



## News Release

### **AZURE DYNAMICS ANNOUNCES 2004 SECOND QUARTER RESULTS**

Toronto, Ontario – August 13, 2004

[Azure Dynamics Corporation \(TSX – AZD\)](#) (“Azure” or the “Company”) a leading developer of hybrid electric powertrains for commercial vehicles is pleased to announce its results for the three months ended June 30, 2004 (“quarter”).

Mr. D. Campbell Deacon, stated, “We made significant progress in the quarter from both a product and financing perspective. On the product front, the highlight was the UK launch of the first ever hybrid-electric black cab with London Taxis International. The Company’s shares began trading on the TSX main board in June 2004. In the quarter, we also laid the foundation for a financing worth \$11.5 million that closed in July 2004 and culminated with a listing of the Company’s shares and certain warrants on the Alternative Investment Market (“AIM”) of the London Stock Exchange in August 2004.”

For the quarter ended June 30, 2004, the Company incurred a net loss of \$1,709,696 (\$0.02 per share) compared to a net loss of \$595,857 (\$0.01 per share) in 2003; for the six months ended June 30, 2004 the cumulative net loss was \$2,916,549 (\$0.04 per share) compared to \$1,419,265 (\$0.03 per share) in 2003. The Company completed equity financings in December 2003 and March 2004 which have enabled it to ramp up its resources and to progress its customer and development programs and hence all activity levels are higher than in the comparable period. Contributions from customers, sponsors and government funding, have helped offset the higher expenditure levels; contributions totalled \$1.5 million for the six months ended June 30, 2004 compared to \$0.7 million for the comparable period in 2003.

Subsequent to the quarter-end, on July 27, 2004, Azure completed a financing raising gross proceeds of \$3 million, secured access to an additional \$8.5 million by way of a underwriting of existing and outstanding warrants, as well as preserved eligibility for up to an additional \$3 million in respect of its facility with Technology Partnerships Canada (“TPC”), subject to TPC conditions. The financing arrangements have positioned the Company with access to funds to support its commercialization activities until the end of December 2005, based on current plans.

The Company’s interim financial statements and Management’s discussion and analysis are attached to this press release and are available for inspection at [www.sedar.com](http://www.sedar.com) or on the Company’s website.

[Azure Dynamics Corporation](#) provides Hybrid Electric Vehicle technology for light and medium duty commercial vehicles in urban areas. Azure is a public company trading on the Canadian TSX Exchange. The company is currently working with various partners and customers worldwide including Purolator Courier, Canada Post, London Taxis International, Leyland Product Development, Renault Trucks UK, and the United States Postal Service. Azure has employees based in Canada, the United States and the United Kingdom.

**Note:** The foregoing information may contain forward-looking statements which involve known and unknown risks, uncertainties and other factors which may cause the actual results to be materially different from any future results, performance or achievements expressed or implied by such statements. Such factors include, but are not limited to: the ability to raise the capital required for product development and operations, product development delays, changing environmental regulations, the ability to attract and retain business partners, competition from other developers of hybrid electric vehicle control systems, competition from other advanced or existing power technologies, evolving markets for power for transportation vehicles. These factors should be considered carefully and readers should not place undue reliance on Azure's forward-looking statements. Investors are encouraged to review the risks detailed from time to time in the company's filings with regulatory authorities.

**FOR MORE INFORMATION, CONTACT:**

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**Azure Dynamics Corporation**  
**(A Development Stage Enterprise)**  
**Unaudited Interim Consolidated Financial Statements**  
**For the six months ended June 30, 2004**

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**Azure Dynamics Corporation**  
**(A Development Stage Enterprise)**  
**Consolidated Balance Sheets**

As at	June 30 2004 (Unaudited)	December 31 2003 (Audited)	June 30 2003 (Unaudited)
	\$	\$	\$
<b>ASSETS</b>			
<b>Current</b>			
Cash and cash equivalents	10,366,435	9,075,219	432,974
Accounts receivable	400,368	337,794	61,714
Contributions receivable	602,343	780,459	72,680
Prepaid expenses	491,173	61,655	41,174
	<b>11,860,319</b>	<b>10,255,127</b>	<b>608,542</b>
<b>Employee loans</b>	-	91,727	257,429
<b>Deferred costs (note 2(a))</b>	<b>815,497</b>	-	-
<b>Property and equipment</b>	<b>482,287</b>	162,048	212,663
<b>Other assets</b>	<b>102,281</b>	117,279	101,286
	<b>13,260,384</b>	<b>10,626,181</b>	<b>1,179,920</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>			
<b>Current</b>			
Accounts payable and accrued liabilities	1,265,007	567,692	372,125
Obligations under capital leases	-	-	2,575
	<b>1,265,007</b>	<b>567,692</b>	<b>374,700</b>
<b>Deferred sponsorship contributions</b>	-	-	527,363
<b>Shareholders' equity</b>			
Share capital	28,503,537	23,991,665	11,813,905
Special warrants	-	-	90,000
Contributed surplus	509,363	167,798	61,367
Deficit	(17,017,523)	(14,100,974)	(11,687,415)
	<b>11,995,377</b>	<b>10,058,489</b>	<b>277,857</b>
	<b>13,260,384</b>	<b>10,626,181</b>	<b>1,179,920</b>
* Certain comparative numbers have been restated as described in Note 3(e).			

Approved on behalf of the Board:

"D. Campbell Deacon" Director

"Dennis A. Sharp" Director

**Azure Dynamics Corporation**  
**(A Development Stage Enterprise)**  
**Unaudited Consolidated Statements of Operations and Deficit**

	For the three months ended		For the six months ended	
	June 30		June 30	
	2004	2003	2004	2003
	\$	\$	\$	\$
<b>Revenue</b>				
Other	47,417	7,674	87,090	13,850
<b>Expenses</b>				
Research and development, net	609,394	69,548	878,838	355,446
Selling and marketing	386,947	151,948	735,070	293,765
General and administrative	597,757	281,927	1,114,659	583,911
Rent and ancillary	110,485	56,843	181,828	113,836
Amortization of property and equipment and other assets	52,530	43,265	93,244	86,157
	<b>1,757,113</b>	603,531	<b>3,003,639</b>	1,433,115
<b>Net loss for the period</b>	<b>(1,709,696)</b>	(595,857)	<b>(2,916,549)</b>	(1,419,265)
Deficit, beginning of period	(15,307,827)	(11,091,558)	(14,100,974)	(10,268,150)
<b>Deficit, end of period</b>	<b>(17,017,523)</b>	(11,687,415)	<b>(17,017,523)</b>	(11,687,415)
<b>Loss per share - basic *</b>	<b>(0.02)</b>	(0.01)	<b>(0.04)</b>	(0.03)
Weighted average number of shares - basic	84,032,618	45,031,042	81,779,593	45,019,716
* No fully diluted earnings per share have been disclosed, as these would be anti dilutive.				
** Certain comparative numbers have been restated as described in Note 3(e).				

**Azure Dynamics Corporation**  
**(A Development Stage Enterprise)**  
**Unaudited Consolidated Statements of Cash Flows**

	For the three months ended		For the six months ended	
	June 30		June 30	
	2004	2003	2004	2003
	\$	\$	\$	\$
<b>Cash flows from operating activities</b>				
Net loss for the period	(1,709,696)	(595,857)	(2,916,549)	(1,419,265)
Adjustments for:	-	-		
Amortization of property and equipment and other assets	52,530	43,265	93,244	86,157
Common shares issued in exchange for services	20,625	6,250	27,500	12,500
Stock option compensation expense	140,337	16,674	341,565	61,367
Changes in non-cash working capital items	681,581	(373,833)	383,339	(303,079)
	(814,623)	(903,501)	(2,070,901)	(1,562,320)
<b>Cash flows from financing activities</b>				
Issuance of common shares (net of costs)	362,681	-	4,484,372	-
Deferred costs	(815,497)	-	(815,497)	-
Research and development sponsorship funds received	-	1,000,000	-	1,000,000
Repayment on obligations under capital lease	-	(3,702)	-	(7,222)
	(452,816)	996,298	3,668,875	992,778
<b>Cash flows from investing activities</b>				
Acquisition of property and equipment	(165,183)	(3,246)	(387,040)	(3,246)
Acquisition of other assets	(7,586)	(7,293)	(11,445)	(24,832)
Changes in loans to employees	68,509	-	91,727	-
	(104,260)	(10,539)	(306,758)	(28,078)
<b>Increase (decrease) in cash and cash equivalents</b>	<b>(1,371,699)</b>	<b>82,258</b>	<b>1,291,216</b>	<b>(597,620)</b>
Cash and cash equivalents, beginning of period	11,738,134	350,716	9,075,219	1,030,594
<b>Cash and cash equivalents, end of period</b>	<b>10,366,435</b>	<b>432,974</b>	<b>10,366,435</b>	<b>432,974</b>
* Certain comparative numbers have been restated as described in Note 3(e).				

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**Azure Dynamics Corporation**  
**(A Development Stage Enterprise)**  
**Notes to the Consolidated Financial Statements**

**Six Months ended June 30, 2004 and 2003 (unaudited)**

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**1. Nature of Operations and Basis of Presentation**

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Azure Dynamics Corporation (“the Company”) (“ADC”) is incorporated under the laws of Alberta. The Company was party to a reverse takeover transaction (“RTO”) between ADC (the deemed acquiree) and Azure Dynamics Inc. (“ADI”) (the deemed acquirer), effective April 24, 2001. ADI is incorporated under the laws of Canada and is a wholly owned subsidiary of ADC. On December 31, 2002, the Company changed the reporting year-end for the consolidated entities to December 31 from June 30. On March 9, 2004, the Company incorporated Azure Dynamics U.S. Inc. under the laws of the State of Delaware, USA. On April 6, 2004, the Company incorporated Azure Dynamics UK Limited under the laws of England and Wales. Azure Dynamics U.S. Inc. and Azure Dynamics UK Limited are wholly owned subsidiaries of ADC.

The Company is a development stage enterprise, involved in developing adaptive hybrid electric vehicle control systems to be used in commercial vehicle applications. The Company has not yet determined the ultimate economic viability of the products under development. The Company is currently in the process of testing its control systems. All costs incurred to date have been recorded as research and development expense. No commercial revenue has been generated from the sale of its products to date.

The consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles on a going concern basis which presumes the realization of assets and discharge of liabilities in the normal course of business for the foreseeable future. There are several development stages to be completed before the marketability, if any, of the Company’s technology can be determined. While the Company has derived limited revenue from the performance of research and development projects for third parties, its ability to continue operations is uncertain and dependent upon the successful completion of technical development of the technology, obtaining additional financing and achieving profitable operations. The outcome of these matters cannot be predicted at this time. These consolidated financial statements do not include any adjustments to the assets and liabilities that might be necessary should the Company be unable to continue in business. The unaudited interim consolidated financial statements and notes do not include all disclosures required for annual statements and should be read in conjunction with the audited financial statements for the year ended December 31, 2003.

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**2. Significant Accounting Policies**

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The unaudited interim consolidated financial statements of the Company have been prepared by management in accordance with generally accepted accounting principles in Canada. The accounting policies and methods of application used in preparation of these financial statements are consistent with the December 31, 2003 audited financial statements except as stated below.

(a) Deferred costs

The costs incurred by the Company in respect of capital financing and related transactions are deferred on the balance sheet until such time as the transactions are concluded, at which time the deferred costs are recognized as charges to the appropriate equity capital account.

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**3. Share Capital, Warrants and Stock Options**

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(a) Authorized

Unlimited common shares without par value

Unlimited preferred shares without par value, non cumulative, redeemable, and non voting

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**Azure Dynamics Corporation**  
**(A Development Stage Enterprise)**  
**Notes to the Consolidated Financial Statements**

**Six Months ended June 30, 2004 and 2003 (unaudited)**

**3. Share Capital, Warrants and Stock Options (Cont'd.)**

(b) Issued and outstanding common shares

	Number of Common Shares	Amount
Balance, December 31, 2003	78,163,836	\$ 23,991,665
Private placement	4,861,110	3,896,399
Issued on exercise of agent's compensation options	80,000	39,600
Issued on exercise of stock options	756,665	245,846
Issued in lieu of non-executive directors fees	42,307	27,500
Issued on exercise of warrants	725,000	449,500
TSX listing costs		(146,973)
Balance, June 30, 2004	84,628,918	\$ 28,503,537

On March 10, 2004, the Company completed a private placement of 4,861,110 common shares of the Company at a price of £0.36 per share (approximately \$0.90 per share), for net proceeds of \$3,896,399 after deducting share issue costs of \$287,851.

On June 4, 2004, the common shares of the Company commenced trading on the main board of the TSX and were de-listed from trading on the TSX Venture Exchange. The costs of listing the common shares on the TSX, \$146,973, have been charged to the share capital account.

(c) Warrants

In conjunction with a private placement financing, completed December 1, 2003, the Company issued 12,691,060 warrants, each warrant being exercisable into one common share of the Company, at a price of \$0.62 per share, until December 1, 2004. As at June 30, 2004, there were 11,966,060 warrants outstanding.

(d) Stock options

The Company has a stock option plan (the "Plan") for which up to 10,350,000 common shares can be reserved for issuance to executive officers and directors, employees and consultants. The exercise price of the options is determined by the Board of Directors' based on their best estimate of the fair value of the common shares at the grant date, subject to applicable stock exchange pricing policies. The options have a maximum term of five years and generally vest over a twelve to twenty-four month period.

As at June 30, 2004, the Company had 7,765,561 stock options outstanding under the Plan and 2,245,508 agent's compensation options outstanding. Of the total 10,011,069 options outstanding, 7,632,474 were exercisable at a weighted average exercise price of \$0.50 per common share. The stock options expire on various dates between December 1, 2004 and May 18, 2009.

Stock option transactions for the six months ended June 30, 2004, and the number of stock options outstanding are summarized as follows:

	Number of Optioned Common Shares #	Weighted Average Exercise Price \$
<b><u>Executive Officers, Directors, Employees and Consultant Options:</u></b>		
Balance, December 31, 2003	6,173,000	0.44
Options granted	2,364,227	0.72
Options exercised	(756,665)	0.33
Options expired/cancelled	(15,001)	0.56
Balance, June 30, 2004	<b>7,765,561</b>	<b>0.53</b>

**Azure Dynamics Corporation**  
**(A Development Stage Enterprise)**  
**Notes to the Consolidated Financial Statements**

**Six Months ended June 30, 2004 and 2003 (unaudited)**

**3. Share Capital, Warrants and Stock Options (Cont'd.)**

(d) Stock options (Cont'd.)

	<b>Number of Optioned Common Shares #</b>	<b>Weighted Average Exercise Price \$</b>
<b><u>Agent's Compensation Options:</u></b>		
Balance, December 31, 2003	2,325,508	0.495
Options exercised – March 2004	(80,000)	0.495
Balance June 30, 2004	<b>2,245,508</b>	<b>0.495</b>
<b>Total Options Outstanding, June 30, 2004</b>	<b>10,011,069</b>	<b>0.52</b>

As at June 30, 2004, the numbers of optioned common shares outstanding and exercisable are as follows:

<b>Expiry date</b>	<b>Number outstanding #</b>	<b>Number exercisable #</b>	<b>Exercise price \$</b>
December 1, 2004	2,245,508	2,245,508	0.495
December 31, 2004	250,000	125,000	0.70
April 25, 2006	1,870,000	1,870,000	0.25
August 20, 2006	160,000	160,000	0.44
November 5, 2006	227,000	227,000	0.45
November 26, 2006	112,000	112,000	0.50
January 22, 2007	50,000	50,000	0.61
February 12, 2007	30,000	30,000	0.61
March 7, 2007	20,000	20,000	0.71
March 11, 2007	1,150,000	1,150,000	0.73
April 12, 2007	30,000	30,000	0.94
May 1, 2007	145,000	145,000	0.80
January 1, 2008	235,000	231,667	0.50
February 1, 2008	147,334	98,223	0.50
August 25, 2008	475,000	183,333	0.30
September 26, 2008	750,000	250,000	0.48
January 1, 2009	1,547,227	515,742	0.65
February 1, 2009	100,000	33,333	0.85
March 22, 2009	25,000	8,333	1.06
May 3, 2009	312,000	104,001	0.90
May 18, 2009	130,000	43,334	0.90
	<b>10,011,069</b>	<b>7,632,474</b>	

(e) Stock compensation expense

Effective January 1, 2003, the Company adopted the revised recommendations in CICA Handbook Section 3870 whereby it measures compensation costs associated with stock-based compensation using the fair value method and the cost is recognized over the vesting period of the stock option. The fair value of each performance share and stock option is determined at each issue or grant date using the Black-Scholes model with the following assumptions: risk free interest rate - 5%, expected life – 4 to 5 years, expected dividend yield - nil, and expected volatility – ranging from 17% to 30%. The Company recorded a compensation expense charge of \$341,565 for the six months ended June 30, 2004.

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**Azure Dynamics Corporation**  
**(A Development Stage Enterprise)**  
**Notes to the Consolidated Financial Statements**

**Six Months ended June 30, 2004 and 2003 (unaudited)**

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**3. Share Capital, Warrants and Stock Options (Cont'd.)**

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(e) Stock compensation expense (Cont'd.)

The comparative numbers for the three and six months ended June 30, 2003 have been restated to include the compensation expense related to options granted during that period. As the change in accounting policy was first implemented in the fourth quarter of 2003, with effect from January 1, 2003, the compensation expense was not previously recorded in the quarterly reporting. Total compensation expense for the three and six months ended June 30, 2003 was \$16,674 and \$61,367, respectively.

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**4. Related Party Transactions**

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- a) During the six months ended June 30, 2004, the Company incurred costs of \$1,709 (2003 - \$7,826) in respect of administrative services provided by Vizon SciTec (formerly B.C. Research Inc.), a significant shareholder.
  - b) During the six months ended June 30, 2004, the Company incurred costs of \$38,067 (2003 - \$74,842) in respect of leased premises and equipment provided by Vizon SciTec.
  - c) During the six months ended June 30, 2004, the Company paid \$121,500 (2003 - \$124,167) to a company controlled by an officer/director for services rendered to the Company in his capacity as an executive officer.
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**5. Commitments**

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Effective February 10, 2004, the Company entered into a sublease and license agreement for premises located at 3900 North Fraser Way, Burnaby, Canada and relocated its Vancouver-based operations to this site. The sub-lease arrangements were such that the Company shared access to the facility with the head leaseholder until May 1, 2004. Effective May 1, 2004, the Company has entered into a five year lease agreement for the premises directly with the Landlord, and also effective May 1, 2004 has entered into a sublease and licence agreement with the outgoing leaseholder, whereby that party continues to share access to the facility until July 31, 2004.

The annual lease commitments relating to this facility, as included in the schedule of commitments in Note 13 to the audited consolidated financial statements for the year ended December 31, 2003, are as follows:

2004	\$ 86,025
2005	\$ 175,150
2006	\$ 179,800
2007	\$ 181,350
2008	\$ 181,350
2009	\$ 60,450

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**Azure Dynamics Corporation**  
**(A Development Stage Enterprise)**  
**Notes to the Consolidated Financial Statements**

**Six Months ended June 30, 2004 and 2003 (unaudited)**

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**6. Subsequent Events**

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On July 27, 2004, the Company announced that it had closed an equity financing, whereby the Company issued 3,811,250 new common shares, at a price of \$0.80 per Unit, for gross proceeds of \$3,049,000. In addition, the Company issued 1,905,625 warrants entitling the holders to purchase one common share of the Company at a price of \$1.00 until July 27, 2005. Senior management of the Company subscribed for \$95,000 of the offering.

Simultaneously, the Company entered into the Capital Assurance Agreement pursuant to which it is ensured to receive by December 15, 2004 approximately \$8.5 million which the Company could otherwise receive upon the exercise of the Corporation's outstanding common share purchase warrants and agent compensation options. The Company has issued and outstanding 11,966,060 common share purchase warrants, each purchase warrant being exercisable at a price of \$0.62 until December 1, 2004 for one Common Share, and 2,245,508 common share agent compensation options, each agent option being exercisable at a price of \$0.495 until December 1, 2004 for one Common Share (collectively the "Old Warrants"). The Company has entered into a binding agreement with a number of parties (the "Obligors") which provides that, to the extent any Old Warrants are not exercised for any reason by their expiry time on December 1, 2004, the Obligors will, on a pro rata basis, subscribe for common shares of the Company at a price of \$0.60 per share, being the weighted average exercise price of the Old Warrants. In consideration for entering into the Capital Assurance Agreement, the Obligors will collectively receive a cash fee of \$765,000 of which \$510,000 was paid on July 27, 2004 and the balance of \$255,000 is due on December 16, 2004. Ludgate Investments Limited, an investment dealer in the United Kingdom, was paid an agent's fee of \$200,000 for services rendered to the Company in connection with the Capital Assurance Agreement. In addition, the Obligors received 1,700,000 warrants (the "Obligor Warrants") of the Company. Each Obligor Warrant will permit the holder to acquire one Common Share at an exercise price of \$1.00 up until July 27, 2005. Holders of the Obligor Warrants will not be able to exercise such warrants until December 16, 2004. A director of the Company undertook an Obligor obligation of \$600,000 and in connection with this undertaking will receive a cash fee of \$54,000 and 120,000 Obligor Warrants.

On August 6, 2004 the Company filed an admission document for a secondary listing of its shares and certain warrants on the Alternative Investment Market ("AIM") of the London Stock Exchange and the shares/warrants were admitted for trading on August 12, 2004.

As at June 30, 2004 the Company estimated that it had incurred costs of \$815,497 in legal, accounting and advisory fees in respect of the aforementioned capital and financing arrangements. These costs have been deferred on the balance sheet pending the conclusion of the transactions at which time the costs will be charged to the appropriate capital account.

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**For the quarter and six months ended June 30, 2004 compared to the quarter and six months ended June 30, 2003 and the year ended December 31, 2003**

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*This "Management's Discussion and Analysis" has been prepared as of August 9, 2004 and should be read in conjunction with the unaudited consolidated financial statements of the Company for the six months ended June 30, 2004 and the notes thereto and the audited consolidated financial statements of the Company for the year ended December 31, 2003 and the notes thereto.*

**Business Strategy of the Company and Overview of Operations**

Azure Dynamics Corporation ("Azure" or the "Company") has developed proprietary hybrid vehicle technology for the light to medium duty commercial vehicle category. The principal business of Azure is the development, and ultimate commercialization of its core technology, Hybrid Electric Vehicle ("HEV") control systems. The Company is a development stage enterprise – it is involved in the development and testing of its technology; commercial sales of its first product is targeted to commence at the end of 2004.

The Company has continued to execute its commercialization strategy and during the quarter has achieved further milestones in respect of product development and corporate/financing objectives. During the second quarter of 2004, Azure has continued the development work on its two powertrain platforms – G1 for vehicles in the medium-duty weight range 7,500 to 14,000 lbs gross vehicle weight, and G2r for vehicles in the light-duty weight range 5,000 to 7,500 lbs gross vehicle weight.

Due to advancements in the product durability and price competitiveness of Nickel-Metal Hydride batteries, the Company has introduced the potential of this battery technology into its Canada Post demonstration vehicles – it is anticipated that the refitted vehicles will be available for demonstration in regular service by the end of the third quarter of 2004. The G1 all-electric delivery vehicle launched in March 2004, in conjunction with Leyland Product Development and Renault Trucks UK, is currently being used for customer demonstration purposes with a view to building a customer order book. The Company also advanced its plans, and is pre-ordering components, for the build phase of the first of its pilot commercial production vehicles for Purolator Courier and in July 2004 launched the first all-electric prototype of the ground-up delivery vehicle that is being developed in conjunction with London Taxis International ("LTI"). The G1 project for the development of a prototype vehicle for the United States Postal Service ("USPS") is in the design and planning stage.

The Company, together with LTI, launched the first hybrid electric black taxi (G2r product) in England in June 2004. Apart from customer demonstrations, the hybrid taxi is undergoing extensive trials at a test facility in England, the results of which will be incorporated in design advancements in a second generation taxi to be delivered to England in the fourth quarter of 2004. The G2r project for the development of a prototype vehicle for USPS is in the design and planning stage.

Organizationally, the Company has settled into its new facilities in Vancouver and has taken steps to bolster its human resources. Numerous positions were filled in the quarter, including the Vice President, Supply Chain and the General Manager for Azure's United Kingdom operations. The Company also executed its plans to broaden and strengthen its financial resources and shareholder base. On June 4, 2004 the Company's shares were listed for trading on the Toronto Stock Exchange (TSX:AZD) and on August 12, 2004 the shares and certain warrants will be listed on the Alternative Investment Market ("AIM") of the London Stock Exchange (AIM:ADC). On July 27, 2004 Azure completed a financing securing gross proceeds of \$3.0 million, secured access to an additional \$8.5 million by way of a underwriting of existing and outstanding warrants, as well as preserved eligibility for up to an additional \$3 million in respect of its facility with Technology Partnerships Canada ("TPC"), subject to TPC conditions.

For the quarter and six months ended June 30, 2004 compared to the quarter and six months ended June 30, 2003 and the year ended December 31, 2003

### Operating Results, Cash Flows and Financial Condition

#### Statement of Operations Discussion:

For the quarter ended June 30, 2004, the Company incurred a net loss of \$1,709,696 (\$0.02 per share) compared to a net loss of \$595,857 (\$0.01 per share) in 2003; for the six months ended June 30, 2004 the cumulative net loss was \$2,916,549 (\$0.04 per share) compared to \$1,419,265 (\$0.03 per share) in 2003. As the Company currently has no commercial revenues it mainly incurs costs to progress its development and commercialization plans. The Company completed equity financings in December 2003 and March 2004 which have enabled it to ramp up its resources and to progress its customer and development programs and hence all activity levels are higher than in the comparable period. Contributions from customers, sponsors and government funding, have helped offset the higher expenditure levels; contributions totalled \$1.5 million for the six months ended June 30, 2004 compared to \$0.7 million for the comparable period in 2003.

#### Selected Quarterly information:

	Q2, 2004 (Apr – Jun)	Q1, 2004 (Jan – Mar)	Q4, 2003 (Oct – Dec)	Q3, 2003 (Jul – Sept)
Revenue	\$ 47,417	\$ 39,673	\$ 23,993	\$ 9,540
Expenses	\$ (1,757,113)	\$ (1,246,526)	\$ (1,182,302)	\$ (1,264,790)
Net loss for the period	\$ (1,709,696)	\$ (1,206,853)	\$ (1,158,309)	\$ (1,255,250)
Loss per share	\$ (0.02)	\$ (0.02)	\$ (0.02)	\$ (0.03)
Weighted average number of Shares	84,032,618	79,525,744	54,547,058	45,044,375

	Q2, 2003 (Apr – Jun)	Q1, 2003 (Jan – Mar)	Q4, 2002 (Oct – Dec)	Q3, 2002 (Jul – Sept)
Revenue	\$ 7,674	\$ 6,176	\$ 7,034	\$ 11,799
Expenses	\$ (603,531)	\$ (829,584)	\$ (862,066)	\$ (1,085,331)
Net loss for the period	\$ (595,857)	\$ (823,408)	\$ (855,032)	\$ (1,073,532)
Loss per share	\$ (0.01)	\$ (0.02)	\$ (0.02)	\$ (0.02)
Weighted average number of Shares	45,031,042	45,008,264	43,682,571	43,555,999

**Revenue:** Revenue for the quarter ended June 30, 2004 was \$47,417 compared to \$7,674 in the second quarter of 2003. Revenue for the six months ended June 30, 2004 was \$87,090 compared to \$13,850 in 2003. Revenue is mainly comprised of interest income earned on monies placed in short-term investments. The amount of interest earned is higher in 2004, compared to 2003, due to larger amounts of cash being held in short-term investment accounts as a result of the recent equity financings.

**Research and development:** Before contributions, the Company expended \$1,383,057 (2003 – \$644,866) on research and development operations in the quarter and \$2,381,255 (2003 – \$1,026,001) year-to-date. The Company is executing the customer programs contained in the various agreements it initiated during 2003 and 2004 and has therefore incurred higher costs during the period. Research and development expenses were reduced by \$773,663 (2003 – \$575,318) in the quarter, and by \$1,502,417 (2003 – \$670,555) year-to-date in respect of contributions from government assistance programs, customers and sponsors. Net research and development costs were \$609,394 (2003 – \$69,548) for the quarter and \$878,838 (2003 – \$355,446) year-to-date.

**For the quarter and six months ended June 30, 2004 compared to the quarter and six months ended June 30, 2003 and the year ended December 31, 2003**

The Company increased its engineering and technical team by 10 people during the quarter and also made use of external resources to execute its customer programs. As of June 30, 2004, the headcount is 26 (June 30, 2003 – 10). Salary and related costs were \$253,861 higher than in 2003 on a cumulative basis. Considerable effort in the quarter was concentrated on finalizing the build of the London Taxi Cab for its launch in June as well as providing support to the Canada Post demonstration project, the all-electric delivery vehicle project with LTI and the continued preparation for the Purolator and USPS projects. The Company incurred direct product development costs (including consulting and outsourced labour) of \$768,279 in the quarter (2003 – \$342,248) and \$1,372,948 year-to-date (2003 – \$391,032). As a result of the project activity, the Company has invoiced customer contributions of \$425,910 (2003 – \$30,000) in the quarter and \$898,323 (2003 – \$30,000) in the six-month period. The Company has also recorded TPC government contributions of \$347,753 (2003 – \$72,681) in the quarter and \$604,094 (2003 – \$167,918) in the six-month period. The Company is required to make royalty payments to TPC, EnCana Corporation and the National Research Council based on future revenues as described in note 13 to its annual financial statements; as the Company has no commercial revenues to date, a royalty liability has not been incurred.

**Selling and marketing:** Selling and marketing expenses were \$386,947 for the quarter ended June 30, 2004, compared to \$151,948 in the quarter ended June 30, 2003. On a cumulative basis, expenses were \$735,070 in 2004 compared to \$293,765 in 2003. In 2004, the Company has engaged advisors in Canada and the United Kingdom to help build brand recognition and promote investor liquidity, which together with higher activity levels, has resulted in marketing, advertising, and public relations expenses for the six month period being \$243,782 higher than the comparable period in 2003. The sales and marketing headcount is three (2003 – two); salary and related costs are \$147,212 higher than in 2003 on a cumulative basis.

**General and administrative:** General and administrative expenses were \$597,757 for the quarter ended June 30, 2004 compared to \$281,927 for the comparable quarter in 2003. Generally, all costs are higher in comparison to the same quarter in 2003 due to the higher activity levels in the current period, the expansion of the Company's infrastructure and expenses related to growth in its shareholder base. More specifically, salary and related costs are \$67,015 higher in the quarter ended June 30, 2004, due to the increased headcount (10 versus 5 people), and legal, regulatory filing and transfer agent's fees are \$54,190 higher due to increased corporate finance and related expenses associated with the growth in the Company's activities and shareholder base. For the six month period, general and administration expenses of \$1,114,659 are \$530,748 higher than the comparable period in 2003 mainly due to the aforementioned reasons.

**Rent and ancillary:** Rent and ancillary expenses for the quarter ended June 30, 2004 are \$110,485 (2003 – \$56,843) and for the six-months ended June 30, 2004 are \$181,828 (2003 – \$113,836). The Company has taken on additional rental commitments to support its growing operations.

**Amortization:** Amortization of property and equipment (mainly shop, computer and office equipment) and other assets (mainly patents and trade marks) was \$52,530 (2003 – \$43,265) in the quarter and \$93,244 (2003 – \$86,157) in the six-month period ended June 30, 2004. In the six-month period ended June 30, 2004, the Company acquired \$387,040 of mainly workshop/vehicle test equipment and computer hardware/software to support the increase in its headcount, the new Vancouver facility, and the implementation of an enterprise computer system. As a result, amortization costs have increased.

**Balance Sheet Discussion**

**Cash and cash equivalents:** Cash and cash equivalents at June 30, 2004 were \$10,366,435 compared to \$9,075,219 at December 31, 2003. Since December 31, 2003 the Company has increased its cash position by approximately \$4.5 million (net of costs) by way of equity infusions, including option and warrant exercises, and has applied approximately \$3.2 million to fund operations and its financing plans.

**For the quarter and six months ended June 30, 2004 compared to the quarter and six months ended June 30, 2003 and the year ended December 31, 2003**

**Accounts receivable:** Accounts receivable are \$400,368 at June 30, 2004 compared to \$337,794 at December 31, 2003. The increase is due to the increased level of activities of the Company resulting in higher levels of contributions receivable from customers, general sales taxes receivable and sundry receivables.

**Contributions receivable:** Contributions receivable at June 30, 2004, of \$602,343 represent two quarterly TPC claims waiting reimbursement whereas the balance at December 31, 2003 of \$780,459 represented amounts owing from three claims.

**Prepaid expenses:** Prepaid expenses are \$491,173 at June 30, 2004 compared to \$61,655 at December 31, 2003. Prepaid expenses have increased mainly due to advance purchases of components required for prototype and demonstration vehicle builds.

**Employee loans:** As at June 30, 2004, all employee share purchase loans were repaid (December 31, 2003 – \$91,727).

**Deferred costs:** During the quarter, the Company commenced financing activities with respect to an equity financing, a capital assurance agreement and an introduction of the Company's shares to AIM. The transactions were concluded in the third quarter of 2004. At June 30, 2004, the Company estimated it had incurred costs totalling \$815,497 in respect of these financing transactions, which costs have been deferred on the balance sheet pending closing of the transactions, at which time they will be charged to the appropriate capital account.

**Property and equipment:** Net property and equipment assets were \$482,287 at June 30, 2004 compared to \$162,048 at December 31, 2003. The increase is mainly due to the establishment of the Company's new facility in Vancouver, the implementation of a new enterprise computer system, as well as asset acquisitions in respect of the Company's recent growth in its employee base.

**Other assets:** Other assets are comprised of patent and trademark assets (as well as a deferred charge representing an unsecured employee loan that was fully amortized in 2003). The net book value of patent and trademark assets was \$102,281 at June 30, 2004 compared to \$117,279 at December 31, 2003.

**Accounts payable and accrued liabilities:** Accounts payable and accrued liabilities were \$1,265,007 at June 30, 2004 compared to \$567,692 at December 31, 2003. Liabilities are higher as at June 30, 2004 mainly due to the higher number of active customer programs and ongoing development work, including payables in respect of prototype components and build/related costs, as well as the activities required to support the Company's sales and recent financing initiatives.

**Share capital and special warrants:** Share capital at June 30, 2004 amounted to \$28,503,537 compared to \$23,991,665 at December 31, 2003. The increase in share capital is attributable to the financing completed in March 2004, for net proceeds of approximately \$3.9 million, as well as option and warrant exercises for net proceeds of approximately \$0.7 million. During the quarter, the Company issued 1,003,666 common shares in respect of various stock option and warrant exercises for net proceeds of \$535,233. In addition, the Company incurred \$146,973 in costs associated with its migration from the TSX Venture to the main board listing on the TSX Exchange. The Company completed a financing subsequent to the period end – refer to the detailed discussion in Liquidity, Capital Resources and Risk Factors below.

**For the quarter and six months ended June 30, 2004 compared to the quarter and six months ended June 30, 2003 and the year ended December 31, 2003**

The number of common shares, warrants, and options issued and outstanding are presented in the following table:

	August 9, 2004	June 30, 2004	December 31, 2003
Common shares	88,440,168	84,628,918	78,163,836
Warrants, exercisable until December 1, 2004 at \$0.62	11,966,060	11,966,060	12,691,060
Agent's compensation options, exercisable until December 1, 2004 at \$0.495	2,245,508	2,245,508	2,325,508
Warrants, exercisable until July 27, 2005 at \$1.00	1,905,625	Nil	Nil
Obligor Warrants, exercisable from December 16, 2004 until July 15, 2004 at \$1.00	1,700,000	Nil	Nil
Stock options issued under the Stock Option Plan, with expiry dates ranging up until March 22, 2009 and average exercise price of \$0.50	7,765,561	7,765,561	6,173,000

**Related Party Transactions**

During the six months ended June 30, 2004, the Company incurred costs of \$1,709 (2003 - \$7,826) in respect of administrative services provided by Vizon SciTec (formerly B.C. Research Inc.), a significant shareholder. The service agreement was terminated in February 2004. The Company also incurred costs of \$38,067 (2003 - \$74,842) in respect of leased premises and equipment provided by Vizon SciTec. The lease agreements expired in February 2004 except for the lease agreement in respect of workshop facilities and test equipment which expired on July 31, 2004.

During the six months ended June 30, 2004, the Company paid \$121,500 (2003 - \$124,167) to a company controlled by an officer/director for services rendered to the Company in his capacity as an executive officer pursuant to an employment contract.

**Liquidity, Capital Resources and Risk Factors**

At June 30, 2004 the Company had \$10,366,435 (June 30, 2003 - \$432,974) in net cash reserves. The Company invests its cash in highly liquid, highly rated financial instruments such as banker's acceptances and term deposits. Working capital was \$10,595,312 at June 30, 2004 compared to \$9,687,435 at December 31, 2003. The increase in working capital is mainly due to the increase in cash balances due to the financing completed in the first quarter of 2004, as well as the increase in prepaid expenses and is partially offset by increases in accounts payable and accrued liabilities.

The Company has no commercial revenue and is therefore dependant on its financing activities to fund its operations. The Company has raised approximately \$4.5 million (net) in new equity funds in the period since December 31, 2003, and gained access to a further \$5 million of its available TPC facility. Subsequent to June 30, 2004, on July 27, 2004, the Company announced that it had closed an equity financing and an underwriting of existing and outstanding warrants whereby the Company has secured access to an additional \$11.5 million in financing by December 15, 2004 which would satisfy the working capital requirements of the Corporation through to the end of December 2005 as well as the working capital requirements established by the London AIM as a condition of listing. Also, the financings

**For the quarter and six months ended June 30, 2004 compared to the quarter and six months ended June 30, 2003 and the year ended December 31, 2003**

will preserve the Corporation's eligibility for up to \$3.0 million of additional funding from Technology Partnerships Canada ("TPC"), subject to TPC conditions.

In accordance with the equity financing, the Company issued 3,811,250 new common shares, at a price of \$0.80 per share, for gross proceeds of \$3.0 million. In addition, the Company issued 1,905,625 warrants entitling the holders to purchase one common share of the Company at a price of \$1.00 per share up until July 27, 2005. Simultaneously, the Company entered into a Capital Assurance Agreement pursuant to which it is ensured to receive by December 15, 2004 approximately \$8.5 million which the Company could otherwise receive upon the exercise of the Corporation's outstanding common share purchase warrants and agent compensation options. The Company has issued and outstanding 11,966,060 common share purchase warrants, each purchase warrant being exercisable at a price of \$0.62 until December 1, 2004 for one Common Share, and 2,245,508 common share agent compensation options, each agent option being exercisable at a price of \$0.495 until December 1, 2004 for one Common Share (collectively the "Old Warrants"). The Company has entered into a binding agreement with a number of parties (the "Obligors") which provides that, to the extent any Old Warrants are not exercised for any reason by their expiry time on December 1, 2004, the Obligors will, on a pro rata basis, subscribe for common shares of the Company at a price of \$0.60 per share, being the weighted average exercise price of the Old Warrants. In consideration for entering into the Capital Assurance Agreement, the Obligors will collectively receive a cash fee of \$765,000 of which \$510,000 was paid on July 27, 2004 and the balance of \$255,000 is due on December 16, 2004. Ludgate Investments Limited, an investment dealer in the United Kingdom, was paid an agent's fee of \$200,000 for services rendered to the Company in connection with the Capital Assurance Agreement. In addition, the Obligors received 1,700,000 warrants (the "Obligor Warrants") of the Company. Each Obligor Warrant will permit the holder to acquire one Common Share at an exercise price of \$1.00 up until July 27, 2005. Holders of the Obligor Warrants will not be able to exercise such warrants until December 16, 2004.

The Company intends to use its cash resources and available financing arrangements to fund ongoing development activities in 2004 and into 2005. Additional financing will be required in the future, to allow for the uninterrupted development of its various products through the commercialization stage (development is anticipated to continue throughout 2005 and into the early part of 2006, with commercial sales of the Company's first product expected to occur late-2004). Never the less, the raising of financing to fund operations remains subject to uncertainty and there is no assurance that such financing will be available on commercially reasonable terms.

The Company holds substantially all of its cash at a recognized Canadian national financial institution, and as such is exposed to all of the risks associated with that institution. Pursuant to certain agreements with industry partners, the Company is to receive approximately \$494,000 in development cost contributions that are denominated in foreign currencies. As such the Company is exposed to foreign currency exchange risk.

Azure's operations are subject to all of the risks inherent in the establishment of a new business enterprise – please see Risk Factors – Annual Information Form, dated May 6, 2004 (this document is available for inspection at [www.sedar.com](http://www.sedar.com)). Management is of the view that, as a result of the recent financings, product and customer developments that risk emphasis in 2004 and 2005 will be less weighted towards financial risk and more weighted towards the practical risks of implementation, for example, the risk that Azure is delayed in the implementation of customer product requirements specified in development agreements, or the risk of delay to the process of establishing the resources required to support the implementation plans. To better manage all risk factors, the Company has embarked on a system of reporting and measuring progress towards milestones on a regular basis; has developed an organization chart commensurate with its growth plans and is actively recruiting key vacancies; and is implementing an internal control and process system – supported by a computer system that will encompass all existing engineering/support operations and provide a platform for sustainable growth. Management accepts the responsibility of ensuring that the control systems and procedures are established, effective and monitored and is required to report to the Board and its sub-committees on a regular basis.