



News Release

AZURE DYNAMICS REPORTS SECOND QUARTER 2006 RESULTS

Toronto, Ontario – July 25, 2006 – [Azure Dynamics Corporation](#) ([TSX: AZD](#) & [LSE: ADC](#)) (“Azure” or the “Company”) a leading developer of hybrid electric and electric powertrains for commercial and military vehicles, today announced its financial results for the second quarter ended June 30, 2006. The Company also provided an update on corporate and product development activities in the period.

“We are pleased with our progress this quarter and reached a major development milestone with the completion of Azure’s first commercially produced Series hybrid electric chassis,” said Campbell Deacon, Deputy Chairman and Chief Executive Officer of Azure. “Moving forward, we are well positioned to increase volume production and advance our product commercialization objectives.”

Corporate

Azure Dynamics is committed to leveraging the strategic value of its asset base to accelerate the commercialization of its technology. The Company’s Strategic Committee of the Board of Directors continues to work with Rothschild, a leading international investment bank, to help in reviewing strategic, value creation opportunities available to the Company. By gaining access to one or more industry partners the Company believes it can accelerate the commercialization of its Technology. In the execution of this strategy, the Company is leveraging its strength in the following four areas.

- Technology - Azure has developed unique electric and hybrid electric Technology and has established know-how in the commercial vehicle industry. Azure’s patents have been recognized and cited by leading companies in the automotive and electronics industries.
- Market Differentiation – Azure is operating in a world-wide niche market and has attracted high profile lead customers.
- Independent Source - Azure is one of the few independent electric and hybrid electric research, development and production companies in the world.
- People - Azure has over 80 highly trained engineers and technicians with a depth of experience unavailable in the general marketplace. Azure’s core expertise is in power electronics, controls software and vehicle system integration.

Evaluation of the Company’s options is ongoing, and the committee and Rothschild are engaged in preliminary discussions with various parties.

Product Developments

In the second quarter of 2006, the Company remained focused on deploying its proprietary technology into powertrain products for light to heavy duty commercial and military vehicles. Azure develops hybrid and electric powertrains and components for four broad vehicle

categories. Within each vehicle category, Azure leverages its powertrain designs to satisfy a broad range of vehicle applications. Significant product developments in the second quarter of 2006 included:

G1 Series (7,500 to 16,000 lbs. gross vehicle weight, "GVW")

- Completion of the first commercially produced G1 Series hybrid electric chassis. A production assembly line has been established by PCI in Union City, Indiana which is capable of handling the initial volume demand for hybrid chassis for delivery van and shuttle bus applications; and,
- Continued development of the G1 shuttle bus cab and body, as well as marketing programs for Azure's hybrid "CitiBus" shuttle bus. Azure has received orders for nine buses to date and deliveries are expected to begin in Q3, 2006; and,
- On July 18, 2006 the Company announced it has signed a Memorandum of Understanding ("MOU") for the production of hybrid shuttle buses with StarTrans, a business division of Supreme Corporation. Under the proposed terms of the MOU, Azure will provide StarTrans with hybrid cab-chassis' on which StarTrans will assemble their shuttle bus body at its manufacturing facilities in Goshen, Indiana. Azure's hybrid cab-chassis is a derivative of Azure's series hybrid chassis integrated with a newly developed cab. When fully assembled, the Azure hybrid electric shuttle bus will be compliant with the United States' Buy-America program and after testing will be eligible for the Federal Transit Administrations funding for bus purchases

P1 Parallel (10,000 – 19,000 lbs. GVW)

- Launched the first in-service P1 Parallel hybrid delivery van developed for the United States Postal Service. Azure continues to evaluate two additional P1 vehicles with a view to system design modifications required to achieve fuel economy optimization targets; and,
- Finalised the build of the AM General High-Mobility Multipurpose Vehicle integrated with a third generation Auxiliary Power Distribution System for military use. After further commissioning, the vehicle was delivered in July, 2006.

P2 Parallel (over 19,000 lbs. GVW)

- Continued the development of the second generation P2 Parallel powertrains and completed the physical build of two P2 Class 7 delivery trucks for Charmer-Sunbelt; after vehicle commissioning the vehicles are scheduled for delivery in the second half of 2006. .

E1 Electric (1,000 – 14,000 lbs. GVW)

- Received a follow-on order for 20 electric powertrain systems from Smith under the supply agreement entered in 2005; and,
- Continued collaboration with Smith in the development of an all-electric airport tug and the conversion of an OEM delivery vehicle to a full electric platform.

Components

- Continued the design, development, and testing of power electronics and drive systems components for the supply agreement with DRS Sustainment Systems, Inc. (formerly DRS Engineered Air Systems Inc.), an operating unit of DRS Technologies, Inc.; and,

- Received a follow-on order valued at CDN\$2.8 million from DRS for invertors, converters, and under-the-hood export power components. In total, the contract with DRS is now for 221 systems, which together with engineering services is valued at approximately CDN\$19 million.

Financial Results

Revenue for the quarter ended June 30, 2006 was \$1.2 million compared to \$1.5 million in the same period a year ago and \$2.4 million year-to-date compared to \$2.5 million during the same period in 2005. The decrease in revenue is attributable to decreased activities in funded engineering contracts in the US operations as focus is shifted towards the Company's core development programs. Revenue is mainly comprised of sales of components, customer engineering contracts, and after-sales service support. After considering direct and applicable indirect costs of sales, the gross margin contribution from revenue in the quarter was \$0.1 million compared to \$0.3 million in the first quarter in 2005 and \$0.4 million year-to-date compared to \$0.6 million in the same period in 2005. Gross margin as a percentage of sales was 6% for the quarter compared to 18% in the first quarter a year ago and 16% year-to-date compared to 22% in 2005. The decrease in gross margin is primarily attributable to a combination of program mix (less higher-margin engineering service work) and additional costs incurred on two development programs in the US operation.

For the quarter ended June 30, 2006, the Company incurred a net loss of \$4.9 million (\$0.03 per share) compared to a net loss of \$5.6 million (\$0.04 per share) in the first quarter of 2005. The reduced net loss in the current quarter is primarily attributable to lower operating expenses, particularly engineering and product development costs, when compared to a period of high-activity spending on the G1 program in the second quarter of 2005. As the G1 program transitions from the development phase to pre-production and production phases, spending levels have decreased. For the six months ended June 30, 2006, the Company incurred a net loss of \$9.4 million compared to \$10.5 million in the corresponding period a year ago.

Before contributions, the Company expended \$2.7 million on engineering, research and development operations in the quarter, including \$1.3 million in respect of product development costs, compared to \$4.1 million for the same period in 2005, including \$2.4 million in respect of product development costs. The expenses were reduced by \$0.4 million in respect of government and customer contributions compared to \$0.8 million in the corresponding period a year ago. For the first six months of 2006 the Company expended \$5.4 million compared to \$7.2 million during the same period in 2005, including \$2.6 million in respect of product development costs compared to \$3.7 million during the corresponding period in 2005. Contributions from the government and customers totalled \$0.7 million year-to-date compared to \$1.2 million in 2005.

The Company had cash and cash equivalents of \$10.7 million at June 30, 2006, compared to \$20.7 million at December 31, 2005 and \$12.8 million at June 30, 2005. Net cash outflows were approximately \$4.9 million in the quarter compared to \$5.9 million in the second quarter of 2005. The current year quarter included proceeds from the exercise of stock options of \$0.7 million compared to \$39,000 in the second quarter of 2005. Net cash outflows in respect of operations, working capital financing and capital expenditures were approximately \$5.6 million in the quarter compared to \$5.9 million in the second quarter of 2005.

The Company's complete 2006 second quarter Financial Statements and Management Discussion and Analysis are available at www.sedar.com or on the Company's website at

www.azuredynamics.com. The Company's financial statements for the three and six-month periods ended June 30, 2006, are attached to this press release.

About Azure Dynamics

[Azure Dynamics Corporation](http://www.azuredynamics.com) is a world leader in the development and production of hybrid electric and electric commercial and military vehicles and systems. The Company estimates it has more than 25 million miles of vehicle experience. Azure Dynamics' operations are based in North America and Europe.

Azure is currently working internationally with various partners and customers, including Purolator Courier Ltd., Canada Post, United States Postal Service, Smith Electric Vehicles, Workhorse Custom Chassis, DRS Sustainment Systems, Inc. and AM General LLC. Azure Dynamics Corporation is a public company trading on the TSX ([TSX: AZD](http://www.tsx.com)) in Canada and on the AIM ([LSE: ADC](http://www.lse.com)) in the UK.

For more Company information please visit www.azuredynamics.com.

The TSX and LSE Exchanges do not accept responsibility for the adequacy or accuracy of this release.

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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.

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Azure Dynamics Corporation
(A Development Stage Enterprise)
Consolidated Balance Sheets
(Stated in thousands)

As at	June 30 2006 (Unaudited)	December 31 2005 (Audited)	June 30 2005 (Unaudited)
	\$	\$	\$
ASSETS			
Current			
Cash and cash equivalents	10,747	20,721	12,784
Accounts receivable	1,130	1,004	1,326
Contributions receivable	639	597	1,757
Inventory and related prepayments	4,328	2,696	2,700
Prepaid expenses	1,017	980	910
	<u>17,861</u>	<u>25,998</u>	<u>19,477</u>
Restricted cash	670	698	778
Property and equipment	5,789	5,573	5,524
Other assets	44	61	61
Intangible assets, net of amortization (note 3)	11,411	12,133	12,949
Goodwill (note 3)	2,932	2,932	2,888
	<u>38,707</u>	<u>47,395</u>	<u>41,677</u>
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current			
Accounts payable and accrued liabilities	3,043	3,403	2,635
Customer deposits and deferred revenue	912	1,574	271
Current portion of notes payable (note 4)	2,427	2,558	238
	<u>6,382</u>	<u>7,535</u>	<u>3,144</u>
Long-term			
Deferred revenue	986	1,038	1,120
Notes payable	-	-	2,486
	<u>986</u>	<u>1,038</u>	<u>3,606</u>
Shareholders' equity			
Share capital (note 5)	82,178	80,701	66,184
Contributed surplus (note 5)	2,768	2,316	1,564
Deficit	(53,607)	(44,195)	(32,821)
	<u>31,339</u>	<u>38,822</u>	<u>34,927</u>
	<u>38,707</u>	<u>47,395</u>	<u>41,677</u>

Certain reclassifications have been made to the June 30 2005 comparative numbers to conform to the current period presentation

Azure Dynamics Corporation
(A Development Stage Enterprise)
Consolidated Statements of Operations and Deficit
(Stated in thousands, except per share amounts)

	For the three months ended June 30 (unaudited)		For the six months ended June 30 (unaudited)	
	2006	2005	2006	2005
Revenues	\$ 1,205	\$ 1,525	\$ 2,353	\$ 2,509
Cost of sales	1,129	1,253	1,972	1,946
Gross Margin	<u>76</u>	<u>272</u>	<u>381</u>	<u>563</u>
Expenses				
Engineering, research, development and related costs,	2,320	3,298	4,737	6,006
Selling and marketing	823	801	1,548	1,448
General and administrative	1,935	2,060	3,752	3,663
Total expenses	<u>5,078</u>	<u>6,159</u>	<u>10,037</u>	<u>11,117</u>
Loss from operations	<u>(5,002)</u>	<u>(5,887)</u>	<u>(9,656)</u>	<u>(10,554)</u>
Interest and other income, net	118	41	255	82
Foreign currency gains/(losses)	<u>38</u>	<u>246</u>	<u>(11)</u>	<u>(50)</u>
Net loss for the period	<u>(4,846)</u>	<u>(5,600)</u>	<u>(9,412)</u>	<u>(10,522)</u>
Deficit, beginning of period	<u>(48,761)</u>	<u>(27,221)</u>	<u>(44,195)</u>	<u>(22,299)</u>
Deficit, end of period	<u>(53,607)</u>	<u>(32,821)</u>	<u>(53,607)</u>	<u>(32,821)</u>
Loss per share - basic	<u>(0.03)</u>	<u>(0.04)</u>	<u>(0.06)</u>	<u>(0.08)</u>
Weighted average number of shares - basic *	158,638	141,203	157,569	133,095

* No fully diluted earnings per share have been disclosed, as these would be anti dilutive.

Azure Dynamics Corporation
(A Development Stage Enterprise)
Consolidated Statements of Cash Flows
(Stated in thousands)

	For the three months ended June 30 (unaudited)		For the six months ended June 30 (unaudited)	
	2006	2005	2006	2005
	\$	\$	\$	\$
Cash flows from operating activities				
Net loss for the period	(4,846)	(5,600)	(9,412)	(10,522)
Adjustments for:				
Amortization of property and equipment and other assets	193	193	386	337
Amortization of intangible assets	408	425	808	708
Unrealized foreign currency gains/(losses)	387	(192)	170	68
Stock option compensation expense	214	342	639	848
	<u>(3,644)</u>	<u>(4,832)</u>	<u>(7,409)</u>	<u>(8,561)</u>
Changes in non-cash working capital items	(1,110)	(878)	(2,873)	(3,812)
Movement due to exchange impact	(43)	(33)	(39)	(32)
	<u>(1,153)</u>	<u>(911)</u>	<u>(2,912)</u>	<u>(3,844)</u>
Total Cash flows from operating activities	<u>(4,797)</u>	<u>(5,743)</u>	<u>(10,321)</u>	<u>(12,405)</u>
Cash flows from financing activities				
Issuance of common shares (net of costs)	673	39	1,290	11,789
Principle payments on notes payable	(14)	-	(28)	(15)
Movement due to exchange impact	(113)	(35)	(103)	(35)
Total Cash flows from financing activities	<u>546</u>	<u>4</u>	<u>1,159</u>	<u>11,739</u>
Cash flows from investing activities				
Acquisition of property and equipment	(367)	(165)	(601)	(456)
Acquisition of other assets	(54)	57	(69)	(39)
Changes in Restricted Cash	-	(13)	-	409
Movement due to exchange impact	(267)	-	(204)	-
Total Cash flows from investing activities	<u>(688)</u>	<u>(121)</u>	<u>(874)</u>	<u>(86)</u>
Decrease in cash and cash equivalents	(4,939)	(5,860)	(10,036)	(752)
Exchange Impact on Cash Held in Foreign Currency	(89)	177	62	1
Cash and cash equivalents, beginning of period	15,775	18,467	20,721	13,535
Cash and cash equivalents, end of period	<u>10,747</u>	<u>12,784</u>	<u>10,747</u>	<u>12,784</u>

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