

ZTEST Electronics Inc.

Management's Discussion and Analysis

For The Year Ended June 30, 2015

(Prepared as at October 22, 2015)

General

The following management's discussion and analysis ("MD&A") of the financial condition and results of operations of ZTEST Electronics Inc. ("ZTEST" or the "Company") constitutes management's review of the factors that affected the Company's consolidated financial and operating performance for the year ended June 30, 2015. The MD&A was prepared as of October 22, 2015 and was approved by the Board of Directors on October 22, 2015. It should be read in conjunction with the consolidated financial statements of the Company for the year ended June 30, 2015, including the notes thereto. Unless otherwise stated, all amounts discussed herein are denominated in Canadian dollars.

Additional information about the Company can be found at www.sedar.com.

The Company

The Company operates a single business segment involving the design, development, and assembly of printed circuit boards. The Company's shares trade on the Canadian Securities Exchange under the symbol "ZTE".

The management of the Company is comprised of the following individuals:

<u>Name</u>	<u>Position(s)</u>
Wojciech Drzazga	Director and CEO
John Perreault ⁽¹⁾	Director and President
K. Michael Guerreiro ^{(1) (2)}	Director
Mike Hiscott ^{(1) (2)}	Director
Michael D. Kindy	VP Finance & CFO
William R. Johnstone	Secretary

⁽¹⁾ Denotes member of audit committee

⁽²⁾ Denotes member of compensation committee

Corporate Performance

The 2015 fiscal year provided some operational challenges while generating positive cash flow from operations as well as significant improvements in the Company's liquidity and capital.

Cash management has long been a focal point for the Company and 2015 represents the tenth consecutive fiscal year for which cash flows from operations have been positive. The positive cash flows throughout this extended period have enabled the Company to invest in its future through strategic equipment additions while also retiring the debts from its past. This emphasis on cash management now enables the Company to go forward into 2016 with financial burdens, and the associated risks, at an all-time low. Cash management will continue to be a point of emphasis and it is anticipated that positive cash flows will continue.

Challenges certainly did arise in 2015 with mergers and acquisitions having a tangible impact upon the Company's marketplace. This includes the acquisition of certain of the Company's customers by U.S. based entities and the redistribution of much of the demand from those customers to U.S. based competitors. The greatest impact of this market activity was experienced in the second quarter when revenues dropped approximately 30% below what had become the quarterly norm. This was followed by a third quarter sale of excess materials, which had been acquired to service a then significant customer, to that customer under the expectation that they would no longer be used in production. The Company not only withstood this challenge but succeeded in replacing departed revenues such that annual revenues declined by less than 2% and annual operating profits were only marginally below break-even. It is anticipated that there will continue to be changes in the market place however management is optimistic that the greatest impact has already been absorbed and that future changes will be less challenging.

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Corporate Performance - continued

During that challenging second quarter the Company successfully concluded negotiations with its former preferred shareholders. Preferred shares had been issued from 2001 to 2003 as a means of funding the Company's operations at that time. These preferred shares had dividend and redemption rights which resulted in an obligation of \$928,839. This unsecured obligation, which had been on the Company's books since 2007, was settled during the second quarter in exchange for a cash payment of \$166,378 thereby adding \$762,461 to the Company's capital position.

The redemption of the preferred shares, the simultaneous waiving of accrued dividends by the preferred shareholders, and the forgiveness of \$51,545 in other short term obligations not only improved the Company's capital position but also had a significant impact upon the Company's liquidity position and eliminated a major source of business risk. Although those obligations were unsecured and bore no carrying costs their existence was still impactful upon the Company including their effect upon the availability and cost of business financing. As at June 30, 2015 the Company has a working capital surplus, current financial assets that exceed its current and total liabilities, and is financed exclusively through commercial working capital and term debt with market-based carrying costs.

The overall financial health of the Company has never been better and management is eager to move forward and to continue efforts to maximize return for stakeholders and minimize business risks. The following data may provide some additional insights relative to the Company's operating performance and financial position:

	For the fiscal years ended:				
	<u>June 15</u>	<u>June 14</u>	<u>June 13</u>		
Total Revenues	3,945,720	4,014,268	4,601,698		
Net income (loss) income from operations	(33,397)	(21,321)	141,007		
Per share - basic	(0.003)	(0.002)	0.017		
Net income (loss) for the year	560,333	(18,579)	148,319		
Per share - basic	0.053	(0.002)	0.018		
Total assets	1,770,999	2,098,100	2,176,189		
Total long-term financial liabilities	121,769	158,244	45,788		
Total liabilities	720,921	1,638,734	1,759,668		
	For the three month periods ended:				
	<u>June 15</u>	<u>Mar. 15</u>	<u>Dec. 14</u>	<u>Sept. 14</u>	<u>June 14</u>
Total Revenues	1,122,088	1,061,276	691,622	1,070,734	1,000,676
Net income (loss) from operations	111,838	(17,243)	(154,718)	26,726	(21,790)
Per share - basic	0.011	(0.002)	(0.015)	0.002	(0.002)
Net income (loss) for the period	111,838	(17,091)	438,159	27,427	(20,988)
Per share - basic	0.011	(0.002)	0.041	0.002	(0.002)
Total assets	1,770,999	1,600,781	1,715,098	1,971,431	2,098,100
Total long-term financial liabilities	121,769	131,642	141,516	151,388	158,244
Total liabilities	720,921	662,541	759,767	1,484,638	1,638,734
	For the three month periods ended:				
	<u>Mar. 14</u>	<u>Dec. 13</u>	<u>Sept. 13</u>	<u>June 13</u>	<u>Mar. 13</u>
Total Revenues	933,391	945,951	1,134,250	1,288,374	1,127,445
Net income (loss) from operations	(3,300)	(59,301)	63,070	81,609	21,311
Per share - basic	(0.000)	(0.006)	0.006	0.008	0.003
Net income (loss) for the period	(2,521)	(58,928)	63,858	83,815	22,379
Per share - basic	(0.000)	(0.006)	0.006	0.008	0.003
Total assets	2,190,139	1,859,824	2,102,184	2,176,189	2,228,452
Total long-term financial liabilities	177,893	18,830	32,498	45,788	57,496
Total liabilities	1,709,785	1,381,168	1,614,305	1,759,668	2,036,126

There were no cash dividends paid or accrued during any of the periods noted above.

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Results of Operations

The final quarter of 2015 provided the largest profit from operations that the Company has realized since the all-time high reported for the quarter ended March 31, 2012. This profit, however, was not quite sufficient to overcome a particularly weak second quarter as, for the second consecutive year, operating results were just below the break-even level. There are many factors that contribute to the Company's operating results and the highlights are discussed below.

Revenues for the final quarter were almost 6% higher than they were in the preceding quarter and more than 12% greater than the final quarter of 2014. The two most recent quarters each provided revenues that were greater than reported for the comparable quarter one year earlier signalling the end to a five quarter period when revenues declined on that same year over year basis. In spite of the revenue growth realized over the final six months the annual revenues still declined in comparison to the prior year, albeit by less than 2%. The marginal decline in annual revenues was the direct result of the uncharacteristically low revenues realized in the second quarter. It is believed that the final six months signifies that the Company has successfully replaced production that departed to the U.S. however the marketplace remains highly competitive and additional market consolidation may still occur.

Gross margins for 2015 amounted to \$1,187,243 or 30% of revenues or lower than had been realized in the 2014 year when margins were \$1,370,984 or 34% of revenues. Although changes in the marketplace contributed to the 2015 decline there was also the 24% margins realized in the second quarter and the third quarter component sales to a departing customer that served to reduce margins for that quarter by 3%. Gross margins have fluctuated from period to period and have often been impacted by specific events just as they were in the final quarter of 2015 when equipment acquisitions led to increased periodic depreciation charges. Management constantly strives to control costs in order to maximize longer term margins and profitability and believes that the 36% gross margins realized in the most recent quarter are a solid indication of adherence to this objective. A better understanding of the margins can be achieved through review of the elements of the cost of product sales.

The different elements of cost of product sales, and the changes realized, are as follows:

Years ended	June 15	June 14	Change
Raw materials and supplies consumed	\$ 1,837,993	\$ 1,588,919	\$ 249,074
Labour costs incurred	645,467	761,263	(115,796)
Depreciation	132,358	141,355	(8,997)
Other costs	135,135	138,285	(3,150)
Net change in finished goods and work in process	7,524	13,462	(5,938)
Total cost of product sales	\$ 2,758,477	\$ 2,643,284	\$ 115,193

Three month periods ended	June 15	June 14	Change
Raw materials and supplies consumed	\$ 502,105	\$ 402,125	\$ 99,980
Labour costs incurred	145,068	203,776	(58,708)
Depreciation	33,089	49,695	(16,606)
Other costs	35,655	47,776	(12,121)
Net change in finished goods and work in process	814	(4,089)	4,903
Total cost of product sales	\$ 716,731	\$ 699,283	\$ 17,448

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Results of Operations - continued

The cost of materials consumed in the final quarter of 2015 was 25% higher than in the similar period ended June 30, 2014 signifying that, like the preceding quarter, a larger proportion of assemblies are being produced from components supplied by the Company as opposed to consignment items provided by customers. The inverse was true during the first 6 months of the 2015 fiscal year however as material costs were lower during that period than they had been in fiscal 2014. Materials costs for the current year also include approximately \$125,000 on account of materials that were sold during the third quarter to departing customers. This type of transaction occurs from time to time but the 2015 transactions were of greater magnitude than the norm. The Company continuously promotes the supply of components as a cost effective solution for its customers however this service remains at the customers' discretion so the materials costs will always vary from period to period.

Labour cost incurred is a measure of labour paid for during the period and reflects a decrease of almost 29% for the quarter and over 15% for the year. Virtually all of the annual cost savings arose during the final six months of the year. In December 2014 the Company implemented a government approved work-share program which, generally speaking, resulted in a 20% reduction in work hours and the corresponding payroll costs without any permanent reduction in the work force. This provided the cost savings realized without impeding the Company's ability to react to increased labour demand, should it arise. The work-share program ended August 2015 at which time labour supply returned to 100%.

The total labour costs included in cost of product sales combine the labour cost incurred with the net change in finished goods and work in process, which is a measurement of the change in labour costs that are included as an element of inventory. The combined figures have declined by 27% for the quarter and 16% for the year. During the 2014 year the Company produced a number of labour intensive products, often resulting in the incurrence of overtime. There have been no comparable occurrences in 2015 as demand was below capacity as suggested by the existence of the work-share program.

Depreciation costs are lower in 2015 year than they were in the 2014 year even though fourth quarter costs were higher last year. The higher cost in the fourth quarter of 2014 was attributable to an equipment addition completed in January 2014 and installed and placed into use in the final quarter. This contributed to the annual decline in 2015 being less than the decline when comparing the final quarter of each year. Depreciation has no correlation with revenues as it is purely a function of time and the carrying value of the manufacturing equipment in use. There are no major equipment additions currently being investigated or considered although management remains diligent in monitoring the equipment market for opportunities that could help to further increase productivity or profitability.

Other costs include repairs and maintenance, stencils and tooling, packaging, and freight costs net of amounts recovered. Each of these costs is incurred on an as-needed basis without any specific correlation with revenues. These costs are closely monitored and are within management expectations so they will not be further elaborated upon.

Selling, general and administrative expenses for the periods ended June 30 were as follows:

Years ended	June 15	June 14	Change
Employee and consultant compensation	\$ 782,492	\$ 856,871	\$ (74,379)
Occupancy costs	261,829	264,970	(3,141)
Professional fees	62,684	75,703	(13,019)
Insurance	33,906	33,694	212
Shareholder services	21,742	25,390	(3,648)
Bad debts	-	3,169	(3,169)
Other costs	42,849	47,250	(4,401)
Total selling, general and administrative	\$ 1,205,502	\$ 1,307,047	\$ (101,545)

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Results of Operations - continued

Three month periods ended	June 15	June 14	Change
Employee and consultant compensation	\$ 191,258	\$ 214,920	\$ (23,662)
Occupancy costs	65,203	64,278	925
Professional fees	15,773	14,595	1,178
Insurance	8,208	8,744	(536)
Shareholder services	1,800	2,393	(593)
Bad debts	-	3,169	(3,169)
Other costs	7,961	10,163	(2,202)
Total selling, general and administrative	\$ 290,203	\$ 318,262	\$ (28,059)

Compensation costs include salaries and benefits, consulting fees and directors' fees, each of which have declined in 2015. The number of independent directors declined from 3 to 2 resulting in a cost reduction. In 2014 there was \$44,000 paid to outside consultants in 2014 to investigate certain business opportunities and this did not recur in 2015. In addition, the effects of the work-share program, combined with lower sales commissions and employee benefit costs, more than offset annual pay rate changes that took effect in January.

Occupancy costs consist primarily of rent and utility charges for the Company's operating facility. Basic rental charges increase by approximately 2% in January of each year but these have been offset by reductions in utility charges. The lease for the Company's operating facility runs through March 2021 and these costs are expected to remain generally comparable throughout that lease term.

Professional fees are comprised of the cost of legal services as well as the cost of the annual financial statement audit. Audit expenses have remained comparable between the 2015 and 2014 periods however legal fees have declined in 2015 due to there being no securities based transactions in 2015 and lower costs associated with the annual shareholders' meeting held during the year.

Shareholder services include the cost of public disclosures, distribution of materials to shareholders, stock exchange fees, and transfer agent fees. The nature and cost of these services has remained reasonably comparable between the 2015 and 2014 periods except that filing fees incurred in 2014 in relation to the related party financing did not recur in 2015.

The Company has an excellent history with respect to the collection of its accounts receivable. The small bad debt that arose in 2014 was the anomaly as most years have no similar costs.

The remaining elements of SG&A are individually insignificant and, in aggregate, represent less than 5% of total SG&A for the periods presented. These expenses are continuously monitored by management and do not warrant detailed investigation or elaboration.

Even though the Company put new financing in place to fund the acquisition of equipment the debt load, and the associated costs of financing, continues to decline. They are comprised of interest on long-term debt, other interest expense, and loan guarantee fees as follows:

Years ended	June 15	June 14	Change
Interest expense ó long term (cash based)	\$ 11,164	\$ 21,636	\$ (10,472)
Interest expense ó long term (accretion)	4,473	9,149	(4,676)
Interest expense ó other	1,523	4,614	(3,091)
Total financing expenses	\$ 17,160	\$ 35,399	\$ (18,239)

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Results of Operations - continued

Three month periods ended	June 15	June 14	Change
Interest expense ó long term (cash based)	\$ 1,944	\$ 6,042	\$ (4,098)
Interest expense ó long term (accretion)	101	712	(611)
Interest expense ó other	155	1,497	(1,342)
Total financing expenses	\$ 2,200	\$ 8,251	\$ (6,051)

The Company has been extremely diligent with respect to retiring its long-term debt and this has resulted in significant reductions in long term interest costs and on the associated cash flow burden. In the 2015 fiscal year the Company reduced its long term debt from 4 obligations aggregating \$281,933 with a weighted average interest rate of 8.06% to a single obligation of \$161,262 bearing interest at the TD Bank prime lending rate (currently 2.70%) plus 1.75%.

Interest accretion arises when the fair value of an obligation, at its inception, is determined to be different from its face value. All debts giving rise to accretion were retired during the 2015 fiscal year.

Interest expense ó other includes any interest incurred except that related to long term debt. Interest arising in 2015 relates to modest use of the Company's operating loan facility plus the financing costs associated with paying its insurance policy monthly. In addition to these sources of other interest the Company also paid interest on a note payable from December 2013 through March.

Liquidity

The Company has a working capital surplus of \$596,259 representing an improvement of \$136,087 during the final quarter and \$688,346 greater than at June 30, 2014. Earlier in the fiscal year the Company settled \$980,384 in obligations, including \$788,737 in current liabilities, through cash payments of \$166,378. At June 30, 2015 the Company had current financial assets of \$802,795 available to settle current financial liabilities of \$599,152. This surplus of \$203,643 represents an improvement of \$134,102 during the quarter. The Company also has access to a \$250,000 bank operating line, which was not drawn upon as of June 30, 2015, to help fund working capital requirements.

The Company utilizes long term debt as a means of financing new equipment acquisitions. In July 2014 the Company obtained a commercial term loan and used the proceeds of that loan to pay out \$200,000 in loans obtained January 2014, from related parties, to finance an equipment purchase.

In addition to satisfying the cost of operations the Company must also address the payment or other settlement of the following amounts as at June 30, 2015:

	Due by June 2016	Due by June 2018	Due by June 2020	Due after June 2020	Total Due
Long-term debt	\$ 39,493	\$ 78,986	\$ 42,783	\$ -	\$ 161,262
Operating leases	<u>95,972</u>	<u>204,620</u>	<u>214,128</u>	<u>80,807</u>	<u>595,527</u>
	<u>\$ 135,465</u>	<u>\$ 283,606</u>	<u>\$ 256,911</u>	<u>\$ 80,807</u>	<u>\$ 756,789</u>

Capital Resources

The Company has a \$250,000 commercial line of credit from which nothing was drawn as at June 30, 2015 and \$25,000 was drawn as at June 30, 2014. The loan bears interest at the prime lending rate plus 2.5%, is due upon demand, and is secured by a general security agreement covering the assets of PEC.

In July 2014 this line of credit was restructured to increase the interest rate from the prime lending rate plus 0.5% and to remove the requirement for term deposit security. The \$250,000 term deposit, previously classified as restricted cash equivalents, became available for general use on July 7, 2014.

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Related Party Transactions

During the final quarter of 2015 a loan payable to 1114377 Ontario Inc. (ö1114377ö) , a company controlled by the spouse of Mr. W. Drzazga, the CEO and a Director of the Company, matured. An option granted to 1114377 at the inception of this loan, to acquire a 24% interest in Permotech Electronics Corporation, also expired during the year.

In July 2014 the Company received \$197,463 from its bank under a 5-year term loan with interest at the TD Bank prime lending rate (currently 2.70%) plus 1.75%. The proceeds were used to retire term loans payable to 1114377 and to Mike Kindy, the Company's CFO, which had been negotiated when commercial financing was not available to the Company. At the inception of the term loans the creditors received 400,000 share purchase warrants with each warrant having an exercise price of \$0.10 and an expiry date of October 31, 2017.

The Company compensates its key management personnel for services rendered. These include salaries and benefits paid to Wojciech Drzazga (CEO) and John Perreault (President), consulting fees paid to Michael D. Kindy (CFO), legal fees paid to a legal firm in which William R. Johnstone (Corporate Secretary) is a partner, Directors' fees, and share-based payments. The Compensation rates are agreed to by the key management personnel and are predicated upon prevailing market rates.

The following balances are due to related parties as at June 30 of each year:

	<u>2015</u>	<u>2014</u>
Loan payable to 1114377 Ontario Inc. at prime +8% ⁽¹⁾	-	46,806
Loan payable to 1114377 Ontario Inc. at 9% ⁽¹⁾	-	150,000
Loan payable to the Company's CFO at 9% ⁽¹⁾	-	50,000
Salaries and benefits payable ⁽²⁾	6,106	3,793
Consulting fees payable ⁽²⁾	83,200	44,800
Legal fees payable ⁽²⁾	1,000	3,129

⁽¹⁾ This is the face value of this obligation. It was reported in the consolidated financial statements at a discounted value included as an element of long-term debt.

⁽²⁾ Reported in the consolidated financial statements as an element of accounts payable and accrued liabilities. Aggregate value of \$90,306 (2014 - \$51,722)

The following expenses have arisen during the years ended June 30 as a result of transactions involving the related parties defined above:

	<u>2015</u>	<u>2014</u>
Salaries and benefits ⁽¹⁾	\$ 267,766	\$ 254,006
Production wages ⁽²⁾	-	3,569
Consulting fees ⁽¹⁾	38,400	40,609
Directors' fees ⁽¹⁾	27,600	35,100
Legal fees ⁽³⁾	24,080	38,053
Interest expense ó long term	<u>7,407</u>	<u>18,150</u>
Cash based expenditures	<u>\$ 365,253</u>	<u>\$ 389,487</u>
Share-based payments	<u>\$ -</u>	<u>\$ 49,705</u>

⁽¹⁾ Reported in the consolidated financial statements as an element of employee and consultant compensation.

⁽²⁾ Reported in the consolidated financial statements as an element of cost of goods sold.

⁽³⁾ Reported in the consolidated financial statements as an element of professional fees.

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Related Party Transactions - continued

The following stock options have been issued to Directors and/or Officers of the Company and were outstanding as at June 30, 2015:

<u>Description</u>	<u>Expiry Date</u>	<u>Number of Common shares</u>
Stock options @ \$0.10 per share	Nov. 2015	275,000
Stock options @ \$0.10 per share	Sept. 2017	130,000
Stock options @ \$0.10 per share	Dec. 2018	500,000

There were 300,000 stock options held by the estate of a former Director, having exercise prices ranging from \$0.10 to \$0.15, which expired April 27, 2015.

Convertible Instruments and Other Securities

The Company has the following securities issued and outstanding:

<u>Share capital</u>	<u>Quantity</u>	<u>Amount</u>
Common shares, June 30, 2014	10,648,696	\$ 22,343,053
Less: paid up capital of preferred shares redeemed	-	(191,646)
Common shares, June 30, 2015 and as at the date of this document	<u>10,648,696</u>	<u>\$ 22,151,406</u>

<u>Preferred shares</u>	<u>Quantity</u>	<u>Amount</u>
Series A preferred shares	166,667	\$ 160,000
Series C preferred shares	288,858	<u>505,501</u>
		665,501
Less: amount accounted for as paid in capital		(191,646)
Liability element of preferred shares at June 30, 2014		473,855
Preferred shares redeemed		<u>(473,855)</u>
Preferred shares as at June 30, 2015 and as at the date of this document		<u>\$ -</u>

In addition to the shares issued and outstanding the Company has issued share purchase warrants and stock options as incentives to various parties. The following list itemizes the common shares that have been reserved to satisfy the conversions and exercise of warrants and options along with the expiry date associated therewith.

<u>Shares reserved</u>	<u>Expiry Date</u>	<u>Number of Common shares</u>
Common shares to be issued for Class A shares ⁽¹⁾		8,246
Stock options @ \$0.10 per share	Nov. 2015	275,000
Warrants @ \$0.10 per share	Feb. 2016	1,100,000
Warrants @ \$0.10 per share	Mar. 2016	900,000
Stock options @ \$0.10 per share	Sept. 2017	130,000
Warrants @ \$0.10 per share	Oct. 2017	400,000
Stock options @ \$0.10 per share	Mar. 2018	<u>500,000</u>
Shares reserved as at June 30, 2015 and as at the date of this document		<u>3,313,246</u>

⁽¹⁾ In the 2013 fiscal year the Company's shareholders approved the issuance of 99,454 common shares in exchange for 100% of the Class A Special Shares outstanding. 91,208 common shares have been issued, representing the entitlement of the identifiable Class A shareholders. 8,246 common shares have been reserved to be issued if and when the remaining Class A shareholders identify themselves to the Company.

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Convertible Instruments and Other Securities - continued

Fully diluted position

Shares issued	10,648,696
Shares reserved	<u>3,313,246</u>
Fully diluted position as at June 30, 2015 and as at the date of this document	<u>13,961,942</u>

Additional disclosures relative to stock options are as follows:

	Common Shares <u>Under Option</u>	Number of <u>Options Vested</u>	Exercise <u>Price</u>	<u>Expiry Date</u>
Granted Nov. 30, 2010	275,000 ⁽¹⁾	275,000	\$ 0.10	Nov. 30, 2015
Granted Sept. 14, 2012	130,000 ⁽¹⁾	130,000	\$ 0.10	Sept. 14, 2017
Granted December 31, 2013	500,000 ⁽¹⁾	500,000	\$ 0.10	Dec. 31, 2018

All stock options are held by Directors and Officers of the Company and have vested. The Company has no ability to cause these options to be exercised.

	Common Shares <u>Under Option</u>	Weighted Average <u>Price/Option</u>	Weighted Average <u>Expiry Date</u>
Balance, June 30, 2014	1,205,000	\$ 0.108	Mar. 28, 2017
Expired April 27, 2015	<u>(300,000)</u>	\$ 0.132	Apr 27, 2015
Balance, June 30, 2015 and as at the date of this document	<u>905,000</u>	\$ 0.100	Nov. 15, 2017

Additional disclosures relative to share purchase warrants are as follows:

	Number of <u>Warrants</u>	Value of <u>Warrants</u>	Exercise <u>Price</u>	<u>Expiry Date</u>
Issued Mar. 24, 2011	900,000	\$ 38,818	\$ 0.10	Mar. 24, 2016
Issued Feb. 4, 2013	1,100,000	37,859	\$ 0.10	Feb. 4, 2016
Issued Jan. 10, 2014	400,000	<u>4,219</u>	\$ 0.10	Oct. 31, 2017
		<u>\$ 80,896</u>		

	Number of <u>Warrants</u>	Weighted Average <u>Price/Warrant</u>	Weighted Average <u>Expiry Date</u>
Balance, June 30, 2014, June 30, 2015 and as at the date of this document	<u>2,400,000</u>	\$ 0.10	June 7, 2016

Changes in Accounting Policy

The accounting policies followed by the Company are established in accordance with International Financial Reporting Standards (IFRS) and once policies are established they will not, as a matter of policy, be revised unless IFRS changes. There were no changes in accounting policy during the current period.

Accounting Standards Effective For Future Periods

IFRS 9, *Financial Instruments*: effective for annual periods beginning on or after January 1, 2018, with early adoption permitted, establishes principles for the financial reporting of financial assets and financial liabilities that will present relevant and useful information to users of the financial statements for their assessment of the amounts, timing and uncertainty of future cash flows. Management anticipates that this standard will be adopted in the Company's financial statements for the year beginning July 1, 2018 and has not yet considered the potential impact of its adoption.

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Accounting Standards Effective For Future Periods - continued

IFRS 15, *Revenue from Contracts with Customers*: effective for annual periods beginning on or after January 1, 2018, with early adoption permitted, replaces existing revenue standards and interpretations with a single standard and provides additional guidance on revenue recognition for contracts with customers. Management anticipates that this standard will be adopted in the Company's financial statements for the year beginning July 1, 2018 and has not yet considered the potential impact of its adoption.

Financial Instruments

The Company's financial instruments are comprised of the following:

Financial assets:

Cash

Restricted cash equivalents

Accounts receivable

Classification

Fair value through profit and loss

Fair value through profit and loss

Loans and receivables

Financial liabilities:

Bank operating loan

Accounts payable and accrued liabilities

Customer deposits

Long-term debt

Classification

Other financial liabilities

Other financial liabilities

Other financial liabilities

Other financial liabilities

Fair value through profit and loss:

Financial assets are designated as fair value through profit and loss if they were acquired principally for the purpose of selling in the short term. Fair value through profit and loss assets are recognized and carried at their fair value.

Loans and receivables:

Loans and receivables are financial assets with fixed or determinable payments that are not quoted in an active market. Such assets are initially recognized at fair value plus any directly attributable transaction costs. Subsequent to initial recognition loans and receivables are measured at amortized cost using the effective interest method, less any impairment losses.

Other financial liabilities:

Other financial liabilities are recognized initially at fair value net of any directly attributable transaction costs. Subsequent to initial recognition these financial liabilities are measured at amortized cost using the effective interest method. The effective interest method is a method of calculating the amortized cost of a financial instrument and of allocating interest and any transaction costs over the relevant period. The effective interest rate is the rate that exactly discounts estimated future cash payments through the expected life of the financial instrument to the net carrying amount on initial recognition. Other financial liabilities are de-recognized when the obligations are discharged, cancelled or expired.

Impairment of financial assets:

Financial assets are assessed for indicators of impairment at the end of each reporting period. Financial assets are impaired when there is objective evidence that, as a result of one or more events that occurred after the initial recognition of the financial assets, the estimated future cash flows of the assets have been negatively impacted.

Evidence of impairment could include:

- significant financial difficulty of the issuer or counterparty; or
- default or delinquency in interest or principal payments; or
- it becoming probable that the borrower will enter bankruptcy or financial re-organization.

The carrying amount of financial assets is reduced by any impairment loss directly for all financial assets with the exception of accounts receivable, where the carrying amount is reduced through the use of an allowance account. When an account receivable is considered uncollectible, it is written off against the allowance account. Subsequent recoveries of amounts previously written off are credited against the allowance account. Changes in the carrying amount of the allowance account are recognized in income for the period.

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Financial instruments - continued

Impairment of financial assets - continued:

If, in a subsequent period, the amount of the impairment loss decreases and the decrease can be related objectively to an event occurring after the impairment was recognized, the previously recognized impairment loss is reversed through income for the period to the extent that the carrying amount of the asset at the date the impairment is reversed does not exceed what the amortized cost would have been had the impairment not been recognized.

Financial instruments recorded at fair value:

Financial instruments recorded at fair value on the consolidated statement of financial position are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

- Level 1 valuation based on quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2 valuation techniques based on inputs other than quoted prices included in Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices);
- Level 3 valuation techniques using inputs for the asset or liability that are not based on observable market data (unobservable inputs).

As of June 30, 2015 and 2014 cash and restricted cash equivalents are measured at fair value and are classified within Level 1 of the fair value hierarchy.

Financial instruments recorded at amortized cost:

Financial instruments recorded at amortized cost on the consolidated statement of financial position are amortized using the market rates of interest prevailing at the inception of the financial instrument applied to expected future cash flows. The amortized cost is recomputed in the event that the underlying terms, and therefore the expected future cash flows, of the financial instrument are altered with any change in the amortized cost being charged to income of the period. Dividends payable and preferred shares are each carried at historical cost as the future cash flows cannot be reasonably estimated.

Risk Factors

Events seemingly unrelated to the Company, or to its industry, may adversely affect its finances or operations in ways that are hard to predict or defend against. For example, credit contraction in financial markets may hamper the Company's ability to access credit when needed or rapid changes in foreign exchange rates may adversely affect its financial results. Finally, a reduction in credit, combined with reduced economic activity, may adversely affect businesses and industries that constitute a significant portion of the Company's customer base. As a result, these customers may need to reduce their purchases, or the Company may experience greater difficulty in collecting amounts due from them. Any of these events, or others caused by uncertainty in world financial markets, may have a material adverse effect on the Company's business, operating results, and financial condition.

In addition to the foregoing, the Company is exposed to credit risk, concentration of credit risk, liquidity risk, and currency risk. The Company's primary risk management objective is to protect earnings and cash flow and, ultimately, shareholder value. Risk management strategies, as discussed below, are designed and implemented to ensure that the Company's risks and the related exposure are consistent with its business objectives and risk tolerance. There have been no changes to the risk management strategies during the current year.

Credit risk

Credit risk is the risk that one party to a financial instrument will fail to discharge an obligation and cause the other party to incur a financial loss. The Company's primary exposure to credit risk is in its accounts receivable. In an effort to mitigate this risk, management actively manages and monitors its receivables and obtains pre-payments where warranted. Bad debt experience has not been significant and it has been determined that no allowance is required as all amounts outstanding are considered collectible.

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Risk Factors - continued

Concentration of credit risk

Concentration of credit risk arises when one or more customers, defined as a major customer, individually account for 10% or more of the Company's revenues during a reporting period. During the current year the Company had major customers which represented 13% and 12% of total revenues. In the prior year one major customer accounted for 25% of revenues. Amounts due from major customers represented 13% of accounts receivable at June 30, 2015 (2014 - 9%). The loss of a major customer, or significant curtailment of purchases by such customer, could have a material adverse effect on the Company's results of operations and financial condition. The Company monitors the relationship with all customers closely and ensures that every customer is subject to the same risk management criteria.

Market risks

The Company is exposed to interest rate risk due to obligations that have floating interest rates as well as currency risk related to cash, accounts receivable and accounts payable denominated in US dollars. Market risks give rise to the potential for future cash flows to fluctuate because of changes in interest rates or foreign exchange rates. Market risks are closely monitored and attempts are made to match foreign cash inflows and outflows. During the current fiscal year the Company has reported a foreign exchange gain of \$5,783 (2014 a gain of \$3,581).

Sensitivity to market risks

At June 30, 2015 the Company had \$161,262 (2014 a Nil) which bears interest at the TD Bank prime lending rate plus 1.75%. A 1% increase in the TD Bank prime lending rate as at the financial reporting date would result in additional interest expense of \$1,432 over the next 12 month period.

At June 30, 2015 the Company had US\$129,966 (2014 a US\$99,330) included in accounts receivable. A 5% increase in the value of the Canadian dollar relative to the US dollar would result in a reduction of \$1,658 in future cash inflow.

At June 30, 2015 the Company had US\$128,894 (2014 a US\$233,439) included in accounts payable. A 5% decrease in the value of the Canadian dollar relative to the US dollar would result in an increase of \$1,645 in future cash outflow.

At June 30, 2015 the Company had US\$20,825 (2014 a US\$38,607) included in cash. A 5% increase in the value of the Canadian dollar relative to the US dollar would result in a reduction of \$266 in carrying value.

Based upon observations of recent market trends management believes that each of these outcomes is possible but most likely exceed the Company's immediate market risk exposures.

Forward-looking Information

Certain statements in this MD&A may constitute "forward-looking" statements which involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company and its subsidiary, or the industry in which they operate, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. When used in this report, the words "estimate", "believe", "anticipate", "intend", "expect", "plan", "may", "should", "will", the negative thereof or other variations thereon or comparable terminology are intended to identify forward-looking statements. Such forward-looking statements reflect the current expectations of the management of the Company with respect to future events based on currently available information and are subject to risks and uncertainties that could cause actual results, performance or achievements to differ materially from those expressed or implied by those forward-looking statements, such as reduced funding, long sales cycles, currency and interest rate fluctuations, increased competition and general economic and market factors and including the risk factors summarized below under the heading "Risk Factors". New risk factors may arise from time to time and it is not possible for management of the Company to predict all of those risk factors or the extent to which any factor or combination of factors may cause actual results, performance or achievements of the Company to be materially different from those expressed or implied in such forward-looking statements. Given these risks and uncertainties, investors should not place undue reliance on forward-looking statements as a prediction of actual results.

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Forward-looking Information - continued

Although the forward-looking statements contained in this MD&A are based upon what management believes to be reasonable assumptions, the Company cannot assure investors that actual results will be consistent with these forward-looking statements. The forward-looking statements contained in this MD&A speak only as of the date hereof. The Company does not undertake or assume any obligation to release publicly any revisions to these forward-looking statements to reflect events or circumstances after the date hereof or to reflect the occurrence of unanticipated events, except as required by law.