** | 501 |

Intangible asset expenditures for the six months ended June 30, 2008 were $0.3 million compared to $0.5 million for the same period of 2007. Intangible asset expenditures for the three months ended June 30, 2008 were $0.1 million compared to $0.2 million for the same period of 2007. The additions for the three and six months ended June 30, 2008 were due to certification and patent costs incurred during the period. The Company will invest in patents and costs associated with product certification in future years to ensure protection of its intellectual property, developed products and production processes.

## Capital Expenditures

(thousands of Canadian dollars)
(unaudited)

| | Three months ended June 30 | | Six months ended June 30 | |
|---|---|---|---|---|
| | **2008** | 2007 | **2008** | 2007 |
| Building and leaseholds | **34** | 227 | **34** | 236 |
| Manufacturing equipment | **76** | 1,152 | **129** | 1,413 |
| Office furniture and other equipment | **-** | 51 | **-** | 103 |
| Computer hardware and software | **5** | 9 | **9** | 21 |
| Manufacturing equipment under construction | **(45)** | (996) | **(24)** | (1,042) |
| | **70** | 443 | **148** | 731 |

Capital expenditures for the six months ended June 30, 2008 were $0.1 million compared to $0.7 million for the same period in 2007. Capital expenditures for the three months ended June 30, 2008 were $0.1 million compared to $0.4 million for the same period in 2007.

The Company's capital resource requirements currently consist of capital expenditures to enhance the existing production line.

## Financial Resources and Liquidity

The Company's principal source of liquidity is cash generated from operations. The Company's principal liquidity requirements relate to the increase in working capital required to maintain our production, sales and research and development projects. The Company's actual funding requirements and financing alternatives could vary depending on a number of factors, including CNG system sales on a global basis, the progress of research and development projects, the Company's ability to improve controllable costs and the development of additional relationships with strategic partners.

The Company also has the ability to fund liquidity requirements through its operating bank line of credit facility, the $5.0 million mortgage facility with Business Development Bank of Canada (BDC), and management of working capital.

As at June 30, 2008 Dynetek had cash and cash equivalents of $4.2 million, compared to $1.8 million at December 31, 2007. Dynetek had a cash flow deficiency from operations of ($2.4) million for the period ended June 30, 2008 compared to cash flow from operations of $1.0 million for the six months ended June 30, 2007.

Actively managing working capital is key to ensuring cash is available to support funding of the Company's ongoing operations. The following table provides additional information on its working capital balances at June 30, 2008 as compared to December 31, 2007.

| (thousands of Canadian dollars) | **June 30, 2008** | December 31, 2007 | Change in working capital |
|---|---|---|---|
| Cash and cash equivalents | **4,154** | 1,756 | 2,398 |
| Accounts receivable | **5,370** | 5,121 | 249 |
| Inventory | **10,241** | 10,304 | (63) |
| Prepaids and other | **319** | 557 | (238) |
| Operating bank line | **-** | - | |
| Accounts payable and accrued liabilities | **(3,243)** | (4,127) | 884 |
| Deferred revenue | **(1,150)** | (1,403) | 253 |
| Current portion of long-term debt and capital leases | **(391)** | (370) | (21) |
| | **15,300** | 11,838 | 3,462 |

At June 30, 2008 accounts receivable were $5.4 million representing an increase of $0.2 million when compared to December 31, 2007. This increase is the result of an increase in shipments in the month of June 2008 as compared to the month of December 2007 as the receivables greater than 30 days is lower at June 30, 2008 than December 31, 2007.

The Company's investment in inventory resulted in a decrease of $0.1 million to $10.2 million at June 30, 2008 from December 31, 2007. The following table summarizes the inventory balance at June 30, 2008 compared to December 31, 2007.

| (thousands of Canadian dollars) | **June 30 2008** | December 31 2007 | Change |
|---|---|---|---|
| Raw materials | **2,761** | 3,046 | (285) |
| Work-in-progress | **4,458** | 3,867 | 591 |
| Finished goods | **3,022** | 3,391 | (369) |
| | **10,241** | 10,304 | (63) |

Work-in-progress substantially represented by confirmed orders increased by $0.6 million to $4.4 million. Raw material levels decreased by $0.3 million to $2.8 million as a result of decreases in the amount of carbon fibre and aluminum tube being held in inventory. Finished goods inventory decreased by $0.4 million to $3.0 million from the December 31, 2007 levels.

Accounts payable at June 30, 2008 were $3.2 million, compared to $4.1 million as at December 31, 2007. This decrease is representative of the decreases in production in the second quarter of 2008 when compared to the fourth quarter of 2007.

The long-term debt and capital leases,  relate to loans repayable research and development funding supplied by NRCan, a mortgage with the BDC and a capital lease.

The agreements with NRCan allow Dynetek to retain the intellectual property and to receive long-term funding. The debt is repayable only in the form of royalties based on specific related commercial product sales and is interest free. The Company has $0.3 million to be repaid in 2008. During the first six months of 2008 the Company received $0.1 million in funding from NRCan in the form of long-term debt.

As of June 30, 2008 the Company has a $5.0 million operating line of credit with Bank of Nova Scotia. As of June 30, 2008 no amounts were drawn down on this credit facility. The credit agreement requires the Company to meet specified tangible net worth ratios and working capital ratios. At June 30, 2008, the Company had not drawn down on the line (December 31, 2007 - $nil).  As at June 30, 2008 the Company is in compliance with all covenants except for the Consolidated Tangible Net Worth (TNW) covenant of $30,000,000 CAD. As at August 13, 2008, the Company has agreed in principle with the bank to reduce the line of credit to $3.5 million and to replace the Consolidated Tangible Net Worth covenant with a Shareholders Equity covenant which the Company is in compliance with.

On March 24, 2008 the Company completed a $5.0 million mortgage of its Calgary production facility with the BDC. The mortgage has a term of 15 years and bears interest at the bank prime rate plus 1.50% per annum. During the first 18 months, with the option to extend for an additional six months, the mortgage payments are interest only and do not include principal.

Dynetek continues to build on the strong strategic alliances with several major OEMs whereby confidential joint funding has been obtained to develop complete hydrogen fuel storage systems. Other research programs with strategic partners, such as government bodies, who provide financial and technical support, are also in place to explore other storage applications in the energy marketplace.

## Contractual Obligations and Commitments

The following table provides Dynetek's contractual obligations at June 30, 2008 for each of the next five years and after 2012.

(thousands of Canadian dollars)

| | Total | 2008 | 2009 | 2010 | 2011 | 2012 | Thereafter |
|---|---|---|---|---|---|---|---|
| Operating lease obligations | 1,761 | 179 | 357 | 357 | 357 | 357 | 154 |
| Capital lease obligations | 790 | 112 | 160 | 160 | 160 | 134 | 64 |
| Mortgage obligation | 7,946 | 169 | 435 | 655 | 632 | 610 | 5,445 |
| Total contractual obligations | 10,497 | 281 | 595 | 815 | 792 | 744 | 5,509 |

The Company has an obligation with a key supplier to purchase materials for approximately $0.5 million used in the normal course of business by December 31, 2008.

The Company is currently not involved in any material litigation or claims.

## Transactions with Related Parties

For the three months and six months ended June 30, 2008, the Company purchased under normal terms and conditions $1.3 million (2007 - $2.3 million) and $1.9 million (2007 - $3.7 million), respectfully, of material used in the production of lightweight fuel storage systems from Mitsubishi Rayon Corporation, a shareholder of the Company.

## Outstanding Share Data

**Issued and outstanding:**

| | **Number of Shares** | **Dollar Amount ('000)** |
|---|---|---|
| **Balance at December 31, 2007 and June 30, 2008** | **20,936,500** | **52,418** |

| | **June 30 2008** | December 31 2007 |
|---|---|---|
| **Securities convertible into common shares:** | | |
| Stock options | **887,000** | 984,500 |
| Warrants | **680,117** | 737,509 |

As at August 8, 2008, common shares outstanding were 20,936,500, options outstanding were 954,000 and warrants outstanding were 680,117.

## CHANGES IN ACCOUNTING POLICIES

As required by the Canadian Institute of Chartered Accountants ("CICA"), on January 1, 2008, the Company adopted CICA Handbook section 3031, Inventories; section 1535, Capital Disclosures; section 3862, Financial Instruments – Disclosures; section 3863, Financial Instruments – Presentation and section 1400 – General Standards of Financial Statement presentation. See Note 3 to the Consolidated Financial Statements for further details.

## INTERNAL CONTROL OVER FINANCIAL REPORTING

There were no changes in the Company's internal control over financial reporting that occurred during the most recent interim period that materially affected, or is reasonably likely to materially affect, the Company's internal control over financial reporting.

## OUTLOOK

The Company remains committed to continuing to grow its CNG and Hydrogen revenue streams globally through targeted marketing initiatives.

In 2008, the Company expects to increase its focus on revenue growth opportunities worldwide in the CNG market for bus and heavy-duty truck applications and for bulk hauling of larger quantities of compressed gas. Major economic and environmental factors worldwide are contributing to high-growth in natural gas demand for vehicles as follows:

- The high growth rate in demand for natural gas stems from the comparative advantages of natural gas compared to diesel, gasoline and bio-fuels;
- Natural gas is cleaner with less toxic emissions than diesel or gasoline and is currently less costly;
- A growing natural gas infrastructure. Continuing investment in infrastructure is adding to the number of compressed natural gas refueling centers; and
- CNG will continue to develop as a transportation fuel as it currently is less costly than oil based fuels which are also becoming supply constrained in developing economies.

The above trends and related market opportunities are expected to create a positive intermediate and longer-term outlook for Dynetek. The largest demand for CNG vehicles is in countries where low cost solutions are required. The Company is currently reviewing strategies to grow the compressed gas system revenue and is evaluating additional product development and sales in order to penetrate price sensitive markets that are actively developing CNG as a transportation fuel. To accomplish this product development and market penetration, the Company will also be evaluating strategic alliances, new joint ventures, new partners and customers, licensing arrangements, new manufacturing techniques and additional product offerings. The Company is committed to change where appropriate to attain its goals of revenue growth and net income.

In the area of bulk hauling, the Company's prime focus will be in markets with access to an abundance of natural gas, where storage technology and pipeline infrastructure are lacking. The Company has already obtained US Department of Transportation (DOT) and Transport Canada (TC) certification for its 223bar bulk hauling system and in 2008, the Company has received DOT approval to sell its 450 bar bulk systems in the US which should help it with penetrating the mobile bulk hauling storage market in 2008 and beyond.

Dynetek expects to incur a loss and negative EBITDA in Q3 of 2008 due to a slowdown in the demand for its products, specifically a postponement of public transit bus manufacturing in Europe. In June 2008 the Company announced Dynetek Europe GmbH has received a CNG complete system order from a major bus manufacturer in Europe and the systems are to be delivered from June 2008 until February 2009, representing revenue of approximately $10 million (CDN). Currently Dynetek is seeing an increase in customer enquiries and expects to see an increase in bid submissions in Q3 2008. The Company will continue to manage its costs responsibly and improve production efficiencies where possible. During the second quarter, the Company reduced production and research and development staff to core levels, reduced executive compensation and continues to review supplier alternatives.

The Company will continue to develop its hydrogen storage technologies to assist in commercializing the hydrogen economy. This includes working with OEMs to implement their hydrogen vehicle strategies and sales to energy-related companies that require mobile refueling units, stationary storage for refueling, and bulk hauling of hydrogen.

In 2008 Dynetek expects to substantially complete the contract with Magna Steyr in connection with Daimler's automotive fuel cell program. In 2007 Dynetek saw an increase in activity in the hydrogen vehicle market and continues to work with Natural Resources Canada (NRCan) and 9 different Original Equipment Manufacturers (OEMs), including Ford, Hyundai, Daimler, Volkswagen and Nissan, to design, manufacture and deliver hydrogen storage solutions on 13 different confidential development programs.

**Additional information relating to Dynetek**
Additional information concerning Dynetek, including the Company's AIF, is available on SEDAR at www.sedar.com.

Dynetek Industries Ltd. is a leading international company engaged in the design, manufacturing and marketing of fueling systems and high-pressure components including valves and regulators. The key component of the storage system is the DyneCell® cylinder, capable of storing high pressure gases including compressed natural gas (CNG), hydrogen, and various industrial gases. Dynetek's cylinder and fuel storage systems applications include but are not limited to: the transportation industry, including passenger automobiles, light and heavy-duty trucks, transit and school buses; the bulk hauling of compressed gases; and stationary storage or ground storage refueling applications.

Dynetek Industries Ltd.

# CONSOLIDATED BALANCE SHEETS

*(thousands of Canadian dollars)*
*(unaudited)*

| | **June 30 2008** | December 31 2007 |
|---|---|---|
| **ASSETS** | | |
| Current assets | | |
| Cash and cash equivalents (note 5) | **4,154** | 1,756 |
| Accounts receivable (note 6) | **5,370** | 5,121 |
| Inventory (note 7) | **10,241** | 10,304 |
| Prepaids and other | **319** | 557 |
| | **20,084** | 17,738 |
| **Intangible assets and deferred costs** | **5,345** | 5,560 |
| **Capital assets** | **15,988** | 16,594 |
| | **41,417** | 39,892 |
| **LIABILITIES** | | |
| Current liabilities | | |
| Accounts payable and accrued liabilities | **3,243** | 4,127 |
| Deferred revenue (note 2) | **1,150** | 1,403 |
| Current portion of long-term debt and capital leases (note 9) | **391** | 370 |
| | **4,784** | 5,900 |
| **Long-term debt and capital leases** (note 9) | **7,259** | 2,120 |
| **Commitments (note 11)** | | |
| **SHAREHOLDERS' EQUITY** | | |
| Share capital (note 12) | **52,418** | 52,418 |
| Contributed surplus (note 13) | **2,680** | 2,638 |
| Deficit | **(25,724)** | (23,184) |
| Accumulated other comprehensive income | **-** | - |
| | **29,374** | 31,872 |
| | **41,417** | 39,892 |

See accompanying notes to the unaudited interim consolidated financial statements

Dynetek Industries Ltd.

# CONSOLIDATED STATEMENTS OF NET LOSS, COMPREHENSIVE LOSS AND DEFICIT

*(thousands of Canadian dollars except share capital and per share amounts)*
*(unaudited)*

| | Three months ended June 30 | | Six months ended June 30 | |
|---|---|---|---|---|
| | **2008** | 2007 | **2008** | 2007 |
| **REVENUE** | | | | |
| Cylinder and system sales | **3,517** | 5,838 | **6,759** | 15,160 |
| Research and development income | **1,443** | 2,259 | **2,639** | 3,177 |
| Investment and other income | **55** | 38 | **66** | 308 |
| | **5,015** | 8,135 | **9,464** | 18,645 |
| **EXPENSES** | | | | |
| Cost of goods sold | **3,247** | 4,817 | **6,023** | 12,447 |
| General and administrative | **881** | 967 | **1,740** | 1,943 |
| Research and product development | **1,312** | 1,184 | **2,498** | 1,842 |
| Marketing | **370** | 383 | **697** | 719 |
| Interest | **108** | 33 | **176** | 101 |
| Depreciation | **389** | 397 | **754** | 755 |
| Amortization | **260** | 245 | **514** | 455 |
| Net foreign exchange (gain) loss | **(93)** | 115 | **(440)** | 114 |
| Stock based compensation (note 13) | **21** | 28 | **42** | 56 |
| | **6,495** | 8,169 | **12,004** | 18,432 |
| **Net income (loss) before income taxes** | **(1,480)** | (34) | **(2,540)** | 213 |
| **PROVISION FOR TAXES** | | | | |
| Future income tax (note 10) | **-** | 2,275 | **-** | 2,355 |
| | **-** | 2,275 | **-** | 2,355 |
| **NET LOSS AND COMPREHENSIVE LOSS** | **(1,480)** | (2,309) | **(2,540)** | (2,142) |
| Deficit, beginning of period | **(24,244)** | (18,310) | **(23,184)** | (18,477) |
| **DEFICIT, END OF PERIOD** | **(25,724)** | (20,619) | **(25,724)** | (20,619) |
| **Per Share Information** | | | | |
| Net loss per share (basic and diluted) | **(0.07)** | (0.11) | **(0.12)** | (0.10) |
| Weighted average number of common shares outstanding | **20,936,500** | 20,940,576 | **20,936,500** | 20,940,576 |

See accompanying notes to the unaudited interim consolidated financial statements

Dynetek Industries Ltd.

# CONSOLIDATED STATEMENTS OF CASH FLOWS

*(thousands of Canadian dollars)*
*(unaudited)*

| | Three months ended June | | Six months ended June | |
|---|---|---|---|---|
| | **2008** | 2007 | **2008** | 2007 |
| **Cash flows provided by (used for) operating activities** | | | | |
| **NET LOSS AND COMPREHENSIVE LOSS** | **(1,480)** | (2,309) | **(2,540)** | (2,142) |
| Items not involving cash | | | | |
| Depreciation | **389** | 397 | **754** | 755 |
| Amortization | **260** | 245 | **514** | 455 |
| Stock based compensation | **21** | 28 | **42** | 56 |
| Future income tax | **-** | 2,275 | **-** | 2,355 |
| Unrealized foreign exchange loss (gain) | **24** | 84 | **(152)** | 94 |
| | **(786)** | 720 | **(1,382)** | 1,573 |
| **Changes in non-cash working capital** | | | | |
| Accounts receivable | **(1,124)** | 2,705 | **(249)** | 2,857 |
| Inventory | **392** | (1,914) | **63** | (2,048) |
| Prepaids and other | **90** | 86 | **238** | 294 |
| Accounts payable and accrued liabilities | **39** | (501) | **(884)** | (2,253) |
| Deferred revenue | **(308)** | (2,236) | **(253)** | 562 |
| Unrealized foreign exchange (gain) loss relating to non-cash working capital | **(16)** | 14 | **102** | 8 |
| Cash flow (deficiency) from operations | **(1,713)** | (1,126) | **(2,365)** | 993 |
| **INVESTING ACTIVITIES** | | | | |
| Additions to intangible assets and deferred costs | **(85)** | (180) | **(299)** | (501) |
| Additions to capital assets | **(70)** | (443) | **(148)** | (731) |
| | **(155)** | (623) | **(447)** | (1,232) |
| **FINANCING ACTIVITIES** | | | | |
| Operating bank line | **-** | 1,990 | **-** | (380) |
| Long-term debt | **(36)** | 91 | **5,160** | 291 |
| | **(36)** | 2,081 | **5,160** | (89) |
| Foreign exchange (gains) loss on cash held in a foreign currency | **(8)** | (98) | **50** | (102) |
| **Increase (decrease) in cash and cash equivalents** | **(1,912)** | 234 | **2,398** | (430) |
| **Cash and cash equivalents, beginning of period** | **6,066** | 1,366 | **1,756** | 2,030 |
| **Cash and cash equivalents, end of period** | **4,154** | 1,600 | **4,154** | 1,600 |

Interest income received during the six month period ended June 30, 2008 was $45,000 (2007 - $15,000) and during the three month period ended June 30, 2008 was $32,000 (2007 - $6,200). Interest paid during the six month period ended June 30, 2008 was $0.2 million (2007 – $ 0.1 million) and the three month period ended June 30, 2008 was $0.1 million (2007 - $33,000).

See accompanying notes to the unaudited interim consolidated financial statements

# SELECTED NOTES TO CONSOLIDATED FINANCIAL STATEMENTS

## For the three months and six months ended June 30, 2008 and 2007 and as at December 31, 2007

*(tabular amounts in thousands of Canadian dollars, except share capital amounts)*
*(unaudited)*

### 1. BASIS OF PRESENTATION

These unaudited interim consolidated financial statements have been prepared by management of Dynetek Industries Ltd. ("Dynetek" or "the Company") in accordance with Canadian generally accepted accounting principles and should be read in conjunction with Dynetek's audited consolidated financial statements and notes for the year ended December 31, 2007. The accounting policies and methods of application used in the preparation of these unaudited interim consolidated financial statements are consistent with the accounting policies used in Dynetek's most recent audited year end consolidated financial statements, except as described in note 3.

### 2. SIGNIFICANT ACCOUNTING POLICIES

**a) Revenue recognition**
Cylinder and system revenue is recognized when finished goods are shipped to the customer.
Research and development revenue is generated by projects co-funded with the original equipment manufacturers (OEMs) and government agencies. This revenue is recognized when contractual deliverables and milestones are met. Timing differences can occur between when costs are incurred and when revenue is invoiced and earned. Customer billings for services not yet rendered or customer deposits are received and deferred and recognized as revenue when the services are rendered and finished goods are shipped to the customer. Any associated deferred revenue is included in current liabilities. Once these services are rendered or product is shipped, the deferred revenue is recognized as income.

**b) Research and development costs**
Research and development costs are expensed as incurred.

**c) Financial Instruments**
All financial assets and liabilities are recognized when the Company becomes a party to the contract creating the item. Financial assets and financial liabilities are initially recognized at fair value and are subsequently accounted for based on their classification. The classification depends on the purpose for which the financial instruments were acquired and their characteristics. Except in very limited circumstances, the classification is not changed subsequent to initial recognition.

The Company has applied the following classifications to each of its significant categories of financial instruments:

| | |
|---|---|
| Cash and cash equivalents | Designated as held-for-trading |
| Accounts receivable | Loans and receivables |
| Accounts payable and accrued liabilities | Other liabilities |
| Operating bank line | Other liabilities |
| Long-term debt and capital leases | Other liabilities |
| Derivative Instruments | Designated as held-for-trading |

Financial instruments that are classified as held-for-trading are re-measured each reporting period at fair value with the resulting gain or loss recognized immediately in net income and other comprehensive income, respectively. All other financial instruments are accounted for at amortized cost with foreign exchange gains and losses recognized immediately in net income.

Derivative instruments are recorded on the consolidated balance sheet at fair value, including those derivatives that are embedded in financial contracts. Changes in the fair values of derivative instruments are recognized through the consolidated statements of net income (loss), comprehensive income (loss) and deficit.

Derivatives embedded in other financial instruments or contracts are separated from their host contracts and accounted for as derivatives when their economic characteristics and risks are not closely related to those of the host contract. If the terms of the embedded derivative are the same as those of a free standing derivative, and the combined instrument or contract is not measured at fair value, any changes in fair value are recognized in consolidated statements of net income (loss), comprehensive income (loss) and deficit (See Note 16 (d)).

The Company records interest income and interest expense as it is received or it is paid.

## 3. CHANGES IN ACCOUNTING POLICIES

As required by the Canadian Institute of Chartered Accountants ("CICA"), on January 1, 2008, the Company adopted CICA Handbook section 3031, Inventories; section 1535, Capital Disclosures; section 3862, Financial Instruments – Disclosures; section 3863, Financial Instruments – Presentation and section 1400 – General Standards of Financial Statement presentation.

### a) Inventories, Section 3031

Effective January 1, 2008, the Company adopted the recommendations of the CICA Handbook Section 3031, Inventories, which replaces Section 3030. The new section is harmonized with International Accounting Standards and provides additional guidance on the measurement and disclosure requirements for inventories. The standard requires inventory to be measured at the lower of cost and net realizable value. Cost of inventories shall be composed of all costs of purchase, costs of conversion and other costs incurred in bringing the inventories to their present location and condition. Net realizable value is the estimated selling price in the ordinary course of business less the estimated costs of completion and the estimated costs necessary to make the sale. When inventories are sold, the carrying amounts of those inventories shall be recognized as an expense in the period in which the related revenue is recognized. The amount of any write-down of inventories to net realizable value and all losses of inventories shall be recognized as an expense in the period the write-down or loss occurs. The amount of any reversal of any write-down of inventories, arising from an increase in net realizable value, shall be recognized as a reduction in the amount of inventories recognized as an expense in the period in which the reversal occurs. The new disclosures are included in Note 7.

### b) Capital Disclosures, Section 1535

Effective January 1, 2008, the Company adopted the CICA Handbook section 1535, Capital Disclosures. Section 1535 establishes standards for disclosing information about an entity's capital and how it is managed. It requires the disclosure of information about: (i) an entity's objectives, policies and processes for managing capital; (ii) qualitative data about what the entity regards as capital; (iii) whether the entity has complied with any capital requirement, and if it has not complied, the consequences of such non-compliance. The new disclosures are included in Note 15.

### c) Financial Instruments, Section 3862 and 3863

Effective January 1, 2008, the Company adopted the new recommendations of CICA Handbook section 3862, Financial Instruments – Disclosures ('section 3862') and CICA Handbook section 3863, Financial Instruments – Presentation ('section 3863').

Section 3862 requires entities to provide disclosures in their financial statements that enable users to evaluate the significance of financial instruments on the entity's financial position and its performance and the nature and extent of risks arising from financial instruments to which the entity is exposed during the period and at the balance sheet date, and how the entity manages those risks.

Section 3863 establishes standards for presentation of financial instruments and non-financial derivatives. It deals with the classification of non-financial instruments, from the perspective of the issuer, between liabilities and equities, the classification of related interest, dividends, losses and gains, and circumstances in which financial assets and financial liabilities are offset.

The adoption of these standards did not have impact on the classification and valuation of the Company's financial instruments. The Company has included disclosures recommended by these new Handbook Sections in Note 16.

### d) General Standards of Financial Statement presentation, Section 1400

Effective January 1, 2008, the Company adopted the revised recommendations of the CICA Handbook Section 1400, General Standards of Financial Statement Presentation. Section 1400 was amended to include requirements to assess and disclose an entity's ability to continue as a going concern. The adoption of this new section does not have an impact on the financial statements.

## 4. FUTURE ACCOUNTING STANDARD CHANGES

The following is an overview of accounting standard changes that the Company will be required to adopt in future years:

Goodwill and Intangible Assets

In February 2008, the CICA issued Section 3064, Goodwill and Intangible Assets, replacing Section 3062, Goodwill and Other Intangible Assets and Section 3450, Research and development costs. Various changes have been made to other sections of the CICA Handbook for consistency purposes. The new Section will be applicable to financial statements relating to fiscal years beginning on or after October 1, 2008. Accordingly, the Company will adopt the new standards for its fiscal year beginning January 1, 2009. Section 3064 establishes standards for the recognition, measurement, presentation and disclosure of goodwill subsequent to its initial recognition and of intangible assets by profit-oriented enterprises. Standards concerning goodwill are unchanged from the standards included in the previous Section 3062. The Company is currently evaluating the impact of the adoption of this new Section on its consolidated financial statements. The Company does not expect that the adoption of this new Section will have a material impact on its consolidated financial statements.

## 5. CASH AND CASH EQUIVALENTS

Cash and cash equivalents consist of cash on deposit and highly liquid short-term interest bearing securities with maturities at the date of purchase of three months or less. The Company has $0.4 million (2007 - $0.4 million) in restricted cash, invested in a guaranteed investment certificate bearing interest at 2.30%, representing funds used as security for guarantees of loans between members of management and a major chartered bank for the purchase of common shares of the Company.

## 6. ACCOUNTS RECEIVABLE

| | **June 30 2008** | December 31 2007 |
|---|---|---|
| Accounts receivable – trade | **4,295** | 3,983 |
| Accounts receivable - other | **1,075** | 1,138 |
| Allowance for doubtful accounts | **-** | - |
| | **5,370** | 5,121 |

The aging of trade receivables as at June 30, 2008 is set out below:

| | |
|---|---|
| Current | 3,139 |
| Past Due 0 – 30 days | 813 |
| Past Due 31 – 60 days | 86 |
| Past Due 61 – 90 days | 203 |
| Past 90 days | 54 |
| | **4,295** |

Accounts receivable - other mainly consist of government funding receivable and value added tax receivable from the government. The Company evaluates the ability to collect each receivable by customer and as at June 30, 2008 the Company believes all of the receivables are collectable and therefore no provision for doubtful accounts has been made. See note 15 for a description of the Company's management of credit risk. This has resulted in some customer accounts exceeding their due dates. Management expects all amounts to be collectible. Of the amounts greater than 60 days, $0.1 million has been collected subsequent to June 30, 2008.

## 7. INVENTORY

| | **June 30 2008** | December 31 2007 |
|---|---|---|
| Raw materials | **2,761** | 3,046 |
| Work-in-progress | **4,458** | 3,867 |
| Finished goods | **3,022** | 3,391 |
| | **10,241** | 10,304 |

The Company measures its inventory at lower of cost and net realizable value. Cost includes the costs associated with getting the inventory to the manufacturing plant. Work-in-progress and finished goods inventory include costs associated with direct labour and include an allocation of fixed and variable production overhead associated with converting raw materials into finished goods.

During the period the Company did not hold any inventory at net realizable value, write-down any inventory, did not reverse any write-downs previously taken, and has pledged inventories as security for the Bank of Nova Scotia operating line of credit, which the Company has not drawn down on as at June 30, 2008.

## 8. OPERATING BANK LINE

As at June 30, 2008, the Company has a $5.0 million line of credit with the Bank of Nova Scotia, which is payable on demand and bears interest at the bank prime rate plus 1.25% per annum. The bank line is secured by an assignment of book debts and inventory. The credit agreement requires the Company to meet specified tangible net worth ratios and working capital ratios. At June 30, 2008, the Company had not drawn down on the line (December 31, 2007 - $nil). As at June 30, 2008 the Company is in compliance with all covenants except for the Consolidated Tangible Net Worth (TNW) covenant of $30,000,000 CAD. As at August 13, 2008, the Company has agreed in principle with the bank to reduce the line of credit to $3.5 million and to replace the Consolidated Tangible Net Worth covenant with a Shareholders Equity covenant which the Company is in compliance with.

## 9. LONG-TERM DEBT AND CAPITAL LEASES

| | **June 30, 2008** | December 31, 2007 |
|---|---|---|
| Loans, unsecured, non-interest bearing, repayment based on 3% to 5% of product related sales, payable in the following fiscal period [a] | **2,014** | 1,869 |
| Capital lease obligations [b] | **636** | 621 |
| Mortgage [c] | **5,000** | - |
| **Total long term debt and capital leases** | **7,650** | 2,490 |
| Less: current portion | **(391)** | (370) |
| **Long term debt and capital leases** | **7,259** | 2,120 |

a) The repayment of unsecured repayable loans to Natural Resources Canada (NRCan) beyond the current year is indeterminable. Repayments of amounts owing are based on future sales of specific related commercial products over a specified period of time. As such the Company cannot determine the amount to be paid over the next five years.

b) The Company has a sale-leaseback for manufacturing assets located at its subsidiary in Germany. The capital lease obligation bears interest at 7.3% per annum, is repayable on a monthly basis and is amortized over a 72 month term. Upon completion of the lease, the Company has the option to purchase the assets for $19,000. During the six month period ended June 30, 2008, $28,000 of interest was paid on the capital lease.

c) In March 2008, the Company completed a $5.0 million mortgage of its Calgary production facility with the Business Development Bank of Canada ('BDC'). The mortgage has a term of 15 years and bears interest at the bank prime rate plus

1.50% per annum. During the first 18 months, with the option to extend for an additional six months, the mortgage payments are interest only and do not include principal. All financing transaction costs have been expensed.

**10. PROVISION FOR INCOME TAXES**

Until June 30, 2007, the future income tax asset represented non-capital loss carry forwards that the Company expected to utilize in future periods to offset current taxes payable. Based on the delays in orders received in the European bus market place, the Company determined that for financial statement purposes the asset was impaired and reduced the value to $nil. The balance of $2.3 million was expensed to the income statement as at June 30, 2007. The non-capital loss carry-forwards for income tax have not been affected by the financial statement impairment.

**11. COMMITMENTS**

The Company has obligations under operating lease, mortgage and capital lease arrangements which require the following minimum annual payments during the respective fiscal years:

| | |
|---|---|
| 2008 | 452 |
| 2009 | 937 |
| 2010 | 1,157 |
| 2011 | 1,134 |
| 2012 | 1,086 |
| Thereafter | 6,023 |

The Company is currently not involved in any material litigation or claims.

The Company has an obligation with a key supplier to purchase materials for approximately $0.5 million used in the normal course of business by December 31, 2008.

**12. SHARE CAPITAL**

The issued and outstanding common shares of the Company along with securities convertible into common shares are as follows:

**Issued and outstanding:**

| | Number of Shares | Amount |
|---|---|---|
| **Balance at December 31, 2007 and June 30, 2008** | **20,936,500** | **52,418** |

| | June 30 2008 | December 31 2007 |
|---|---|---|
| **Securities convertible into common shares:** | | |
| Stock options | **887,000** | 984,500 |
| Warrants | **680,117** | 737,509 |

The estimated fair value of the options used for accounting purposes has been determined using the Black Scholes option-pricing model with the following assumptions:

| | Six months ended June 30 | |
|---|---|---|
| | **2008** | 2007 |
| Weighted average risk-free interest rate | **3.45%** | 4.59% |
| Weighted average expected life | **5 years** | 5 years |
| Estimated volatility in the market price of the common shares | **86%** | 76% |
| Dividend yield | **0%** | 0% |

The weighted average fair value per option was $nil for the six months ended June 30, 2008 and $1.73 for the comparable period of 2007.
During the first six months of 2008, nil (2007 – 56,000) options were issued to employees.

## 13. CONTRIBUTED SURPLUS

The following table summarizes information about contributed surplus.

| | |
|---|---|
| Balance at December 31, 2007 | 2,638 |
| Stock based compensation expense | 42 |
| **Balance at June 30, 2008** | **2,680** |

## 14. TRANSACTIONS WITH RELATED PARTIES

For the three months and six months ended June 30, 2008, the Company purchased under normal terms and conditions $1.3 million (2007 - $2.3 million) and $1.9 million (2007 - $3.7 million), respectfully, of material used in the production of lightweight fuel storage systems from Mitsubishi Rayon Corporation, a shareholder of the Company.

## 15. CAPITAL RISK MANAGEMENT

The Company's objective when managing capital is to safeguard its accumulated capital in order to maintain its ability to continue as a going concern and to provide returns to shareholders and benefits to other stakeholders. The capital structure of the Company consists of equity and debt and is summarized in the table below;

| | **June 30 2008** | December 31 2007 |
|---|---|---|
| Shareholders' Equity | **29,344** | 31,872 |
| Long-term debt and leases, including current portion | **7,650** | 2,490 |
| Total Capital | **36,994** | 34,362 |

The Company manages its capital structure and makes adjustments to it in light of economic conditions. The Company, upon approval from its Board of Directors, will balance its overall capital structure through new share or debt issuances or by undertaking other activities as deemed appropriate under the specific circumstances.

The Company is not subject to externally imposed capital requirements other than the operating line of credit agreement requires the Company to meet specified tangible net worth and working capital ratios (1.5:1). The Company's overall strategy with respect to capital risk management remains unchanged from the year ended December 31, 2007.

## 16. FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT

### a) Credit Risk

The Company is exposed to credit risk as it grants unsecured credit to its customers. Certain European customers' accounts are insured through Export Development Canada. All customers are subject to credit approval prior to acceptance of purchase order. Credit terms vary from cash on delivery to 90 days depending on the risk of each customer. Each customer has a credit limit established by management and once the customer reaches the credit limit, shipments are halted until payments are made. The Company currently does not have any receivables outstanding to one customer greater than 10% of the Company's outstanding receivable balance.

The Company assesses quarterly if there has been any impairment of financial assets. As at June 30, 2008, management determined there was no impairment of any of the financial assets of the Company.

The carrying value of the accounts receivable approximates their fair value due to the relatively short periods to maturity on these instruments. The maximum exposure to credit risk is represented by the carrying amount on the balance sheet. There are no material financial assets that the Company considers past due.

## b) Market Risk

### Interest Rate Risk

Interest rate risk refers to the risk that cash flows associated with a financial instrument will fluctuate due to changes in market interest rates. The Company is exposed to interest rate cash flow risk on floating interest rate bank debt due to fluctuations in market interest rates.

As at June 30, 2008, the Company has a $5.0 million line of credit with the Bank of Nova Scotia, which is payable on demand and bears interest at the bank prime rate plus 1.25% per annum. As at June 30, 2008 the Company was not drawn down on this facility. The credit agreement requires the Company to meet specified tangible net worth ratios and working capital ratios. The credit agreement requires the Company to meet specified tangible net worth ratios and working capital ratios. At June 30, 2008, the Company had not drawn down on the line (December 31, 2007 - $nil). As at June 30, 2008 the Company is in compliance with all covenants except for the Consolidated Tangible Net Worth (TNW) covenant of $30,000,000 CAD. As at August 13, 2008, the Company has agreed in principle with the bank to reduce the line of credit to $3.5 million and to replace the Consolidated Tangible Net Worth covenant with a Shareholders Equity covenant which the Company is in compliance with. The Company has a $5.0 million mortgage of its Calgary production facility with the Business Development Bank of Canada ('BDC'). The mortgage has a term of 15 years and bears interest at the bank prime rate plus 1.50% per annum. During the first 18 months, with the option to extend for an additional six months, the mortgage payments are interest only and do not include principal.

The remainder of the Company's financial assets and liabilities are not exposed to interest rate risk. The Company currently does not use interest rate hedges or fixed interest rate contracts to manage the Company's exposure to interest rate fluctuations.

A 0.25% change in the interest rate would have impacted the net income (loss) of the Company during the six months ended June 30, 2008 by approximately $6,250. A sensitivity of 0.25 percent was selected as this is considered reasonable given the current level of the bank prime rate and market expectations for future movements.

### Foreign currency risk

The Company is exposed to foreign currency risk arising from operations and sales outside of Canada. A significant portion of the Company's revenues and expenses are denominated in United States dollars and Euros. The Company's cash flow from sales will therefore be impacted by fluctuations in foreign exchange rates.

The Company does not use foreign exchange rate hedges or fixed foreign exchange contracts to manage the Company's exposure to foreign exchange rate fluctuations.

A $0.05 increase or decrease in the Canadian / EURO exchange rate would have impacted the net income (loss) of the Company by $25,000. A sensitivity of five percent was selected as this is considered reasonable given the current level of the Canadian to EURO exchange rate and market expectations for future movements.

A $0.05 CDN increase or decrease in the Canadian / US exchange rate would have impacted the net income (loss) of the Company by $156,000. A sensitivity of five percent was selected as this is considered reasonable given the current level of the Canadian to US dollar exchange rate and market expectations for future movements.

## c) Liquidity Risk

Liquidity risk includes the risk that, as a result of the Company's operational liquidity requirements:

- The Company will not have sufficient funds to settle a transaction on the due date;
- The Company will be forced to sell financial assets at a value which is less than what they are worth; or
- The Company may be unable to settle or recover a financial asset at all.

The Company's operating cash requirements including amounts projected to complete its existing capital expenditure program are continuously monitored and adjusted as input variables change. These variables include but are not limited to, available bank lines, order back log from existing customers, ability of the Company to develop new customers, raw material pricing, competitors entering the market resulting in the Company reducing sales prices in order to maintain market share, and cost overruns in capital projects. As these variables change, liquidity risks may necessitate the need for the Company to conduct equity issues or obtain project debt financing.

The following table provides Dynetek's cash flow on contractual obligations at June 30, 2008 for each of the next five years and after 2012.

(thousands of Canadian dollars)

| | Total | 2008 | 2009 | 2010 | 2011 | 2012 | Thereafter |
|---|---|---|---|---|---|---|---|
| Capital lease obligations | 790 | 112 | 160 | 160 | 160 | 134 | 64 |
| Mortgage obligation | 7,946 | 169 | 435 | 655 | 632 | 610 | 5,445 |
| Total contractual obligations | 8,736 | 281 | 595 | 815 | 792 | 744 | 5,509 |

**d) Fair values of Financial Instruments**

The Company's financial instruments are classified as cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, operating bank line, capital lease, mortgage and loans. The carrying value and fair value of these financial instruments at June 30, 2008 is disclosed below by financial instrument category:

| **Financial Instrument** | **Carrying Value** | **Fair Value** | **Foreign Exchange** |
|---|---|---|---|
| **Assets held for Trading** | | | |
| Cash and cash equivalents | 4,154 | 4,154 | - |
| **Loans and Receivables** | | | |
| Accounts receivables | 5,370 | 5,370 | - |
| **Other Liabilities** | | | |
| Accounts payable and accrued liabilities [(1)] | 3,243 | 3,243 | 1 |
| Loans[(2)] | 2,014 | 2,014 | - |
| Mortgage | 5,000 | 5,000 | - |
| Capital lease | 636 | 636 | - |

(1) Included in accounts payable is $1,000 relating to contracts with customers that had not been fulfilled as at June 30, 2008 and which contained embedded derivatives as the Company has sale contracts in currencies (U.S. dollars and Euros) that are not the functional currency of either the customer or the Company.

(2) The fair values of the loans cannot be measured reliably due to the lack of set repayment terms.

**17. SEGMENTED INFORMATION**

The Company currently conducts business in one operating segment, which involves the manufacture and sale of lightweight fuel storage systems. The majority of the Company's operations and assets relating to commercial production were located in Canada at June 30, 2008. Revenues attributed to foreign countries are based on the location of the customer.

| | **Three months ended June 30** | | **Six months ended June 30** | |
|---|---|---|---|---|
| | **2008** | 2007 | **2008** | 2007 |
| Cylinder and system sales | | | | |
| Canada | **419** | 840 | **488** | 958 |
| United States | **636** | 1,121 | **1,065** | 3,701 |
| Japan | **57** | 504 | **176** | 1,094 |
| European Union | **2,087** | 3,152 | **4,525** | 8,932 |
| Other | **318** | 221 | **505** | 475 |
| | **3,517** | 5,838 | **6,759** | 15,160 |