

Interim Condensed Consolidated Financial Statements of

NEW FLYER INDUSTRIES INC.

October 2, 2016

(Unaudited)

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NEW FLYER INDUSTRIES INC.

INTERIM CONDENSED CONSOLIDATED STATEMENTS OF NET EARNINGS AND TOTAL COMPREHENSIVE INCOME

For the period ended October 2, 2016

(unaudited, in thousands of U.S. dollars except per share figures)

	13-Weeks Ended October 2, 2016	13-Weeks Ended September 27, 2015	40-Weeks Ended October 2, 2016	39-Weeks Ended September 27, 2015
Revenue (note 12)	\$ 511,483	\$ 364,683	\$ 1,651,646	\$ 1,119,996
Cost of sales (note 4)	423,137	315,349	1,359,450	982,604
Gross profit	88,346	49,334	292,196	137,392
Sales, general and administration costs and other operating expenses	42,673	23,723	140,010	68,583
Foreign exchange (gain) loss	(960)	628	(3,118)	(139)
Earnings from operations	46,633	24,983	155,304	68,948
Unrealized foreign exchange loss on non-current monetary items	1,365	984	401	2,069
Earnings before interest and income taxes	45,268	23,999	154,903	66,879
Finance costs				
Interest on long-term debt	4,094	2,161	14,363	6,695
Accretion in carrying value of long-term debt	599	609	2,030	1,791
Other interest and bank charges	1,215	590	4,940	1,918
Fair value adjustment on interest rate swap	(3,010)	128	3,232	305
	2,898	3,488	24,565	10,709
Earnings before income tax expense	42,370	20,511	130,338	56,170
Income tax expense (note 5)				
Current income taxes	14,702	14,380	44,647	40,638
Deferred income tax (recovered) expense	1,666	(10,428)	2,355	(24,252)
	16,368	3,952	47,002	16,386
Net earnings for the period	\$ 26,002	\$ 16,559	\$ 83,336	\$ 39,784
Other comprehensive income (loss)				
Actuarial gain (loss) on defined benefit pension plan - this item will not be reclassified subsequently to profit or loss (note 15)	2,701	—	(5,059)	356
Total comprehensive income for the period	\$ 28,703	\$ 16,559	\$ 78,277	\$ 40,140
Net earnings per share (basic) (note 9)	\$ 0.43	\$ 0.30	\$ 1.42	\$ 0.72
Net earnings per share (diluted) (note 9)	\$ 0.42	\$ 0.29	\$ 1.40	\$ 0.71

The accompanying notes are an integral part of the unaudited interim condensed consolidated financial statements.

NEW FLYER INDUSTRIES INC.

INTERIM CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION

As at October 2, 2016

(unaudited, in thousands of U.S. dollars)

	October 2, 2016	December 27, 2015
Assets		
Current		
Cash	\$ —	\$ 24,880
Accounts receivable (note 3,11e)	314,804	317,096
Income tax receivable	8,480	4,723
Inventories (note 4)	417,113	353,756
Derivative financial instruments (note 11b,c)	1,978	—
Prepaid expenses and deposits	14,042	6,560
	756,417	707,015
Property, plant and equipment	127,839	132,396
Deferred tax assets (note 5)	10,080	12,145
Goodwill and intangible assets	904,308	920,666
	\$ 1,798,644	\$ 1,772,222
Liabilities		
Current		
Bank indebtedness	\$ 467	\$ —
Accounts payable and accrued liabilities	334,324	273,069
Income taxes payable	15,164	21,470
Derivative financial instruments	—	163
Current portion of deferred revenue	33,261	31,703
Current portion of provision for warranty costs (note 14)	26,490	22,246
Current portion of long-term debt (note 6)	76,000	180,060
Current portion of deferred compensation obligation	11,544	9,783
Current portion of convertible debentures (note 7)	15,682	—
Current portion of obligations under finance leases	5,092	3,219
	518,024	541,713
Accrued benefit liability (note 15)	30,746	26,251
Obligations under finance leases	4,719	6,673
Deferred compensation obligation	9,695	8,212
Deferred revenue	9,361	11,969
Other long-term liabilities	16,396	14,377
Provision for warranty costs (note 14)	35,777	29,650
Deferred tax liabilities (note 5)	109,335	111,278
Long-term debt (note 6)	476,851	475,753
Convertible debentures (note 7)	—	61,135
Derivative financial instruments (note 11b,c)	4,583	1,351
	1,215,487	1,288,362
Commitments and contingencies (note 13)		
Shareholders' equity		
Share capital (note 8)	645,195	591,758
Stock option reserve	3,333	2,832
Equity component of convertible debentures (note 7)	948	3,791
Accumulated other comprehensive loss	(11,379)	(6,320)
Deficit	(54,940)	(108,201)
	583,157	483,860
	\$ 1,798,644	\$ 1,772,222

The accompanying notes are an integral part of the unaudited interim condensed consolidated financial statements.

Authorized for issue by the board of directors on November 10, 2016.

NEW FLYER INDUSTRIES INC.

INTERIM CONDENSED CONSOLIDATED STATEMENT OF CHANGES IN EQUITY

For the period ended October 2, 2016

(unaudited, in thousands of U.S. dollars)

	Share Capital	Equity Component of Convertible Debentures (note 7)	Stock Option and Restricted Share Unit Reserve	Accumulated Other Comprehensive Loss	Deficit	Total Shareholders' Equity
December 28, 2014	\$ 589,586	\$ 3,820	\$ 1,046	\$ (6,049)	\$ (135,781)	\$ 452,622
Net earnings	—	—	—	—	39,784	39,784
Other comprehensive income	—	—	—	356	—	356
Dividends declared on common shares	—	—	—	—	(19,901)	(19,901)
Share-based compensation, net of deferred income taxes	—	—	1,186	—	—	1,186
Shares issued	73	—	(73)	—	—	—
Conversion of debentures to common shares	83	(5)	—	—	—	78
September 27, 2015	\$ 589,742	\$ 3,815	\$ 2,159	\$ (5,693)	\$ (115,898)	\$ 474,125
Net earnings	—	—	—	—	14,110	14,110
Other comprehensive loss	—	—	—	(627)	—	(627)
Dividends declared on common shares	—	—	—	—	(6,413)	(6,413)
Share-based compensation, net of deferred income taxes	—	—	920	—	—	920
Shares issued	1,600	—	(247)	—	—	1,353
Conversion of debentures to common shares	416	(24)	—	—	—	392
December 27, 2015	\$ 591,758	\$ 3,791	\$ 2,832	\$ (6,320)	\$ (108,201)	\$ 483,860
Net earnings	—	—	—	—	83,336	83,336
Other comprehensive loss	—	—	—	(5,059)	—	(5,059)
Dividends declared on common shares	—	—	—	—	(30,075)	(30,075)
Deferred tax assets recognized as a result of historical share redemptions	301	—	—	—	—	301
Shares issued	3,909	—	(602)	—	—	3,307
Share-based compensation, net of income taxes	—	—	1,103	—	—	1,103
Conversion of debentures to common shares	49,227	(2,843)	—	—	—	46,384
October 2, 2016	\$ 645,195	\$ 948	\$ 3,333	\$ (11,379)	\$ (54,940)	\$ 583,157

The accompanying notes are an integral part of the unaudited interim condensed consolidated financial statements.

NEW FLYER INDUSTRIES INC.

INTERIM CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS

For the period ended October 2, 2016

(unaudited, in thousands of U.S. dollars)

	13-Weeks Ended October 2, 2016	13-Weeks Ended September 27, 2015	40-Weeks Ended October 2, 2016	39-Weeks Ended September 27, 2015
Cash generated from (used in)				
Operating activities				
Net earnings for the period	\$ 26,002	\$ 16,559	\$ 83,336	\$ 39,784
Income tax expense	16,368	3,952	47,002	16,386
Depreciation of plant and equipment	8,046	4,652	20,976	13,323
Amortization of intangible assets	7,459	5,369	23,599	16,050
Share-based compensation	281	272	990	795
Finance costs recognized in profit or loss	2,898	3,488	24,565	10,709
Fair value adjustment for total return swap	258	—	(1,741)	—
Unrealized foreign exchange loss on non-current monetary items	1,365	984	401	2,069
Foreign exchange loss (gain) on cash held in foreign currency	207	738	(542)	961
Realized investment tax credits	—	—	—	169
Defined benefit expense	1,602	821	5,364	6,068
Defined benefit funding	(4,078)	(793)	(8,011)	(2,358)
Cash generated from operating activities before non-cash working capital items and interest and income taxes paid	60,408	36,042	195,939	103,956
Changes in non-cash working capital items (note 10)	(1,720)	(6,471)	1,226	(44,182)
Cash generated from operating activities before interest and income taxes paid	58,688	29,571	197,165	59,774
Interest paid	(5,380)	(3,811)	(21,193)	(9,609)
Income taxes paid	(23,819)	(14,143)	(60,877)	(32,600)
Net cash generated from operating activities	29,489	11,617	115,095	17,565
Financing activities				
Repayment of obligations under finance leases	(859)	(501)	(2,342)	(1,407)
Share issuance	1,095	—	3,307	—
(Repayment) proceeds from issuance of long-term debt	(15,000)	(4,000)	(104,060)	4,000
Repayment of other long-term liabilities	—	—	(2,252)	(1,923)
Dividends paid	(11,003)	(6,816)	(21,116)	(20,074)
Net cash used in financing activities	(25,767)	(11,317)	(126,463)	(19,404)
Investing activities				
Acquisition of intangible assets	—	(15)	(176)	(111)
Acquisition of property, plant and equipment	(5,673)	(1,849)	(14,345)	(8,031)
Net cash used in investing activities	(5,673)	(1,864)	(14,521)	(8,142)
Effect of foreign exchange rate on cash	(207)	(738)	542	(961)
Decrease in cash	(2,158)	(2,302)	(25,347)	(10,942)
Cash — beginning of period	1,691	8,816	24,880	17,456
(Bank indebtedness) cash — end of period	\$ (467)	\$ 6,514	\$ (467)	\$ 6,514

The accompanying notes are an integral part of the unaudited interim condensed consolidated financial statements.

NEW FLYER INDUSTRIES INC.
NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS
For the period ended October 2, 2016
(unaudited, in thousands of U.S. dollars)

1. CORPORATE INFORMATION

New Flyer Industries Inc. ("NFI" or the "Company") was incorporated on June 16, 2005 under the laws of the Province of Ontario. The Company is the largest transit bus and motor coach manufacturer and parts distributor in North America with fabrication, manufacturing, distribution and service centers in Canada and the United States and employs approximately 5,000 team members. The Company also operates North America's most comprehensive aftermarket parts organization providing support for all types of transit buses and motor coaches.

The Company's common shares (the "Shares") are listed on the Toronto Stock Exchange ("TSX") under the symbol "NFI" and the Company's 6.25% convertible unsecured subordinated debentures (the "Debentures") are listed on the TSX under the symbol "NFI.DB.U".

These unaudited interim condensed consolidated financial statements (the "Statements") were approved by the Company's board of directors on November 10, 2016.

1.1 Acquisition of Motor Coach Industries

On December 18, 2015 (the "Acquisition Date"), New Flyer Holdings, Inc., acquired 100% of the voting equity interest in Motor Coach Industries International, Inc. ("MCI") from an affiliate of KPS Capital Partners, L.P. for cash consideration of approximately \$468.7 million, which includes the final working capital adjustment. The purchase price was funded by the proceeds from the Company's new senior secured credit facility. MCI is North America's leading motor coach manufacturer and parts and service supplier. The acquisition has been accounted for using the acquisition method. The fair values of the identifiable assets and liabilities acquired have been based on management's best estimates and valuation techniques as at the Acquisition Date. The Company adjusted the preliminary purchase price allocation as set out below to account for information that was not previously available. This included the addition of the intangible for backlog of sales orders, a detailed valuation of deferred revenue, completion of the valuation studies on property, plant and equipment and finalization of the 2015 U.S corporate tax returns. The adjustments recorded resulted in an increase to goodwill of \$3,693 from the amount originally reported.

	Original	Previous adjustments	Current adjustments	Revised
Cash purchase price	\$ 468,672	\$ —	\$ —	\$ 468,672
Net assets acquired				
Accounts receivable	62,571	—	1,582	64,153
Inventories	152,684	—	—	152,684
Prepaid expenses and deposits	2,866	—	—	2,866
Property, plant and equipment	69,848	(4,717)	—	65,131
Deferred tax assets	19,652	—	1,599	21,251
Accounts payable and accrued liabilities	(92,285)	—	(4,417)	(96,702)
Deferred revenue	(15,160)	1,158	—	(14,002)
Provision for warranties	(6,520)	—	—	(6,520)
Accrued benefit liability	(21,717)	—	—	(21,717)
Other long-term liabilities	(8,213)	—	—	(8,213)
Deferred tax liabilities (note 5)	(93,291)	(1,270)	(828)	(95,389)
Net tangible assets acquired	70,435	(4,829)	(2,064)	63,542
Trade names	62,000	—	—	62,000
Patent and licenses	11,000	—	—	11,000
Customer relationships	157,000	—	—	157,000
Backlog of sales orders	—	3,200	—	3,200
Identifiable intangible assets acquired	230,000	3,200	—	233,200
Goodwill acquired	\$ 168,237	\$ 1,629	\$ 2,064	\$ 171,930

The goodwill acquired is largely attributable to the synergies and economies of scale expected from the combined businesses of NFI and MCI. This goodwill is not deductible for tax purposes. The estimated purchase price allocation remains subject to adjustments that could arise as a result of new information that would impact the determination of fair value of the assets acquired and liabilities assumed. There is continued analysis to be undertaken which will complete the validation of the deferred tax valuation assumptions.

NEW FLYER INDUSTRIES INC.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

October 2, 2016

(unaudited, in thousands of U.S. dollars except per share figures)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these Statements are the same as those applied by the Company in its consolidated financial statements as at and for the 52-week period ended December 27, 2015 ("Fiscal 2015"). These Statements should be read in conjunction with the Company's consolidated financial statements for Fiscal 2015.

2.1 Statement of Compliance

The Statements are unaudited and have been prepared in accordance with IAS 34 Interim Financial Reporting and do not include all the information required for full annual financial statements.

2.2 Basis of preparation

The Statements were prepared on a going concern basis in accordance with International Financial Reporting Standards ("IFRS") which requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, revenue and expenses. Actual results may differ from these estimates.

In preparing these Statements, the significant judgments made by management in applying the Company's accounting policies and the key sources of estimation uncertainty were the same as those applied by the Company in its consolidated financial statements for Fiscal 2015.

2.3 Principles of consolidation

The Statements include the accounts of all of the Company's subsidiaries: New Flyer Holdings, Inc., Transit Holdings, Inc., New Flyer of America Inc., New Flyer Industries Canada ULC, 1176846 Alberta ULC, TCB Enterprises, LLC, The Aftermarket Parts Company, LLC, Transit Acquisition, LLC, Transit Finco, Inc, Carriage Acquisition, LLC, Parts Convergence, LLC, New MCI Holdings, Inc., MCII Holdings, Inc., MCI, Motor Coach Industries, Inc., MCI Sales and Service, Inc., MCI Service Parts, Inc., MCIL Holdings, Ltd., Motor Coach Industries Limited and Frank Fair Industries Ltd.

The Company and Alexander Dennis Limited have a contractual joint arrangement for the commercialization of MiDi[®], a mid-sized bus, in the medium-duty transit markets in Canada and the United States. The Company is responsible for sales, marketing, manufacturing and aftermarket support with Alexander Dennis Limited performing design, engineering, test and prototype development activities. The Company recognizes in relation to its interest in a joint operation: its assets, including its share of any assets held jointly; its liabilities, including its share of any liabilities incurred jointly; its revenue from the sale of its share of the output arising from the joint operation; its share of the revenue from the sale of the output by the joint operation; and its expenses, including its share of any expenses incurred jointly.

2.4 Standards issued but not yet adopted

IFRS 9 - Financial Instruments:

The International Accounting Standards Board ("IASB") issued IFRS 9 to replace IAS 39, which will become effective January 1, 2018 and early adoption is permitted. IFRS 9 - Financial Instruments introduces new requirements for the classification and measurement of financial instruments. Management is in the process of reviewing the standard to determine the impact on the Company's financial statements.

IFRS 15 - Revenue from Contracts with Customers:

The IASB issued IFRS 15 - Revenue from Contracts with Customers, which will become effective January 1, 2018 and early adoption is permitted. Under this standard, revenue will be recognized over time in a manner that best reflects the Company's performance, or at a point in time, when control of the good or service is transferred to customers. Management is in the process of reviewing the standard to determine the impact on the Company's financial statements.

IFRS 16 - Leases:

IFRS 16 eliminates the distinction between operating and finance leases and requires most leases to be recorded on the balance sheet for lessees under a single model unless the lease term is twelve months or less or the underlying asset has a low value. Lessor accounting remains largely unchanged and the distinction between operating and finance leases is retained. The standard has an effective date for annual periods beginning on or after January 1, 2019 with an early adoption permitted if IFRS 15 - Revenue from Contracts with Customers has also been applied. Management is in the process of reviewing the standard to determine the impact on the Company's financial statements.

NEW FLYER INDUSTRIES INC.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

October 2, 2016

(unaudited, in thousands of U.S. dollars except per share figures)

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)

2.5 Fiscal periods

The Company's 2016 fiscal period is divided in quarters as follows:

	Period from December 28, 2015 to January 1, 2017 (“Fiscal 2016”)		Period from December 29, 2014 to December 27, 2015 (“Fiscal 2015”)	
	Period End Date	# of Weeks	Period End Date	# of Weeks
Quarter 1	April 3, 2016	14	March 29, 2015	13
Quarter 2	July 3, 2016	13	June 28, 2015	13
Quarter 3	October 2, 2016	13	September 27, 2015	13
Quarter 4	January 1, 2017	13	December 27, 2015	13
Fiscal year	January 1, 2017	53	December 27, 2015	52

3. ACCOUNTS RECEIVABLE

	October 2, 2016		December 27, 2015	
Trade	\$	284,646	\$	284,118
Other		30,158		32,978
	\$	314,804	\$	317,096

4. INVENTORIES

	October 2, 2016		December 27, 2015	
Raw materials	\$	168,960	\$	152,405
Work in process		119,054		138,902
Finished goods		129,099		62,449
	\$	417,113	\$	353,756

	13-Weeks Ended October 2, 2016		13-Weeks Ended September 27, 2015		40-Weeks Ended October 2, 2016		39-Weeks Ended September 27, 2015	
Cost of inventories recognized as expense and included in cost of sales	\$	402,333	\$	304,709	\$	1,296,221	\$	938,410
Write-down of inventory to net realizable value in cost of sales		1,112		408		3,825		1,563
Reversal of a previous write-down in inventory		—		—		136		181

NEW FLYER INDUSTRIES INC.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

October 2, 2016

(unaudited, in thousands of U.S. dollars except per share figures)

5. DEFERRED TAXES AND INCOME TAX EXPENSE

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset and when the deferred income tax assets and liabilities relate to income taxes levied by the same taxation authority on either the taxable entity or different taxable entities where there is an intention to settle the balances on a net basis. The offset amounts by tax jurisdiction presented on the consolidated statements of financial position are as follows:

	October 2, 2016	December 27, 2015
As presented on statements of financial position:		
Deferred tax assets	\$ 10,080	\$ 12,145
Deferred tax liabilities	(109,335)	(111,278)
	\$ (99,255)	\$ (99,133)

The gross movement on the deferred income tax account is as follows:

	13-Weeks Ended October 2, 2016	13-Weeks Ended September 27, 2015	40-Weeks Ended October 2, 2016	39-Weeks Ended September 27, 2015
Beginning of period	\$ (96,617)	\$ (33,911)	\$ (99,133)	\$ (46,230)
Assumed on December 18, 2015 relating to MCI acquisition (note 1.1)	771	—	(499)	—
Exchange differences	(166)	(1,794)	264	(3,033)
Tax recorded through net earnings	(1,666)	10,430	(2,355)	24,254
Tax recorded through other comprehensive loss	(1,096)	—	2,724	(197)
Benefit of loss carry forward and share issuance costs recognized against income taxes payable	(59)	(87)	(240)	(275)
Tax recorded through equity	(422)	272	(16)	391
End of period	\$ (99,255)	\$ (25,090)	\$ (99,255)	\$ (25,090)

The movement in deferred income tax assets and liabilities during the period, without taking into consideration the offsetting of balances within the same tax jurisdiction, is as follows:

Deferred tax liabilities	Property Plant and Equipment	Goodwill and Intangibles	Unrealized Foreign Exchange	Other	Total
December 27, 2015	\$ (6,917)	\$ (183,695)	\$ —	\$ (4,558)	\$ (195,170)
Assumed on December 18, 2015 relating to MCI acquisition	(583)	(1,192)	—	—	(1,775)
Tax recorded through net earnings	(533)	6,984	(4,641)	(302)	1,508
October 2, 2016	\$ (8,033)	\$ (177,903)	\$ (4,641)	\$ (4,860)	\$ (195,437)

Deferred tax assets	Unrealized Foreign Exchange	Tax Credits	Provisions	Property Plant and Equipment	Pension	Deferred Financing Costs and Interest	Other	Total
December 27, 2015	\$ 5,712	\$ 10,340	\$ 28,790	\$ 6,813	\$ 9,118	\$ 3,041	\$ 32,223	\$ 96,037
Assumed on December 18, 2015 relating to MCI acquisition	—	(643)	195	—	(36)	2,319	(559)	1,276
Tax recovered (charged) through net earnings	(5,729)	(4,281)	6,136	(156)	(247)	(2,598)	3,019	(3,863)
Tax recorded through other comprehensive loss	—	—	—	—	2,724	—	—	2,724
Benefit of loss carry forward and share issuance costs recognized against income taxes payable	—	—	—	—	—	(240)	—	(240)
Exchange differences	17	—	88	21	28	9	94	264
Tax recorded through equity	—	—	—	—	—	301	(317)	(16)
October 2, 2016	\$ —	\$ 5,416	\$ 35,209	\$ 6,678	\$ 11,587	\$ 2,832	\$ 34,460	\$ 96,182

NEW FLYER INDUSTRIES INC.

NOTES TO INTERIM CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

October 2, 2016

(unaudited, in thousands of U.S. dollars except per share figures)

5. DEFERRED TAXES AND INCOME TAX EXPENSE (Continued)

The reconciliation of income tax computed at the U.S. statutory rate to income tax expense is as follows:

	13-Weeks Ended October 2, 2016	13-Weeks Ended September 27, 2015	40-Weeks Ended October 2, 2016	39-Weeks Ended September 27, 2015
Earnings before income tax expense	\$ 42,370	\$ 20,511	\$ 130,338	\$ 56,170
Tax calculated using a 35% U.S. tax rate	14,830	7,179	45,619	19,659
Tax effect of:				
Withholding and other taxes	315	302	222	779
Non-taxable income	(2,601)	(1,066)	(9,124)	(2,012)
Rate differential on income taxed at other than U.S. statutory rate	(552)	(205)	(897)	(672)
Revision of tax estimate	1,200	(1,295)	1,200	(1,295)
Foreign exchange impact	3,380	(1,409)	6,346	(1,732)
State taxes	549	998	3,940	2,245
Other	(753)	(552)	(304)	(586)
Income tax expense for the period	\$ 16,368	\$ 3,952	\$ 47,002	\$ 16,386

Income tax expense reported for the period is an estimate reflecting the Company's anticipated effective tax rate for Fiscal 2016.

Certain of MCI's Canadian income tax returns for the 2005 through 2010 taxation years are under review by Canada Revenue Agency ("CRA") with respect to transfer pricing policies applied for those years. MCI has received Notices of Reassessment from the CRA for the 2005-2007 taxation years, with respect to the reallocation of income to the Canadian operations from the U.S. operations in relation to splitting consolidated profit between the two jurisdictions. The basis of allocating income to Canada was based on a CRA proposed transfer pricing methodology which differed from the transfer pricing approach followed by MCI. MCI has filed Competent Authority notifications with both the CRA and the Internal Revenue Service to allow for treaty benefits to remain open. MCI has also filed requests for Competent Authority assistance in Canada for the 2005-2007 years. The Company has recorded a reasonable estimate for the tax liability associated with this matter in the income taxes payable account recorded in the interim condensed consolidated statements of financial position. An equal and offsetting indemnity amount receivable from the previous owner of MCI has also been recorded in the interim condensed consolidated statements of financial position. The amount of the tax exposure is uncertain and could significantly increase or decrease with respect to this transfer pricing audit, however, the amount of such change cannot be reasonably estimated by management given the stage of the review. If the amount of the tax exposure increases materially, the indemnity may not be sufficient to offset it fully.

6. LONG-TERM DEBT

	Face Value	Unamortized Transaction Costs	Net Book Value October 2, 2016	Net Book Value December 27, 2015
Term Credit Facility	\$ 482,000	\$ 5,149	\$ 476,851	\$ 475,753
Revolving Credit Facility ("Revolver")	76,000	—	76,000	180,060
	558,000	5,149	552,851	655,813
Less: current portion of long-term debt	76,000	—	76,000	180,060
	\$ 482,000	\$ 5,149	\$ 476,851	\$ 475,753

On December 18, 2015, the Company entered into its fifth amended and restated credit agreement (the "Credit Facility") which has a total borrowing limit of \$825.0 million. The term facility (the "Term Credit Facility") and the Revolver mature on December 18, 2019. Under the Credit Facility the borrowing limit of the Revolver is \$343.0 million to support working capital fluctuations. The Revolver includes a \$55.0 million letter of credit sub-facility, of which \$10.9 million of outstanding letters of credit were drawn at October 2, 2016. Under the Credit Facility the borrowing limit of the Term Credit Facility is \$482.0 million. The Credit Facility also includes an accordion feature of \$75.0 million.

Loans under the Term Credit Facility bear interest at a rate equal to LIBOR or a U.S. base rate for loans denominated in U.S. dollars and a Canadian prime rate or bankers' acceptance rate for loans denominated in Canadian dollars, plus an applicable margin to those rates. The obligations in respect of the Credit Facility are secured by: (a) a perfected lien on, and pledge of, (i) all inter-company notes owing to NFI, and (ii) certain of the capital stock of, and all inter-company notes owing to all of NFI's existing and direct and indirect subsidiaries, and (b) a perfected lien on, and security interest in, all of the existing and future tangible and intangible properties and assets of NFI and its direct and indirect subsidiaries, with certain exceptions.

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7. CONVERTIBLE DEBENTURES

On June 5, 2012, the Company completed a public offering of \$65,000 aggregate principal amount of Debentures, bearing interest at a rate of 6.25% per annum, payable semi-annually on the last day of June and December commencing on December 31, 2012. The Debentures will mature on June 30, 2017 (the "Maturity Date"). The Debentures are convertible at the holder's option into Shares at a conversion price of \$10.00 per Share (the "Conversion Option").

On and after June 30, 2015 and prior to maturity, the Debentures may be redeemed in whole or in part from time to time at the Company's option, at a price equal to their principal amount plus accrued and unpaid interest, provided that the volume weighted average trading price of the Shares on the TSX for the 20 consecutive trading days preceding the date on which the notice of redemption is given is not less than 125% of the conversion price.

On the Maturity Date, the Company shall repay the holders in cash the principal of the Debentures and all accrued and unpaid interest thereon, up to but excluding the Maturity Date. However, the Company may, at its option, subject to receiving all applicable regulatory approvals and giving the required notice, elect to satisfy its obligation to repay on the Maturity Date the principal amount, in whole or in part, by issuing and delivering to holders that number of fully paid and non-assessable freely tradeable Shares calculated by dividing the principal amount of Debentures by 95% of the current market price of the Shares on the fifth trading day preceding the Maturity Date.

On the date of issuance, the gross proceeds in the amount of \$65,000 were allocated firstly to the liability component of the Debentures based on the fair value of a similar instrument without a conversion option and the residual value being allocated to the Conversion Option. The fair value of the Debentures was estimated by calculating the discounted cash flows of the Debentures using prevailing market rates for similar non-convertible debt instruments. The fair value of the Debentures is classified as a liability, while the residual value of the Debentures, net of taxes, is classified as a separate component of shareholders' equity. The liability component will accrete to its final redemption amount of \$65,000 less all conversions, at Maturity Date at an effective interest rate over the five-year term of the Debentures.

Principal amounts of \$9,739 of Debentures were converted by debenture holders to Shares during 2016 Q3. The principal amount of Debentures outstanding at October 2, 2016 is \$16,038.

The net book value of the outstanding Debentures at October 2, 2016 is reflected as a current liability on the interim condensed consolidated statements of financial position, as the Maturity Date is less than 12 months from the reporting date.

	Debt liability component	Equity component of Debt	Net Book Value October 2, 2016	Net Book Value December 27, 2015
Proceeds from issue of Debentures	\$ 59,412	\$ 5,588	\$ 65,000	\$ 65,000
Debt issuance costs	(3,463)	(326)	(3,789)	(3,789)
Net proceeds	55,949	5,262	61,211	61,211
Deferred taxes	—	(351)	(351)	(1,421)
Accretion in carrying value of debt liability	6,917	—	6,917	5,986
Conversion of Debentures to Shares	(47,184)	(3,963)	(51,147)	(850)
Net book value	\$ 15,682	\$ 948	\$ 16,630	\$ 64,926

8. SHARE CAPITAL

Authorized

Unlimited Shares

Issued

	October 2, 2016	December 27, 2015
60,958,977 Shares (December 27, 2015: 55,739,281)	\$ 645,195	\$ 591,758

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8. SHARE CAPITAL (Continued)

The following is a summary of changes to the issued and outstanding capital stock during the periods:

Shares	Number (000s)	Net Book Value
December 27, 2015	55,739	\$ 591,758
Stock options exercised	403	3,768
Restricted share units exercised	6	141
Conversion of Debentures to Shares	4,811	49,227
Deferred tax assets recognized as a result of historical share redemptions	—	301
October 2, 2016	60,959	\$ 645,195

9. EARNINGS PER SHARE

	13-Weeks Ended October 2, 2016	13-Weeks Ended September 27, 2015	40-Weeks Ended October 2, 2016	39-Weeks Ended September 27, 2015
Net earnings attributable to equity holders	\$ 26,002	\$ 16,559	\$ 83,336	\$ 39,784
Weighted average number of Shares outstanding	60,760,931	55,517,364	58,774,488	55,511,927
Add: net incremental Shares from assumed conversion of stock options and exercise of restricted share units	797,465	598,555	735,029	448,851
Weighted average number of Shares for calculation of diluted earnings per Share	61,558,396	56,115,919	59,509,517	55,960,778
Net earnings per Share (basic)	\$ 0.4279	\$ 0.2982	\$ 1.4179	\$ 0.7166
Net earnings per Share (diluted)	\$ 0.4224	\$ 0.2950	\$ 1.4004	\$ 0.7109

Basic earnings per Share is calculated by dividing the net earnings attributable to equity holders of the Company by the weighted average number of Shares outstanding during the period excluding Shares purchased by the Company and held as treasury shares. During the period the Company did not hold any Shares as treasury shares.

Diluted earnings per Share is calculated using the same method as basic earnings per Share except that the average number of Shares outstanding includes the potential dilutive effect of outstanding stock options and restricted share units granted by the Company as determined by the treasury stock method. Dilution could occur through the exercise of stock options, restricted share units or the exercise of the Conversion Option or the Debentures being repaid with Shares at Maturity Date at 95% of market price. Currently, the 1.6 million Shares issuable pursuant to the conversion of the Debentures are considered anti-dilutive, therefore both the convertible debenture Shares and the related interest are disregarded in calculating diluted earnings per Share.

10. SUPPLEMENTAL CASH FLOW INFORMATION

Changes in non-cash working capital items

	13-Weeks Ended October 2, 2016	13-Weeks Ended September 27, 2015	40-Weeks Ended October 2, 2016	39-Weeks Ended September 27, 2015
Cash inflow (outflow)				
Accounts receivable	\$ 3,116	\$ (28,480)	\$ 2,292	\$ (5,534)
Income taxes recoverable	(5,782)	—	(3,757)	778
Inventories	(49,694)	1,935	(63,357)	(10,376)
Prepaid expenses and deposits	2,080	127	(7,482)	669
Accounts payable and accrued liabilities	36,806	1,227	61,255	(30,053)
Income taxes payable	1,816	(100)	(6,306)	6,392
Deferred revenue	(3,674)	9,511	108	(13,849)
Provision for warranty costs	4,859	2,454	10,371	9,789
Other	8,753	6,855	8,102	(1,998)
	\$ (1,720)	\$ (6,471)	\$ 1,226	\$ (44,182)

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11. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

(a) Financial Instruments

The Company has made the following classifications:

Cash	Loans and receivables
Accounts receivable	Loans and receivables
Deposits	Loans and receivables
Income tax receivable	Loans and receivables
Accounts payables and accrued liabilities	Other Liabilities
Convertible debentures	Other Liabilities
Income taxes payable	Other Liabilities
Long-term debt	Other Liabilities
Derivative financial instruments	Fair value through profit or loss

(b) Fair value measurement of financial instruments

The Company categorizes its fair value measurements of financial instruments recorded at fair value according to a three-level hierarchy. The hierarchy prioritizes the inputs used by the Company's valuation techniques. A level is assigned to each fair value measurement based on the lowest level input significant to the fair value measurement in its entirety. The three levels of the fair value hierarchy are defined as follows:

Level 1 - fair value measurements that reflect unadjusted, quoted prices in active markets for identical assets and liabilities that the Company has the ability to access at the measurement date.

Level 2 - fair value measurements using inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly or indirectly. These include quoted prices for similar assets and liabilities in active markets, quoted prices for identical or similar assets and liabilities in inactive markets, inputs that are observable that are not prices (such as interest rates and credit risks) and inputs that are derived from or corroborated by observable market data.

Level 3 - fair value measurements using significant non-market observable inputs. These include valuations for assets and liabilities that are derived using data, some or all of which is not market observable data, including assumptions about risk.

The following table presents the carrying amounts and fair values of financial assets and financial liabilities, including their levels in the fair value hierarchy. The table distinguishes between those financial instruments recorded at fair value and those recorded at amortized cost. The table also excludes fair value information for financial assets and financial liabilities not measured at fair value if the carrying amount is a reasonable approximation of fair value.

	October 2, 2016		
	Fair value level	Carrying amount	Fair value
Financial assets recorded at fair value			
Total return swap contracts	Level 2	\$ 1,726	\$ 1,726
Foreign exchange forward contracts	Level 2	252	252
Derivative financial instrument assets		\$ 1,978	\$ 1,978
Financial liabilities recorded at fair value			
Derivative financial instrument liabilities			
Interest rate swap	Level 2	\$ 4,583	\$ 4,583
Financial liabilities recorded at amortized cost			
Debentures (including equity conversion option)	Level 2	\$ 16,630	\$ 49,610

(c) Risk Management

The Company uses derivative financial instruments including interest rate swaps, total return swaps, foreign exchange options and forward foreign exchange contracts. These instruments are financial contracts whose value depends on interest rates, share price and foreign currency prices.

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11. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)

The use of derivatives allows the transfer, modification and reduction of current and expected risks, including interest rate, share price, foreign exchange and other market risks. The Company uses derivative financial instruments to manage interest rate, share price and foreign exchange risks in accordance with its risk management policies. Certain derivative instruments, while providing effective economic hedges, are not designated as hedges for accounting purposes. Changes in the fair value of the total return swap are recognized in "sales, general and administration costs and other operating expenses" and foreign exchange forward contracts are recognized as "unrealized foreign exchange loss on non-current monetary items" in the interim condensed consolidated statements of net earnings and total comprehensive income consistent with the underlying nature and purpose of the derivative instruments.

On January 22, 2016, the Company replaced the \$142,000 interest rate swap with a new interest rate swap designed to hedge floating rate exposure on the \$482,000 term loan. The new interest rate swap fixes the interest rate at 1.034% plus the applicable interest margin until December 2019. The fair value of the interest rate swap liability at October 2, 2016 is \$4,583 (December 27, 2015: \$1,351) and the change in fair value has been recorded within finance costs for the reported period. The related liability has been recorded on the interim condensed consolidated statements of financial position as a derivative financial instruments liability.

On March 30, 2016, the Company entered into a total return swap transaction to hedge the exposure associated with increases in its share value on a portion of the outstanding performance share units, deferred share units and restricted share units. The Company does not apply hedge accounting to these derivative instruments and as such, gains and losses arising from marking these derivatives to market are recognized in net earnings in the period in which they arise. As at October 2, 2016, the Company had built a position of 569,614 Shares at a weighted average price of C\$35.57. The total return swap has a re-investment feature which increases the number of Shares in the swap when dividends are paid by the Company.

(d) Liquidity Management

The Company's approach to managing liquidity risk is to ensure, as far as possible, that it will always have sufficient liquidity to meet liabilities when due. At October 2, 2016, the Company had bank indebtedness of \$467 (December 27, 2015: \$24,880 of cash) and the \$343,000 Revolver. As at October 2, 2016, there was \$76,000 of direct borrowings (December 27, 2015: \$180,060) and \$10,910 of outstanding letters of credit (December 27, 2015: \$13,975) under the Revolver.

The Company's principal sources of funds are cash generated from its operating activities, share or debt issuances and borrowing capacity remaining under the Credit Facility. Management believes that these sources of funds will provide NFI with sufficient liquidity and capital resources to meet its current and future financial obligations as they come due, as well as to provide funds for its financing requirements, capital expenditures and other needs for the foreseeable future.

(e) Credit risk

The carrying amount of accounts receivable is reduced through the use of an allowance account and the amount of the loss is recognized in the interim condensed consolidated statements of net earnings and total comprehensive income within "sales, general and administration costs and other operating expenses". When a receivable balance is considered uncollectible, it is written off against the allowance for doubtful accounts. Subsequent recoveries of amounts previously written off are credited against "sales, general and administration costs and other operating expenses" in the interim condensed consolidated statements of net earnings and total comprehensive income.

The following table details the aging of the Company's receivables and related allowance for doubtful accounts as follows:

	October 2, 2016	December 27, 2015
Current, including holdbacks	\$ 281,840	\$ 292,717
Past due amounts but not impaired		
1 - 60 days	22,197	17,977
Greater than 60 days	11,410	7,047
Less: Allowance for doubtful accounts	(643)	(645)
Total accounts receivables, net	\$ 314,804	\$ 317,096

As at October 2, 2016, there was no amount that would otherwise be past due or impaired whose terms have been renegotiated.

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11. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (Continued)

There are certain financial covenants under the Credit Facility that must be maintained. These financial covenants include an interest coverage ratio and total leverage ratio. The total leverage ratio covenant of less than 4.00 reduces to 3.75 beginning January 2, 2017 and finally reduces to 3.50 beginning January 1, 2018. As at October 2, 2016, the Company was in compliance with the financial covenants in the Credit Facility. The results of the financial covenants tests as of such date are as follows:

	October 2, 2016	December 27, 2015
Total Leverage Ratio (must be less than 4.00)	2.08	2.91
Interest Coverage Ratio (must be greater than 3.00)	12.02	18.48

Compliance with financial covenants is reported quarterly to the board of directors. Other than the requirements imposed by borrowing agreements, the Company is not subject to any externally imposed capital requirements. Capital management objectives are reviewed on an annual basis. The capital management objectives are unchanged from the last reporting period.

12. SEGMENT INFORMATION

The Company has two reportable segments: Manufacturing Operations and Aftermarket Operations, which are the Company's strategic business units. The strategic business units offer different products and services, and are managed separately because they require different economic characteristics and marketing strategies. For each of the strategic business units, the Company's President and CEO reviews internal management reports on a monthly basis.

The Manufacturing Operations segment derives its revenue from the manufacture of transit buses and motor coaches. The Aftermarket Operations segment derives its revenue from the provision of service parts and support related to transit buses and motor coaches. These operating segments are consistent with the management of the business, which is based on the products and services offered.

There is no inter-segment revenue. Unallocated items in the consolidated earnings before income taxes primarily include unrealized foreign exchange gains or losses and finance costs. Corporate overhead costs are allocated fully to the Manufacturing Operations segment.

The Manufacturing Operations segment has recorded vendor rebates of \$1,306 (2015 Q3: \$777), which have been recognized into earnings during 2016 Q3, but for which the full requirements for entitlement to these rebates have not yet been met.

The unallocated total assets of the Company primarily include cash, intangible assets, derivative financial instruments and deferred income tax assets. Corporate assets that are shared by both operating segments are allocated fully to the Manufacturing Operations segment.

Segment information about profits and assets is as follows:

	13-Weeks Ended October 2, 2016			
	Manufacturing Operations	Aftermarket Operations	Unallocated	Total
Revenue from external customers	\$ 412,447	\$ 99,036	\$ —	\$ 511,483
Operating costs and expenses	384,085	80,765	—	464,850
Earnings (loss) before income tax expense	28,362	18,271	(4,263)	42,370
Total assets	1,131,004	389,732	277,908	1,798,644
Addition of intangible assets	—	—	—	—
Addition of capital expenditures	5,314	359	—	5,673
Goodwill	252,626	131,959	—	384,585

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12. SEGMENT INFORMATION (Continued)

	13-Weeks Ended September 27, 2015			
	Manufacturing Operations	Aftermarket Operations	Unallocated	Total
Revenue from external customers	\$ 292,970	\$ 71,713	\$ —	\$ 364,683
Operating costs and expenses	281,725	57,975	—	339,700
Earnings (loss) before income tax expense	11,245	13,738	(4,472)	20,511
Total assets	571,905	200,335	362,941	1,135,181
Addition of intangibles assets	4	11	—	15
Addition of capital expenditures	1,800	49	—	1,849
Goodwill	149,950	62,705	—	212,655

	40-Weeks Ended October 2, 2016			
	Manufacturing Operations	Aftermarket Operations	Unallocated	Total
Revenue from external customers	\$ 1,333,351	\$ 318,295	\$ —	\$ 1,651,646
Operating costs and expenses	1,234,216	262,126	—	1,496,342
Earnings (loss) before income tax expense	99,135	56,169	(24,966)	130,338
Total assets	1,131,004	389,732	277,908	1,798,644
Addition of intangibles assets	15	161	—	176
Addition of capital expenditures	12,646	1,699	—	14,345
Goodwill	252,626	131,959	—	384,585

	39-Weeks Ended September 27, 2015			
	Manufacturing Operations	Aftermarket Operations	Unallocated	Total
Revenue from external customers	\$ 869,474	\$ 250,522	\$ —	\$ 1,119,996
Operating costs and expenses	845,919	205,129	—	1,051,048
Earnings (loss) before income tax expense	23,555	45,393	(12,778)	56,170
Total assets	571,905	200,335	362,941	1,135,181
Addition of intangibles assets	7	104	—	111
Addition of capital expenditures	7,937	94	—	8,031
Goodwill	149,950	62,705	—	212,655

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13. COMMITMENTS AND CONTINGENCIES

- (a) Through the normal course of operations, the Company has indemnified the surety companies providing surety bonds required under various contracts with customers. In the event that the Company fails to perform under a contract and the surety companies incur a cost on a surety bond, the Company is obligated to repay the costs incurred in relation to the claim up to the value of the bond. The Company's guarantee under each bond issued by the surety companies expires on completion of obligations under the customer contract to which the bond relates. The estimated maturity dates of the surety bonds outstanding at October 2, 2016 range from October 2016 to May 2018.

At October 2, 2016, outstanding surety bonds guaranteed by the Company totaled \$276,533 (December 27, 2015: \$182,096). The Company has not recorded any liability under these guarantees, as management believes that no material events of default exist under any contracts with customers.

- (b) The Company has a letter of credit sub-facility of \$55,000 as part of the \$343,000 Revolver. As at October 2, 2016, letters of credit totaling \$10,910 (December 27, 2015: \$13,975) remain outstanding under the letter of credit facility.

As at October 2, 2016, management believes that the Company is in compliance in all material respects with all applicable contractual obligations and the Company has not provided for any costs associated with these letters of credit.

14. PROVISION FOR WARRANTY COSTS

The Company generally provides its customers with a base warranty on the entire bus or motor coach as well as a base corrosion warranty on the related structure. The Company also provides certain extended warranties, including those covering brake systems, lower level components, fleet defect provisions and engine-related components, covering a warranty period of approximately one to five years, depending on the product and customer contract. The extended warranty liability is recorded as deferred revenue.

The movements in the provision for the base warranty costs during the period are as follows:

	Total
December 27, 2015	\$ 51,896
Additions	25,962
Amounts used	(15,943)
Unwinding of discount and effect of changes in the discount rate	(77)
Exchange differences	429
	62,267
Less: current portion	(26,490)
October 2, 2016	\$ 35,777

15. ACCRUED BENEFIT LIABILITY

For the 13-weeks ended October 2, 2016, the Company recorded an actuarial gain of \$2,701 (net of \$1,096 of income tax expense) on its defined benefit plans and an actuarial loss of \$5,059 (net of \$2,724 of income tax recovered) for the 40-weeks ended October 2, 2016. The actuarial gain and loss resulted from a decrease in the discount rate offset by changes in the demographic assumptions used to value the defined benefit obligation.