



First Quarter  
Interim Report 2009  
AirBoss of  
America Corp.





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# AirBoss of America Operations

AirBoss of America Corp. is one of North America's largest custom compounding companies. We develop, manufacture, and sell high-quality proprietary rubber-based products offering enhanced performance and productivity to transportation, defence and industrial markets. AirBoss has a capacity to supply 250 million pounds of rubber annually to a diverse group of rubber manufacturers. We are dedicated to unequalled excellence in the manufacturing of our high performance proprietary rubber-based products by providing the stability, ingenuity and capability our customers demand.

#### Rubber Compounding

Manufactures custom compounds from natural and synthetic rubber gum, binding agents, and chemicals. Uses state of the art equipment, technical staff, and strong customer focus to achieve consistent on-time service customers can depend on.

#### Military and Industrial Products

Manufacturer of protective wear for military and first response applications. Manufactures extruded, calendered, cushion gum, and compression moulded rubber products.

# To Our Shareholders

Sales for the three-month period were \$53.1 million and earnings before interest and tax equalled \$1.1 million. The results were led by a strong performance by defense products group.

## **AirBoss-Defense**

Gross sales for the quarter ending March 31, 2009 increased by 34% over the same period in 2008 while divisional earnings before interest and tax increased by over 180%. These positive results were due to increases in sales volume for our CBRN footwear and gloves, a favourable product mix and the change in the US dollar exchange rate.

The Company anticipates this increased sales volume to continue for the remainder of the year and into 2010 and is in the process of adding production capacity to remove sales constraints. When complete, this will entail additional injection molding equipment which will be situated in the United States. This will not likely be in place until the end of the year; however, we hope to increase capacity by the end of the 3rd quarter with the delivery of additional glove and footwear molds. In April, we went to 3 shifts per day, 7 days a week from 5 days a week on glove production.

A significant portion of the sales of our military protective wear are billed in US dollars and the exchange rate has an important impact on profitability given the magnitude of the trends. Accordingly, in order to hedge existing contracts and anticipated US dollar orders, the Company has sold US dollars forward maturing at various times in the year to correspond with the estimated net excess of US dollar collections over expenditures for the entire year.

## **AirBoss Rubber Compounding**

The effect of the economy negatively impacted virtually all industrial sectors serviced by the Company in the first quarter. This was an industry wide phenomenon forcing everyone to reduce production levels so as to compensate for poor demand. Sales were down by 16% and margins were non-existent due to the negative impact of the high raw material prices of 2008 ending inventory being consumed. The low-point in volume was reached in February and demand has been increasing steadily ever since. We expect volumes to return to acceptable levels mid-way through the second quarter.

**Outlook**

AirBoss-Defense military protective wear business orders and sales are progressing as expected, and the business is headed for another record year for sales and divisional profits. The Company expects this to continue throughout 2010 and is finalizing plans to add capacity located in the US to support this surge.

The economic downturn that has affected the rubber industry has also impacted our rubber compounding business. Volumes are beginning to show signs of significant recovery and the division should have consumed most of the high priced raw materials by the end of April, thus enabling margin recovery. AirBoss only has a slight exposure to the automotive industry and as a result, is optimistic of being amongst the first to resume normal activity levels.

The currency hedging program will help to lock in the profits of AirBoss-Defense at an exchange rate of \$1.22. While this program shows a non-cash loss of \$647,000 for the 3 months ended March 31, 2009, this becomes a \$800,000 profit using April 30, 2009 exchange rates and significantly higher profit at current market rates.

Given the improved performance of the defense business, management is optimistic of achieving similar EBITDA results as in 2008.



**P.G. Schoch**  
Chairman



**R.L. Hagerman**  
President and CEO

## Management's Discussion and Analysis of Financial Condition and Results of Operations

The following Management's Discussion and Analysis of Financial Condition and Results of Operations of AirBoss of America Corp. ("AirBoss" as the "Company") for the three-month period ended March 31, 2009 has been prepared as of May 12, 2009 and should be read in conjunction with the Unaudited Consolidated Financial Statements and Notes prepared in accordance with Canadian generally accepted accounting principles. The quarterly consolidated financial statements and any amounts shown in this MD&A were not reviewed or audited by our external auditors. All tabular dollar amounts are shown in thousands of Canadian dollars unless otherwise specified. Additional information regarding the Company, including its Annual Information Form, can be found at SEDAR at [www.sedar.com](http://www.sedar.com) and at the Company's website at [www.airbossofamerica.com](http://www.airbossofamerica.com).

**Forward-Looking Statements** – Certain statements included herein, including those that express management's expectations or estimates of future developments or AirBoss' future performance, constitute "forward-looking statements" within the meaning of applicable securities laws. Words such as "may", "could" "expects", "anticipates", "forecasts", "plans", "intends" or similar expressions are intended to identify forward-looking statements.

Forward-looking statements are necessarily based upon a number of estimates and assumptions that, while considered reasonable by management at the time the statements are made, are inherently subject to significant business, economic and competitive uncertainties and contingencies. AirBoss cautions that such forward-looking statements involve known and unknown risks, uncertainties and other risks that may cause AirBoss' actual financial results, performance, or achievements to be materially different from its estimated future results, performance or achievements expressed or implied by those forward-looking statements. Numerous factors could cause actual results to differ materially from those in the forward-looking statements, including without limitation: changes in accounting policies and methods including uncertainties associated with critical accounting assumptions and estimates; AirBoss' ability to maintain existing customers or develop new customers in light of increased competition; cyclical trends in the tire and automotive, construction, mining, retail and rail transportation industries; sufficient availability of raw materials at economical costs; weather conditions affecting raw materials, production and sales; potential product liability and warranty claims; its dependence on key customers; equipment malfunction; changes in the value of the Canadian dollar relative to the US dollar; ability to obtain financing on acceptable terms; environmental damage caused by it and non-compliance with environmental laws and regulations; changes in tax laws, and potential litigation.

This list is not exhaustive of the factors that may affect any of AirBoss' forward-looking statements. Investors are cautioned not to put undue reliance on forward-looking statements. All subsequent written and oral forward-looking statements attributable to AirBoss or persons acting on its behalf are expressly qualified in their entirety by this notice. Whether as a result of new information, future events or otherwise, AirBoss disclaims any intent or obligation to update publicly these forward-looking statements. Risks and uncertainties about AirBoss' business are more fully discussed under the heading "Risk Factors" section of the Company's annual report on pages 21 to 23.

### Highlights

The current economic environment continues to impact sales and profitability of our rubber compounding business which has been negatively impacted by uncertainty in demand, commodity prices and the effect the economic downturn has had on its customers. In spite of these conditions and in part due to the significant increase in profitability of our defense products we have remained profitable and reduced our borrowing requirements.

We continue to seek out new markets, product offerings, operational efficiency and acquisition opportunities to mitigate this economic risk and enhance shareholder value. We will continue to monitor our policies and procedures with respect to granting credit and we will manage our capital expenditures and working capital to further improve our liquidity position.

On January 1, 2009, we adopted handbook section 3064, "Goodwill and intangible assets." The revised standard establishes guidance for the recognition, measurement and disclosure of goodwill and intangible assets, including internally generated intangible assets. As required by this standard, we have retroactively reclassified \$0.5 million of computer software costs from capital assets to other assets as well as adjusted opening retained earnings by \$0.7 million to expense start-up costs when these were incurred.

## MD&amp;A (cont'd)

**Selected Financial Information**

- 34% sales increase in AEP due to AirBoss-Defense sales
- Other markets affected by US dollar and softening economy
- Margins improved by \$0.9 million from a weakening Canadian dollar

Three months ended March 31

(\$ thousands, except per share amount)

	2009	2008
<b>Financial results:</b>		
Net sales	53,085	55,134
Net income	422	998
Net income per share		
- Basic and Diluted	0.02	0.04
EBITDA (non-GAAP financial measure)	2,338	3,497
Operating cash flow provided by (used) in operations	5,159	1,551
Capital expenditures	1,050	571

(\$ thousands)

March 31, 2009

December 31, 2008

**Financial Position:**

Total assets	132,979	156,292
Demand loan	11,513	17,788
Term loan and other debt	27,880	28,060
Shareholders' Equity	65,727	65,166
Outstanding shares	23,805	23,805

**Non-GAAP Financial measure**

This MD&A is based on reported income in accordance with Canadian generally accepted accounting principles ("GAAP") and on the following non-GAAP financial measure, from continuing operations:

EBITDA Earnings before financing income, financing expense, income taxes and depreciation and amortization

This non-GAAP measure is directly derived from the interim consolidated financial statements, but do not have a standardized meaning prescribed by GAAP and is not necessarily comparable to similar measures presented by other issuers. The Company discloses EBITDA, a financial measurement used by interested parties and investors to monitor the ability of an issuer to generate cash from operations for debt service, financing working capital and capital expenditures and pay dividends. EBITDA is not a measure of performance under GAAP and should not be considered in isolation or as a substitute for net income under GAAP.

**A reconciliation of this measure, is presented below:**

Three months ended March 31

(\$ thousands)

	2009	2008
<b>EBITDA:</b>		
Income before income taxes	660	1,579
Net financing interest expense	524	707
Depreciation and amortization	1,154	1,211
EBITDA	2,338	3,497

## MD&amp;A (cont'd)

## RESULTS OF OPERATIONS

## NET SALES

Sales revenues decreased 3.7% primarily from lower volumes in the compounding segment. The reduction in sales was mitigated by higher sales volumes in AirBoss-Defense. The weaker Canadian dollar had a favorable impact on US dollar denominated sales compared to the same period last year. The average exchange rate this year was 1.24 compared to 1.00 in the first quarter of last year.

(\$ thousands)		Rubber Compounding Operations	AEP & Other	Total
Net sales	<b>2009</b>	<b>34,624</b>	<b>18,461</b>	<b>53,085</b>
	2008	41,383	13,751	55,134
Increase (decrease) \$		(6,759)	4,710	(2,049)
Increase (decrease) %		(16.3)%	34.3%	(3.7)%

## Rubber Compounding

Sales decreased by 16% compared to the same period in 2008 despite higher pricing in the first half of the quarter. Volume decreases were experienced across all sectors. This decrease in demand was an industry-wide phenomenon and was accompanied by rapidly declining sales prices throughout the quarter. February represented the sales low and volumes have been increasing thereafter. The Company has less than 10% of its customer base supplying the automotive sector and therefore expects demand to return to acceptable levels by mid-to-late second quarter 2009.

## AirBoss Engineered Products

AirBoss-Defense sales have increased by \$3.2 million due to the increased unit sales of Chemical, Biological, Radiological and Nuclear ("CBRN") protective hand and footwear. While sales prices were mainly fixed, in accordance with long term contracts, the increase in the US dollar further increased sales denominated in Canadian dollars. This increase in demand is expected to continue for the remainder of this year and 2010. The Company has increased capacity for the second quarter by extending production to 3 shifts, seven days a week on certain products and plans to open a second US based injection molding facility which will be operational by early 2010.

Industrial sales volume was up 24% mainly due to higher raw material costs. As costs drop sales prices will return to 2007 levels. This will impact second quarter sales. This division does not have a material exposure to the automotive industry and although some continuing demand slump is expected it is not anticipated to be as severe or as long lived.

## GROSS MARGIN

Gross margin for the quarter ended March 31, 2009 and 2008 was \$5.0 million. This was impacted by higher raw material costs, the weakening of the Canadian dollar and higher Defense sales.

(\$ thousands)		Rubber Compounding Operations	AEP & Other	Total
Gross Margin	<b>2009</b>	<b>691</b>	<b>4,290</b>	<b>4,981</b>
	2008	2,542	2,460	5,002
Increase (decrease) \$		(1,851)	1,830	(21)
% net of sales	<b>2009</b>	<b>2.0</b>	<b>23.2</b>	<b>9.4</b>
	2008	6.1	17.9	9.1

## Rubber Compounding

In Q4 2008, ARC incurred a significant write-down certain key raw materials to net realizable value. This was necessary due to falling sales prices precipitating by lower market prices for raw materials. Although the segment generated a modest gross margin during Q1 2009, none was generated in its compounding activities. A majority of the high priced 2008 purchased raw material was consumed in the quarter and we estimate that, except for a limited number of materials it should be totally eliminated by the end of April. The positive margins generated were as a result of chemical product sales and exchange gains which are inventory hedging losses classified in other income.

## AirBoss Engineered Products

The increased sales volumes in the Defense division improved efficiency and overhead absorption. Combined with the increase in the US dollar, these factors accounted for the increased gross margins in the first quarter.

## MD&amp;A (cont'd)

## OPERATING EXPENSES

(\$ thousands)		Rubber Compounding Operations	AEP & Other	Unallocated Corporate Costs	Total
Operating expenses	<b>2009</b>	<b>1,566</b>	<b>1,148</b>	<b>612</b>	<b>3,326</b>
	2008	1,446	1,249	472	3,167
Increase (decrease) \$		120	(101)	140	159
% net of sales	<b>2009</b>	<b>4.5</b>	<b>6.2</b>	<b>N/A</b>	<b>6.3</b>
	2008	3.5	9.1	N/A	5.7

**Rubber Compounding**

Sales and marketing costs increased \$0.1 million relating to efforts to increase market share.

**AirBoss Engineered Products**

AEP operating costs reflect \$0.1 million lower product development costs compared to the first quarter of last year. 2008 included costs associated with a mask project.

**Unallocated Corporate Costs**

Unallocated corporate costs increased as a result of salary and bonus increases of \$0.1 million and higher statutory compliance costs in the quarter compared to the same quarter last year.

## INTEREST, FOREIGN EXCHANGE AND OTHER INCOME

(\$ thousands)		Rubber Compounding Operations	AEP & Other	Unallocated Corporate Costs	Total
Interest, FX & Other Income	<b>2009</b>	<b>467</b>	<b>(49)</b>	<b>577</b>	<b>995</b>
	2008	925	73	(742)	256
Increase (decrease) \$		(458)	(122)	1,319	739
% net of sales	<b>2009</b>	<b>1.3</b>	<b>(0.3)</b>	<b>N/A</b>	<b>1.9</b>
	2008	2.2	0.5	N/A	0.5

Interest expense for the three months ended March 31, 2009 was \$0.5 million compared to \$0.7 million for the same period in 2008. Most of this decrease is due to lower interest rates, however, the Company anticipates borrowing levels will be significantly reduced from the prior year due to deflation in rubber raw materials which will result in lower working capital requirements.

Each quarter, we incur unrealized foreign exchange gains and losses on the translation of foreign currency denominated asset and liability balances including forward contracts. The amount fluctuates from quarter to quarter and is dependent on exchange rates and the value of the net foreign assets or liabilities on hand. There was an exchange loss of \$0.6 million in the current quarter compared to an exchange gain of \$0.3 million in 2008. To mitigate foreign exchange gains and losses, the Company uses a combination of US dollar denominated debt and forward sales of US dollars to hedge its net foreign currency balance sheet position. In addition, the Company establishes cash-flow hedges and sells forward its expected net US dollar receipts for the year when they are reasonably predictable, such as with the Defense division. As at March 31, 2009, the Company held forward contracts to sell US dollars prior to year end totaling US \$24 million at an average rate of approximately CAD \$1.22. These have been adjusted to market, resulting in a translation loss at March 31, 2009 of \$0.4 million. These same contracts translated at the April month end rate, would have resulted in a gain of approximately \$0.8 million.

**INCOME TAX EXPENSE**

We conduct business operation in the US and in Canada. Each jurisdiction is subject to different tax rates and the Company's effective tax rate varies quarter to quarter depending on the mix and volume of business in each jurisdiction as well as the impact of incentives, non-tax-deductible expenses, and the resolution of prior period tax assessments.

The Company recorded an income tax expense of \$0.2 million or an effective income tax rate for the quarter of 34.0% (38.9% in 2008). The primary factor contributing to a higher effective tax rate in 2008 was \$0.2 million of non-tax-deductible foreign exchange translation losses incurred in the US entities.

**NON-CONTROLLING INTEREST**

Non-controlling interest increased by \$0.0 million representing its share of net income for the quarter.

**NET INCOME AND EARNINGS PER SHARE**

Net income in Q1 2009 amounted to \$0.4 million and \$1.0 million in 2008. The basic and fully diluted earnings per share in the quarter were \$0.02 (2008-\$0.04) based on basic and fully diluted shares outstanding 23,805.

## MD&amp;A (cont'd)

**QUARTERLY INFORMATION**

(\$ thousands except per share amounts)

Quarter Ended	Net Sales	Net Income (Loss)		Net Income (Loss) Continuing Operations per share		Net Income (Loss) per share	
		Continuing	Total	Basic	Diluted	Basic	Diluted
March 31, 2009	53,085	469	422	0.02	0.02	0.02	0.02
December 31, 2008	74,008	(6,949)	(6,756)	(0.29)	(0.29)	(0.28)	(0.28)
September 30, 2008	65,467	2,133	2,080	0.09	0.09	0.09	0.09
June 30, 2008	64,805	2,547	2,771	0.11	0.11	0.12	0.12
March 31, 2008	55,134	962	998	0.04	0.04	0.04	0.04
December 31, 2007	48,758	1,177	993	0.05	0.05	0.04	0.04
September 30, 2007	50,943	825	1,199	0.03	0.03	0.05	0.05
June 30, 2007	54,510	876	913	0.04	0.04	0.04	0.04

**Items impacting comparability of quarters**

- The first quarter of 2009 was impacted by lower volumes and high raw material costs in the compounding segment.
- The fourth quarter of 2008 reflected a goodwill impairment charge of \$7.9 million.
- The fourth quarter of 2007 included \$0.7 million reduction of corporate taxes.

**LIQUIDITY AND CAPITAL RESOURCES****Cash flows from operations**

AirBoss generated \$2.3 million in operating cash flows before changes in working capital in the first quarter of 2009 and 2008. Q1 2009 reflected lower net income offset by comparable non-cash items.

**Non-cash working capital**

The investment in non-cash working capital relating to continuing operations decreased by \$4.1 million in the quarter as follows:

Accounts receivable decreased by \$5 million due to:

- Rubber Compounding receivables decreased by \$6.0 million from lower volumes and pricing.
- AEP receivables increased \$1.0 million from higher defense sales
- DSO improved by 10 days since December, 2008 and 5 days compared to March, 2008

Inventories decreased by \$14.9 million due to the timing of receipts:

- Rubber Compounding inventory decreased \$13.6 million by drawing down inventory on hand from December and restricting purchases. The segment is developing a lean approach to its inventory management which should lead to lower levels on hand.
- AEP decreased its inventory by \$1.3 million

Accounts payable decreased by \$13.1 million from lower inventory purchases:

- Rubber Compounding \$11.8 million
- AEP \$0.7 million
- Head office \$0.6 million

During the first quarter of 2009, the Company had made a final income tax remittance of \$2.9 million for the 2008 fiscal year relating to its Canadian operations.

**Capital expenditures**

Capital expenditures for the quarter ended March 31, 2009 were \$1.0 million compared to \$0.6 million in 2008. In 2009, the spending was as follows:

- Rubber Compounding spent \$0.4 million relating to reconfiguring its downstream mills
- AEP incurred \$0.5 million for manufacturing equipment including enhancements to an extruder for the industrial business and packaging and footwear equipment to support higher volumes

## MD&amp;A (cont'd)

**Other assets**

During the first quarter of 2009, all the funds in escrow were released. Rubber compounding spent \$0.2 million relating to system integration and enhancement initiatives.

**Financing**

At March 31, 2009, the Company has drawn \$9.4 million (2008 - \$21.0 million) against its \$35 million (2008 - \$45 million) operating line facility.

Under the term debt facility, the Company had made its required principal repayments of \$0.4 million (2008 - \$0.3 million).

\$0.6 million of dividends were paid out in the quarter.

The Company expects to fund its 2009 operating cash requirements, including required working capital investments, capital expenditures, and scheduled debt repayments from cash on hand, cash flow from operations and committed borrowing capacity.

**Commitments and contractual obligations**

The Company's contractual obligations as at December 31, 2008 are described on page 19 in the Management's Discussion and Analysis of Company's 2008 Annual Report. For the three-month period ended March 31, 2009, the Company did not enter into any material contractual obligations outside the normal course of business.

Purchase obligations include enforceable and legally binding commitments to purchase raw materials, services and capital expenditures in the normal course of business. Capital expenditures can be financed with additional drawings against a term facility.

**Forward exchange contracts**

At March 31, 2009, the Company has forward contracts to sell US \$24 million for CAD \$29.3 million to December 31, 2009.

**TRANSACTIONS WITH RELATED PARTIES**

The Company rents corporate office space from a company controlled by the Chairman of the Company. This lease provides for an annual rental of \$90,000 payable monthly and expires in August 2012. The lease provides for the purchase of the building should certain events occur which are beyond the control of the Chairman. The annual rental of \$90,000 approximated the fair market rental at the inception of the lease in 2002. The rent paid in the first quarter was \$22,500 (\$22,500 in 2008).

During the first quarter, the Company paid monthly dues relating to a facility in South Carolina of approximately \$4,000 (\$3,000 in 2008) to a company in which the Chairman is an officer.

The Company provided a \$0.1 million share purchase loan in 2006 to an employee due June 15, 2009 bearing interest at 5% annually with full recourse and is included in the financial statements under the caption "other assets".

**CHANGES IN ACCOUNTING POLICIES**

Commencing January 1, 2009, the Company adopted new accounting standards issued by the Canadian Institute of Chartered Accountants (the "CICA") as follows:

**Fair value of financial assets and financial liabilities**

On January 20, 2009, the CICA published EIC-173, entitled Credit Risk and the Fair Value of Financial Assets and Financial Liabilities, which provides further information on the determination of the fair value of financial assets and financial liabilities under Section 3855, entitled Financial Instruments – Recognition and Measurement. This EIC states that an entity's own credit and the credit risk of the counter-party should be taken into account in determining the fair value of financial assets and financial liabilities, including derivative instruments. This recommendation should be applied retrospectively without restatement of prior periods to all financial assets and liabilities measured at fair value in interim and annual financial statements for periods ending on or after the date of issuance of the Abstract, that is January 20, 2009.

The standard is applicable to the Company for the first quarter of 2009 and has had no material impact on the results.

**Goodwill and intangible assets**

In February 2008, the CICA issued Handbook Section 3064, Goodwill and Intangible Assets. Section 3064 states that upon their initial identification, intangible assets are to be recognized as assets if they meet the definition of an intangible asset and if they satisfy the recognition criteria contained in the Handbook section. This section also provides further information on the recognition of internally generated intangible assets (including research and development costs).

Section 3064 carries forward the requirements of the old Section 3062, Goodwill and Other Intangible Assets with regards to the subsequent measurement of intangible assets, goodwill, and disclosure. The new section will become effective on January 1, 2009 for the Company.

The standard is applicable to the Company for the first quarter of 2009 and the Company retroactively expensed start-up costs.

**International Financial Reporting Standards**

On February 13, 2008, the Canadian Accounting Standards Board confirmed that International Financial Reporting Standards will replace Canada's current generally accepted accounting principles for publicly accountable profit-oriented enterprises for interim and annual financial statements effective January 1, 2011. The Company is evaluating the effects of adopting this standard.

## Management's Responsibility for Financial Reporting

### CHANGES IN INTERNAL CONTROLS OVER FINANCIAL REPORTING

During the most recent interim period, there have been no changes in the Company's policies and procedures and other processes that comprise its internal control over financial reporting, that have materially affected, or are reasonably likely to materially affect, the Company's internal control over financial reporting.

### OUTLOOK

AirBoss-Defense military protective wear business orders and sales are progressing as expected and the business is headed for another record sales and divisional profit for the year. The Company expects this to continue throughout 2010 and is finalizing plans to add capacity in the US to support this surge.

The economic downturn that has affected the rubber industry has also impacted our rubber compounding business. Volumes are beginning to show signs of significant recovery and the division should have consumed most of the high priced raw materials by the end of April thus enabling margin recovery. AirBoss only has a slight exposure to the automotive industry and as a result is optimistic of being amongst the first to resume normal activity levels.

We remain optimistic of achieving similar operating results, prior to goodwill adjustments, in 2009 as in 2008 although it will most certainly be led by our defense business. This will require a stabilizing of commodity prices and a return to more usual compounding volumes later in the second half of the year.



**R.L. Hagerman**  
President and Chief Executive Officer



**S.W. Richards**  
Vice-President Finance and CFO

## Notice of Disclosure of Non-Auditor Review of Interim Financial Statements

For the three month periods ended March 31, 2009 and 2008

Pursuant to Ontario Securities Legislation's National Instrument 51-102, Part 4, subsection 4.3(3)(a), if an auditor has not performed a review of the interim financial statements, the interim financial statements must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

The accompanying unaudited interim consolidated financial statements of the Company for the interim periods ended March 31, 2009 and 2008, have been prepared in accordance with Canadian generally accepted accounting principles and are the responsibility of the Company's management.

The Company's independent auditors, KPMG LLP, have not performed a review of these interim consolidated financial statements in accordance with the standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

Dated this 12th day of May, 2009.

## Consolidated Balance Sheets

(thousands \$ CDN)	March 31, 2009	December 31, 2008
	(unaudited)	(restated note 2)
<b>ASSETS</b>		
<b>Current assets:</b>		
Accounts receivable	\$ 26,949	\$ 31,864
Inventories	37,980	52,849
Prepaid expenses	332	637
Income taxes receivable	322	-
Total current assets	65,583	85,350
Capital assets	53,299	53,362
Goodwill	7,182	7,182
Future income tax assets	6,195	6,105
Other assets	720	4,293
Total assets	\$ 132,979	\$ 156,292
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current liabilities:</b>		
Demand loan	\$ 11,513	\$ 17,788
Accounts payable and accrued liabilities	15,175	28,301
Income taxes payable	-	2,503
Dividends payable	-	596
Current liabilities of discontinued operations	1,110	2,409
Current portion of term loan and other debt	1,526	1,513
Total current liabilities	29,324	53,110
Term loan and other debt	26,354	26,547
Future income tax liabilities	9,234	9,202
Accrued post retirement benefit liability	2,340	2,267
Total liabilities	67,252	91,126
<i>Commitments (Note 5)</i>		
<b>Shareholders' equity:</b>		
Share capital	40,537	40,537
Non-controlling interest	47	-
Contributed surplus	2,003	1,911
Accumulated other comprehensive loss	-	-
Retained earnings	23,140	22,718
Total shareholders' equity	65,727	65,166
Total liabilities and shareholders' equity	\$ 132,979	\$ 156,292

See accompanying notes to consolidated financial statements.

On behalf of the Board



**Robert L. Hagerman**  
Director



**Robert L. McLeish**  
Director

## Consolidated Statements of Income and Retained Earnings

(unaudited) (thousands \$ CDN, except per share amounts)

For the three-month periods ended March 31

	2009	2008
<b>NET SALES</b>	<b>\$ 53,085</b>	<b>\$ 55,134</b>
Cost of sales	48,104	50,132
Gross margin	4,981	5,002
<b>OPERATING EXPENSES</b>		
General and administrative	2,092	1,919
Selling, marketing and distribution	996	954
Product research	238	294
Total operating expenses	3,326	3,167
Income from continuing operations before undernoted items	1,655	1,835
Other income (expense)	(471)	451
Income from continuing operations before interest expense	1,184	2,286
Interest expense	(524)	(707)
Income from continuing operations before income taxes	660	1,579
Provision for income taxes	(191)	(617)
Net income before discontinued operations and non-controlling interest	469	962
Income from discontinued operations	-	36
Net income attributable to non-controlling interest	(47)	-
Net income	422	998
Retained earnings, beginning of year	23,245	25,522
Change in accounting policy related to goodwill and intangible assets (Note 2)	(527)	(704)
Retained earnings, end of year	\$ 23,140	\$ 25,816
Net income per share		
- Basic and Diluted	\$ 0.02	\$ 0.04

See accompanying notes to consolidated financial statements.

## Consolidated Statements of Comprehensive Income and Accumulated Other Comprehensive Income

(unaudited) (thousands \$ CDN)

For the three-month periods ended March 31

	2009	2008
Net Income	\$ 422	\$ 998
Other comprehensive income (loss) - net of income tax	-	111
Comprehensive income	\$ 422	\$ 1,109
Accumulated other comprehensive loss, beginning of period	\$ -	\$ (823)
Accumulated other comprehensive income (loss) - net of income tax	-	111
Accumulated other comprehensive loss, end of period	\$ -	\$ (712)

See accompanying notes to consolidated financial statements.

## Consolidated Statements of Cash Flows

(unaudited) (thousands \$ CDN)

For the three-month periods ended March 31

	2009	2008
<b>CASH PROVIDED BY (USED IN):</b>		
<b>Operating Activities:</b>		
Net income from continuing operations	\$ 422	\$ 962
Items not affecting cash:		
Amortization	1,154	1,211
Future income taxes	(58)	(288)
Net income attributable to non-controlling interest	47	18
Foreign exchange loss	588	225
Options expense	92	64
Post-retirement benefits expense	73	74
	<b>2,318</b>	<b>2,266</b>
Changes in non-cash operating working capital balances	<b>4,140</b>	<b>288</b>
Net cash provided by continuing operations	<b>6,458</b>	<b>2,554</b>
Net cash used in discontinued operations	<b>(1,299)</b>	<b>(1,003)</b>
Cash provided by operating activities	<b>5,159</b>	<b>1,551</b>
<b>Investing Activities:</b>		
Purchase of capital assets	<b>(1,050)</b>	<b>(571)</b>
Purchase of other assets	<b>(175)</b>	<b>(154)</b>
Proceeds of disposal of other assets	<b>3,292</b>	<b>-</b>
Cash provided by (used in) investing activities	<b>2,067</b>	<b>(725)</b>
<b>Financing Activities:</b>		
Net increase (decrease) in demand loan	<b>(6,275)</b>	<b>83</b>
Repayment of term loan	<b>(355)</b>	<b>(314)</b>
Dividends paid	<b>(596)</b>	<b>(595)</b>
Cash used in financing activities	<b>(7,226)</b>	<b>(826)</b>
Increase (decrease) in cash during the period	<b>-</b>	<b>-</b>
Cash and short-term deposits at the beginning of the period	<b>-</b>	<b>-</b>
Cash and short-term deposits at the end of the period	<b>\$ -</b>	<b>\$ -</b>
<b>Supplementary Cash Flow Information:</b>		
Cash Interest paid	<b>\$ 480</b>	<b>\$ 840</b>
Cash income taxes remitted	<b>3,434</b>	<b>429</b>

See accompanying notes to consolidated financial statements.

## Notes to Consolidated Financial Statements

Three months ended March 31, 2009 and 2008

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

### NOTE 1 SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

#### Basis of Presentation

These unaudited interim consolidated financial statements include the accounts of the Company and its wholly owned subsidiaries (collectively, the "Company"). Intercompany balances and transactions have been eliminated upon consolidation. The unaudited interim consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles for financial statements, except that certain disclosures required for annual financial statements have not been included. Accordingly, these interim consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements for the year ended December 31, 2008, except as noted below. The unaudited interim consolidated financial statements have been prepared on a basis consistent with the policies set out in the Company's consolidated annual financial statements for fiscal 2008, except as described in note 2.

#### Seasonality

The Company is affected by seasonal factors in that rubber compounding volumes are lower in the first and fourth quarter.

### NOTE 2 CHANGES IN ACCOUNTING POLICIES

Commencing January 1, 2009, the Company adopted new accounting standards issued by the Canadian Institute of Chartered Accountants (the "CICA") as follows:

#### Fair value of financial assets and financial liabilities

On January 20, 2009, the CICA published EIC-173, entitled Credit Risk and the Fair Value of Financial Assets and Financial Liabilities, which provides further information on the determination of the fair value of financial assets and financial liabilities under Section 3855, entitled Financial Instruments – Recognition and Measurement. This EIC states that an entity's own credit and the credit risk of the counter-party should be taken into account in determining the fair value of financial assets and financial liabilities including derivative instruments. This recommendation should be applied retrospectively without restatement of prior periods to all financial assets and liabilities measured at fair value in interim and annual financial statements for periods ending on or after the date of issuance of the Abstract, that is January 20, 2009.

The standard is applicable to the Company for the first quarter of 2009 and has had no material impact on the results.

#### Goodwill and intangible assets

In February 2008, the CICA issued Handbook Section 3064, Goodwill and Intangible Assets. Section 3064 states that upon their initial identification, intangible assets are to be recognized as assets if they meet the definition of an intangible asset and if they satisfy the recognition criteria contained in the Handbook section. This section also provides further information on the recognition of internally generated intangible assets (including research and development costs).

Section 3064 carries forward the requirements of the old Section 3062, Goodwill and Other Intangible Assets with regards to the subsequent measurement of intangible assets, goodwill, and disclosure. The new section will become effective on January 1, 2009 for the Company.

This new standard is effective for the Company's interim and annual consolidated financial statements commencing January 1, 2009 and was applied retrospectively, with restatement of prior periods. The adoption of CICA 3064 resulted in a \$1.1 million decrease in other assets relating to pre-operating costs, \$0.4 million decrease in future income tax liabilities and \$0.7 million decrease in retained earnings. As well, \$0.7 million of software costs and \$0.2 million of accumulated depreciation was reclassified to other assets.

### RECENTLY ISSUED ACCOUNTING PRONOUNCEMENTS

#### International Financial Reporting Standards

On February 13, 2008, the Canadian Accounting Standards Board confirmed that International Financial Reporting Standards will replace Canada's current generally accepted accounting principles for publicly accountable profit-oriented enterprises for interim and annual financial statements effective January 1, 2011. The Company is evaluating the effects of adopting this standard.

### NOTE 3 STOCK OPTIONS

During the first quarter ended March 31, 2009, the Company recorded stock-based compensation of \$92,000 (\$64,000 in 2008) relating to prior year option grants in general and administrative expenses of the statement of income.

### NOTE 4 FUTURE RETIREMENT BENEFITS

During the three month periods ended March 31, 2009 and 2008, the Company's future retirement benefit expenses were \$73,000 and \$74,000 respectively.

### NOTE 5 COMMITMENTS AND RELATED PARTY TRANSACTIONS

#### Related Party Transactions

Lease payments for corporate office space paid to a company controlled by the Chairman of the Company were \$22,500 for the three-month period ended March 31, 2009 (\$22,500 in 2008). The Company paid dues relating to a facility in South Carolina of approximately \$4,000 for the three-month period (\$3,000 in 2008) to a company in which the Chairman is an officer.

The Company provided a \$0.1 million share purchase loan in 2006 to an employee due June 15, 2009 bearing interest at 5% annually with full recourse and is included in the financial statements under the caption "other assets".

#### Forward Exchange Contracts

At March 31, 2009, the Company has forward contracts to sell US \$24 million for CAD \$29.3 million to December 31, 2009.

## Notes to CFS (cont'd)

## NOTE 6 SEGMENTED INFORMATION

	Sales excluding inter-company				Inter-company
	Canada	US	Other	Total	
<b>March 2009</b>					
Rubber Compounding Operations	12,794	21,747	84	34,625	705
AEP and Other	2,942	13,529	1,989	18,460	3,321
Total	15,736	35,276	2,073	53,085	4,026
<b>March 2008</b>					
Rubber Compounding Operations	18,710	22,580	94	41,384	510
AEP and Other	2,634	10,122	994	13,750	1,653
Total	21,344	32,702	1,088	55,134	2,163
		Rubber Compounding Operations	AEP & Other	Corporate and Inter-company Eliminations	Total
<b>March 2009</b>					
Sales		35,330	21,781	(4,026)	53,085
Cost of sales		34,639	17,491	(4,026)	48,104
		691	4,290	-	4,981
Operating expenses		1,566	1,148	612	3,326
Other expense (income)		103	(208)	576	471
Interest expense		364	159	1	524
		(1,342)	3,191	(1,189)	660
Provision for income taxes					(191)
Net income from continuing operations					469
Assets employed					
Canada		66,953	41,679	1,777	110,409
US		22,570	-	-	22,570
Total		89,523	41,679	1,777	132,979
Purchase of capital assets		473	572	5	1,050
Amortization of capital assets and other assets		671	461	11	1,143
Goodwill		-	7,182	-	7,182
		Rubber Compounding Operations	AEP & Other	Corporate and Inter-company Eliminations	Total
<b>March 2008</b>					
Sales		41,894	15,403	(2,163)	55,134
Cost of sales		39,352	12,943	(2,163)	50,132
		2,542	2,460	-	5,002
Operating expenses		1,446	1,249	472	3,167
Other expense (income)		360	(69)	(742)	(451)
Interest expense		565	142	-	707
		171	1,138	270	1,579
Provision for income taxes					(617)
Net income from continuing operations					962
Assets employed					
Canada		73,705	42,735	2,240	118,680
US		17,487	266	-	17,753
Total		91,192	43,001	2,240	136,433
Purchase of capital assets		84	456	-	540
Amortization of capital assets and other assets		750	421	28	1,199
Goodwill		7,944	7,182	-	15,126

## Notes to CFS (cont'd)

**NOTE 7 FINANCIAL INSTRUMENTS****Financial risk management**

The Company's activities result in exposure to a variety of financial risks, including risks related to commodity prices, currency fluctuation, interest rates, credit, and liquidity. The risk factors described on pages 21 to 23 of the Company's 2008 Annual Report is an integral part of these interim consolidated financial statements and provides the earnings sensitivity to market risks.

**Market Risk****Commodity prices and supplies**

The Company's financial performance depends on certain outside sources for raw materials including carbon black and synthetic and natural rubber used in the production of its products, the price and availability of which are subject to fluctuations from such factors as weather, exchange rates, the price of oil, changes in industry production capacity, changes in world inventory levels and other factors beyond the Company's control.

The Company manages its commodity price and supply risk by matching purchase commitments to its customers' requirements during the term of the price quote ranging from 1 to 3 months and maintains supply sources in different areas of the world. The Company does not enter into commodity contracts other than to meet the Company's expected usage and sale requirements; such contracts are not settled net.

During the first quarter of 2009, raw material prices continued to decline creating pressure on selling prices in the rubber compounding business and eroding margins until higher priced inventories were consumed.

**Currency Risk**

Most of the Company's products are sold at prices denominated in US dollars or based on prevailing US dollar prices; most of the raw material purchases are denominated in US dollars, and a significant portion of its operational costs and expenses are incurred in Canadian dollars. Therefore, an increase in the value of the Canadian dollar relative to the US dollar reduces the revenue in Canadian dollar terms realized by the Company from sales made in US dollars, which reduces operating margin and the cash flow available to fund operations. The net US monetary assets of its Canadian operations represent a currency risk as the balances are re-measured at the month end spot rate creating an unrealized exchange gain or loss.

The Company manages its currency risk relating to monetary assets and liabilities denominated in US dollars by increasing or decreasing the proportion of operating or term loan denominated in US funds or forward currency contracts. The Company chooses to manage the exchange exposure relating to raw materials purchased in US dollars in the rubber compounding division by offsetting this inventory with US denominated 30 day LIBOR debt and a 30 day revolving forward contract which are valued at month end rates. The Rubber Compounding segment's profit and loss is somewhat naturally hedged in that sales denominated in US dollars offset US dollar expenses and debt service costs. AEP's business has relatively lower US dollar expense content and is not naturally hedged.

The weaker Canadian dollar had a favorable impact on US dollar denominated sales compared to the same period last year. The average exchange rate this year was 1.24 compared to 1.00 in the first quarter of last year; margins improved by \$0.9 million as a result of a weakening Canadian dollar.

**Interest Rate Risk**

The Company's interest rate risk mainly arises from the interest rate impact on cash, floating rate debt and pension obligation.

When the demand loan and term loan were negotiated, the primary objective was to obtain flexibility to manage its currency exposure. In Q4 of 2008, the Company increased its proportion of borrowings on a fixed rate basis to balance its exposure. Currently, 44.8% (2008 – 21.3%) of borrowings are on a fixed rate basis and the Company has benefited from the reduction in the variable rates.

At the reporting date, the interest profile of the Company's interest-bearing financial instruments was:

	2009	2008
Fixed rate instruments		
Financial assets	157	158
Financial liabilities	(17,651)	(8,251)
Variable rate instruments		
Financial assets	-	3,837
Financial liabilities	(21,728)	(30,466)
Total	(39,222)	(34,722)

**Credit Risk**

The Company sells its products to a variety of customers under various payment terms in the normal course of its operations and therefore is exposed to credit risks. The Company's exposure to credit risk is influenced by general economic conditions, the default risk of the industry and the relative concentration of business. A majority of the Company's trade receivables are derived from sales to distributors, and manufacturers who have been transacting with the Company for over five years.

In monitoring credit risk, the Company considers industry, volume and aging trends, maturity, and other relevant factors. The Company performs ongoing credit evaluations of its customers' financial condition and limits the amount of credit extended when deemed necessary. Purchase limits established for certain accounts represent the maximum open balance permitted without approval from the CEO. The Company maintains reserves for potential credit losses relating to specific exposures, and any such losses to date have been within management's expectations. The loss of any such customers or the delay or cancellation of any orders under certain high-volume contracts could have a significant impact on the Company.

The Company did not experience any material bad debts in the first quarter of 2009 and still believes that its five largest customers are credit worthy.

## Notes to CFS (cont'd)

**Liquidity Risk**

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due. The Company's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due, under normal and stressed conditions.

The Company manages liquidity by maintaining adequate cash balances, having appropriate lines of credit available and monitoring cash requirements to meet expected operational expenses including debt service and capital requirements. In addition, the Company maintains a facility permitting the Company to borrow up to \$35 million. At the quarter end, the Company had drawn \$9.4 million against this facility (2008: \$21.0 million). When negotiating its term facility, the Company obtained a 7 year term.

**Fair value of financial instruments**

The Company's financial instruments consist of accounts receivable, restricted funds, demand loan, accounts payable and accrued liabilities, term loan and other debt. The fair values of accounts receivable, restricted funds, demand loan, accounts payable and accrued liabilities, as recorded in the consolidated balance sheets approximate their carrying amounts due to the short-term maturities of these instruments. The term loan reflects current market interest rates therefore the carrying amount approximate fair value. The fair value of the other debt is not readily determinable. The fixed rate exchange contracts to sell US \$24 million for CAD \$29.3 million have been recorded at their fair market value as a net liability of \$0.4 million.

The Company has designated:

- forward contracts as held for trading
- accounts receivable, note receivables and restricted funds as loans and receivables
- accounts payable, demand loan and term debt as other liabilities

The carrying value and fair value are as follows:

	March 31, 2009	December 31, 2008
Held for trading	(432)	(8)
Loans and receivables	27,060	35,315
Other liabilities	(54,569)	(74,148)

**Capital Management**

The Company has defined its capital as follows:

	March 31, 2009	December 31, 2008
Demand loan	11,513	17,788
Term loan and other debt	27,880	28,060
Shareholders' equity	65,727	65,166
	<b>\$ 105,120</b>	<b>\$ 110,014</b>

The Company's business is cyclical and it experiences significant changes in cash flow over the business cycle. In addition, the Company's financial performance can be materially influenced by changes in the relative value of the Canadian and US dollar.

The Company's fundamental objective in managing capital is to ensure adequate liquidity and financial flexibility at all times, but particularly at the bottom of the business cycle and in a strong Canadian dollar environment. The Company constantly monitors and assesses its financial performance in order to ensure that its net debt levels are prudent taking into account the anticipated direction of the business cycle. When reviewing financing decisions, the Company considers the impact of debt and equity financing on its existing and future shareholders. The Company has established a committed revolving line of credit that provides liquidity and flexibility when capital markets are restricted.

Directors and Officers currently own 23.4% or 5,565,473 shares of the Company. Each Director is required to hold shares for value equal to 3 years retainer fees in order to align objectives with that of shareholders. There is no plan to extend availability of options beyond key management and senior employees. The Company implemented a semi-annual dividend policy to provide an additional return.

The Board has approved a normal course issuer bid to purchase up to 1.8 million shares as it believes it will be accretive to shareholders and would consider a share issue to finance a sizeable acquisition should an opportunity arise.

Neither the Company nor any of its subsidiaries are subject to externally imposed capital requirements.

# AirBoss of America Corp.

## OFFICES

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Vice-President Finance and CFO:  
Stephen W. Richards

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Vice-President Sales and Marketing:  
John Tomins

Vice-President of Supply Chain Management:  
John Bergman

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