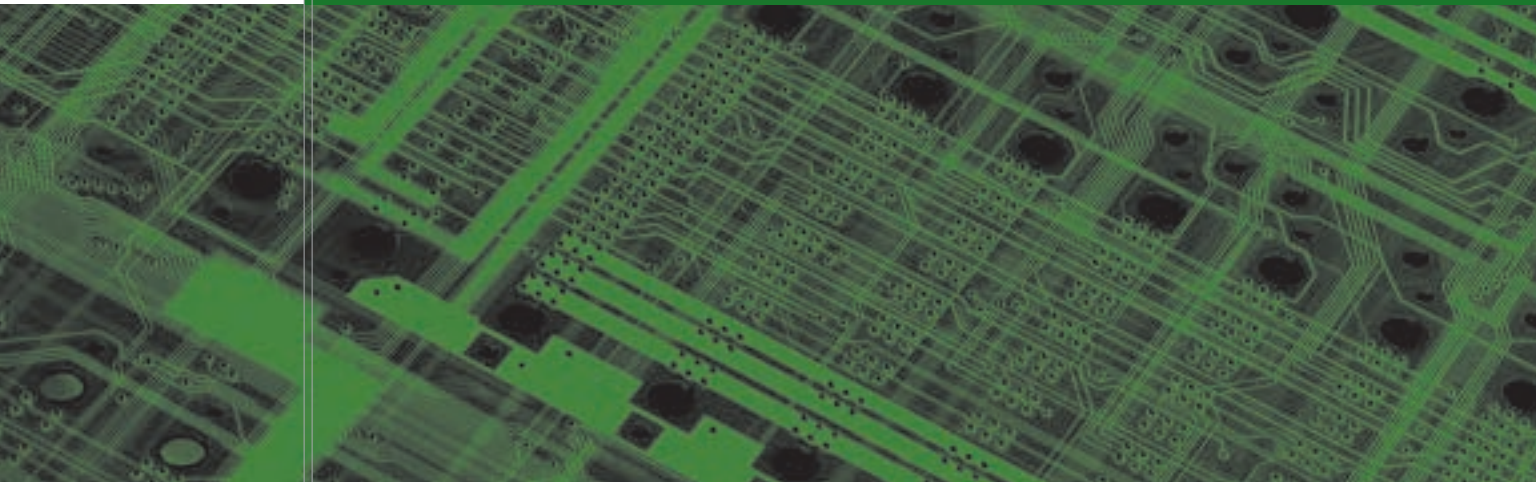


*a year of recovery*

CORETEC 2003 ANNUAL REPORT



*how far, how fast?*

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**CORPORATE PROFILE** The connections between individual electronic components used in virtually all electronic products would not be possible without printed circuit boards (PCBs). Coretec is the largest Canadian-owned fabricator of PCBs and one of the largest in North America. The Company distinguishes itself from its competitors by providing complete PCB service solutions – including highly engineered design, design consulting, educational seminars, advance prototyping, quick-turn production and high volume facilitation – to electronics markets in Canada, the United States and Europe. Coretec's business is highly customized and focused on value-added engineering.

## how far, how fast?

Our corporate brand is best described by a simple proposition: *how far, how fast?* This motto refers to the three core operating principles of our business: technology, value-added services and time.

**Technology** Coretec's technological capability is truly a competitive differentiator. We have one of the most advanced and comprehensive product offerings in the circuit board industry today. This offering is continuously being refined through our dedication to interconnection research and development.

*how far is far?* We appreciate the ever-increasing performance needs of the electronics industry and the fact that our products and services are technology enablers. As such, we choose to think of technology as an opportunity to demonstrate our ingenuity.

**Value-Added Services** Coretec's value-added services are exceptional in the industry. Our advanced design and engineering initiatives have proven to be tremendous tools with respect to gaining and retaining market share.

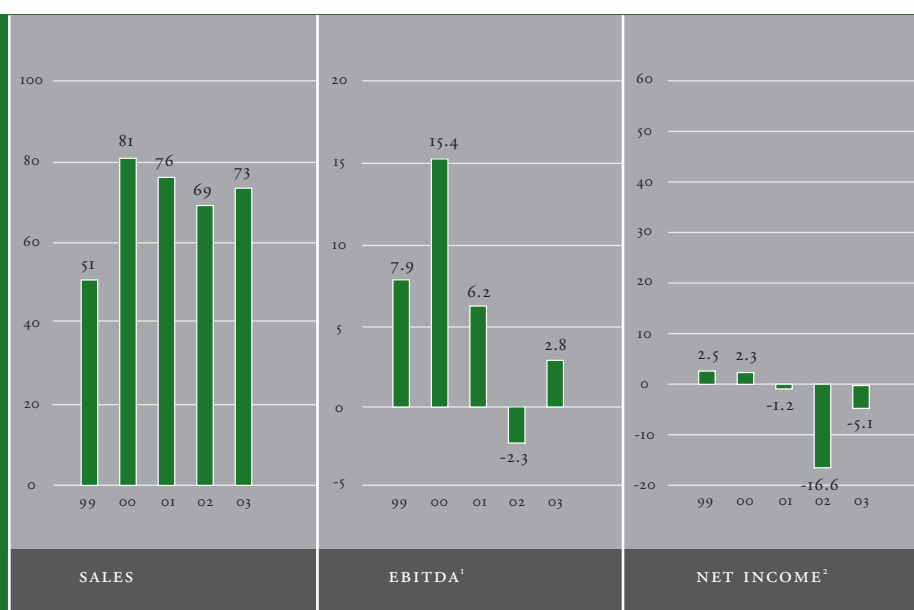
*how far is far?* Our objective is to be an extension of the client's design team and help them to get better products to market faster. We are committed to being a strategic resource for our customers, continually.

**Time** Coretec's manufacturing lead times are world-class. Our continuous improvement culture and systems are tailored to meet the needs of rapid-response manufacturing, regardless of the technology or quantity required.

*how fast is fast?* In a world of compressing product lifecycles, we understand the need for speed. We believe that our focus, proximity and technology specific operations are fundamental to us providing world-class solutions in world-class time.

## Financial Highlights

(S in millions of Canadian dollars)



<sup>1</sup>EBITDA is calculated as earnings before interest and certain other expenses, provision for income taxes, depreciation and amortization and impairment of capital assets. EBITDA is not a measure recognized under Canadian generally accepted accounting principles ("GAAP"). Management believe that many of the Company's shareholders, creditors, other stakeholders and analysts prefer to assess the Company's performance using EBITDA in addition to the GAAP measures. The Company's method of calculating EBITDA may differ from other companies and accordingly may not be comparable to measures used by other companies.

<sup>2</sup>Net income for 2002 includes a pre-tax asset impairment charge of 8.1 million.

## Letter to Shareholders



PAUL COLIN LANGSTON  
*President, CEO & Chairman*



MARK THORNLEY  
*Chief Financial Officer*

We are pleased to report that 2003 represented a year in which we experienced resumption in revenue growth and improved operating results despite formidable challenges. Prior to 2001 Coretec had achieved 20 straight years of uninterrupted revenue growth and profitability. Unfortunately, we were unable to maintain this impressive record through a tumultuous 2001 and 2002 when we experienced a cumulative 14% decline in revenues, reduced operating margins and significant losses. Hence, our improving financial metrics make us firmly optimistic for 2004.

In 2003 Coretec grew its revenues by 6% year over year. In comparison, the printed circuit board ("PCB") industry in North America realized its third consecutive year of contracting shipments in dollar terms, estimated by IPC, an industry association, to be a 17% decline versus 2002. Our relative out-performance is made even more impressive when the impact of foreign exchange on our revenues is taken into consideration. In 2003 approximately 60% of our revenues were denominated in US dollars, a currency that declined close to 20% against the Canadian dollar since January 1, 2003.

We attribute the market share gains achieved over the past three years to our dedication to our core operating principles of time, technology and value-added services. The investments that we made in marketing and sales, in process technology, in systems, and above all, in our people have been consistent with this brand commitment. As a result, we have been able to re-engineer our end market and customer exposure to what we believe is a much more balanced and expandable business mix. For example, on a comparative basis, in 2000 we had virtually no presence in the robust defense and aerospace sector while today the sector represents a significant portion of our total revenues. Similarly in 2000 our exposure to one of the most stable end markets, instrumentation, was only 17% versus 23% in 2003. In 2000 our business was relatively concentrated (46% in total) in the telecommunications and computer segments. By 2003 our exposure to these volatile and price sensitive end markets was reduced by half.

According to industry consultants, Prismark Partners, the sectors offering the greatest growth potential to North American PCB fabricators over the next three years will be instrumentation and defense/aerospace. In addition, the demand for prototype and quick turn services is projected to be robust versus higher volume production which is expected to continue its offshore migration. Prismark is also projecting higher growth rates for complex PCBs (high layer count and High Density Interconnect). As such, we believe our rapid response dedication, advanced technology capability and end market orientation are well aligned with the new paradigms of the North American industry.

### TIME



Coretec's business is rapid-response manufacturing and design. Our culture and systems are focused on providing customer solutions in the shortest timeframe possible.

### TECHNOLOGY



Our product capability is world-class, and we design and manufacture to some of the most demanding standards in the industry today.

THROUGHOUT 2003 WE AUGMENTED CAPACITY AT EACH OF OUR SITES THROUGH STRATEGIC PERSONNEL AND EQUIPMENT ADDITIONS, SYSTEMS IMPLEMENTATIONS AND DEPLOYMENT OF SPECIFIC MACHINERY IN STORAGE.

While PCB shipments in North America declined year over year, recent statistics suggest that the industry is once again growing. According to Henderson Ventures, industry capacity utilization reached its highest level in over three years in December 2003 (>85%) and similarly the industry's average lead-time stretched to 24 days, the longest timeframe reported since 2000. The Book-to-Bill ratio as reported by IPC was above parity for 10 out of 12 months in 2003 with a marked strengthening in the second half of 2003. Furthermore, analyst estimates for growth in North American industry shipments are a healthy 6-8% in 2004 and a further 8-10% in 2005. As a result, the more positive tone permeating the industry has us excited about our prospects for 2004. Historically, high capacity utilization rates coupled with extended lead times has led to upward price pressure for quick turn services.

Industry analysts suggest approximately 40% of the North American industry capacity has been permanently removed over the past two to three years and further facility closures are expected in 2004. Particularly vulnerable are companies who are financially or technologically challenged. What remains in North America is a highly fragmented industry where the vast majority of industry players are small (<US\$10 million in revenues), regional facilities with limited capital resources. In fact fewer than 15 companies, including Coretec, had revenues in excess of US\$50 million in 2003. We believe a significant opportunity exists for those few companies, like Coretec, that possess the scale, access to capital, technology and intellectual resources required to meet the market's requirements for higher densities, improved product reliability and performance.

Anticipating this opportunity, in 2003 we undertook a series of strategic initiatives in order to optimize our potential in an industry that is once again on a growth trajectory. Specifically, we expanded our sales organization to include all regions of the US and improved our field applications engineering coverage; measures that meaningfully extended our brand awareness, new account penetration and new program wins at existing accounts. Furthermore, our strategy of performing a program management role with offshore partners for targeted customers gained traction in the year. The fourth quarter of 2003 was the first quarter in which our reselling of offshore parts exceeded \$1 million in revenues.

Throughout 2003 we augmented capacity at each of our sites through strategic personnel and equipment additions, systems implementations and deployment of specific machinery in storage. In 2004 we will complete the implementation of the remaining \$3 million worth of fully paid for equipment that is presently in storage, as well as purchase approximately \$3 million worth of new capital equipment corporate wide.

#### VALUE-ADDED SERVICES



We welcome opportunities to redefine what is possible, working closely with our clients through education, advanced design capability, consulting and collaborative R&D.

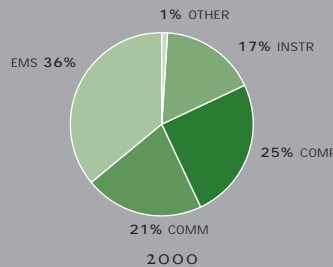
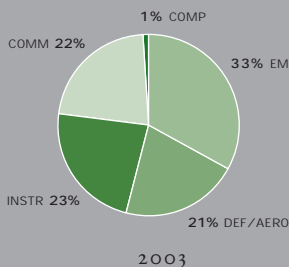
During 2003 we harmonized our engineering, quotations and ERP systems between sites and introduced web-based customer service tools that enable automated order entry and job tracking. In addition, our ongoing focus on cost control and automation resulted in a \$2 million reduction in selling, general and administrative costs year over year.

Our relatively strong balance sheet has facilitated many of these strategic initiatives over the past year when most industry competitors struggled with weakened capital structures and limited financing options. We are committed to maintaining a prudent capital structure to take advantage of strategic opportunities as the industry rebounds, while improving our positive free cash flow on a quarterly basis. We believe that both of these objectives are key to gaining market share in the future, as customers become more concerned about the security of their supply chain and the ability of their existing PCB supply base to provide the requisite technology and value added services.

Subsequent to the 2003 year end we completed the purchase of Proto-Circuit, Inc., our second strategic site in the United States. We are extremely excited about the additional capacity and capability, particularly the rigid flex product line, this acquisition brings to Coretec. This division operates out of a purpose-built 40,000 square foot facility located near Cleveland, Ohio and boasts an impressive equipment platform and

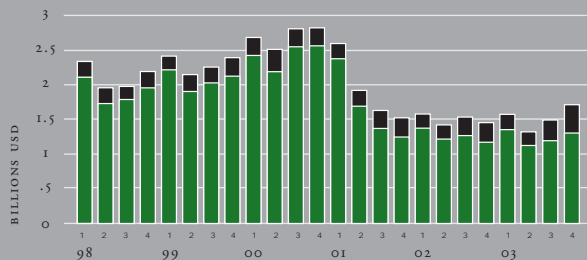
### CORETEC END MARKETS 2003 VS. 2000

	03	00
EMS	33%	36%
COMPUTER	01%	25%
DEFENSE/AEROSPACE	21%	-
INSTRUMENTS	23%	17%
COMMUNICATION	22%	21%
OTHER	-	01%



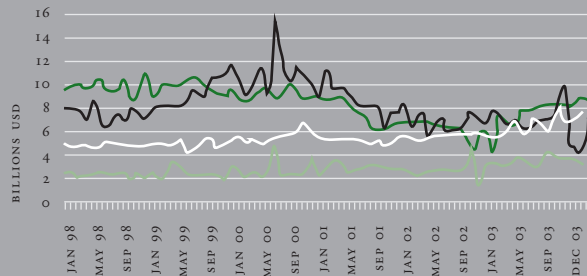
WE HAVE BEEN ABLE TO RE-ENGINEER OUR END MARKET AND CUSTOMER EXPOSURE TO WHAT WE BELIEVE IS A MUCH MORE BALANCED AND EXPANDABLE BUSINESS MIX.

### NORTH AMERICAN PCB SHIPMENTS (Quarterly Sales)



THE PRINTED CIRCUIT BOARD INDUSTRY IN NORTH AMERICA REALIZED ITS THIRD CONSECUTIVE YEAR OF CONTRACTING SHIPMENTS.

### US ELECTRONIC EQUIPMENT ORDERS MONTHLY DATA (Seasonally Adjusted)



THE MOST STABLE END MARKETS SINCE 2000 (DEFENSE/AEROSPACE AND INSTRUMENTATION) ALSO OFFER THE GREATEST GROWTH POTENTIAL TO NORTH AMERICAN PCB FABRICATORS OVER THE NEXT THREE YEARS.

suite of approvals. Most importantly, this facility has a team of professionals who have a proven track record of manufacturing advanced technology products for some of the most demanding defense and aerospace customers in the industry. This site will be renamed Coretec Cleveland by the end of the second quarter of 2004 and will be partnered with our Coretec Denver operation in terms of attacking existing and new opportunities in the defense and aerospace sector.

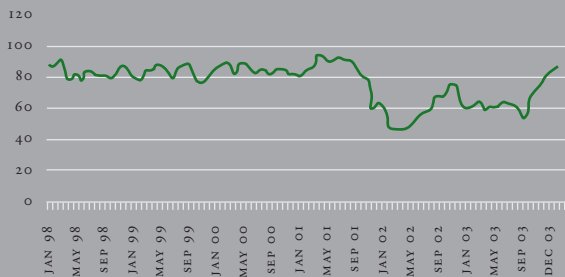
Throughout the year, our Board of Directors was ever more focused on corporate governance, undertaking a thorough review and update of our Board policies, procedures and practices in keeping with the new regulatory standards and expectations of the investment community.

Our teams of employees at each of our sites deserve to be acknowledged for their commitment and sacrifice. They are the reason that we have outperformed many of our competitors during the worst recession in our industry's history and are the reason why we are so confident that Coretec will continue to be an industry leader in the future.

At Coretec we believe that our how far, how fast? brand is absolutely in harmony with the "new" industry. Hence, as the industry recovery continues, we look forward to delivering to all of our stakeholders renewed and responsible growth and prosperity.

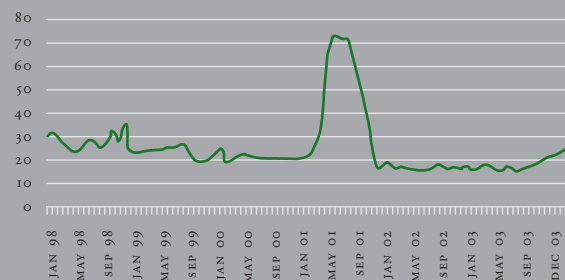
Thank you for your ongoing support and partnership.

NORTH AMERICAN PCB INDUSTRY CAPACITY UTILIZATION %



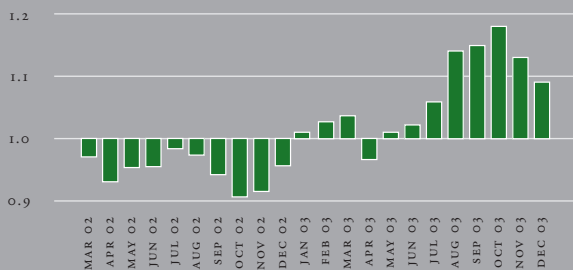
INDUSTRY CAPACITY UTILIZATION IN NORTH AMERICA REACHED ITS HIGHEST LEVEL IN OVER THREE YEARS BY DECEMBER 2003.

NORTH AMERICAN PCB INDUSTRY AVERAGE LEAD TIME (Days)



THE AVERAGE LEAD-TIME IN NORTH AMERICA STRETCHED TO 24 DAYS BY DECEMBER 2003, THE LONGEST TIMEFRAME SINCE 2000.

NORTH AMERICAN PCB BOOK-TO-BILL (IPC)



THE BOOK-TO-BILL RATIO IN NORTH AMERICA WAS ABOVE PARITY FOR 10 OUT OF 12 MONTHS IN 2003 WITH A MARKED STRENGTHENING IN THE SECOND HALF OF 2003.

# MD&A

## MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS FOR THE YEAR ENDED DECEMBER 31, 2003

*(dollar amounts in Canadian dollars unless otherwise indicated)*



The following is a discussion of the consolidated financial condition and results of operations of Coretec Inc. (the "Company" or "Coretec") for the periods indicated and of certain factors that the Company believes are likely to affect its prospective financial condition. All references to a year refer to the fiscal year that ended on December 31 of that year. The following should be read in conjunction with the Consolidated Financial Statements of the Company and notes thereto.

Coretec is one of the leading fabricators of Printed Circuit Boards ("PCBs") for the prototype and quick turn production segments of the North American market. The Company distinguishes itself from its competitors by providing complete PCB service solutions including highly engineered design, advanced prototyping and quick turn production. The Company's motto is "how far? how fast?".

The Company's marketing and sales focus is on servicing the product engineering requirements and expedited time-to-market needs of some of North America's leading original equipment manufacturers ("OEMs") and contract electronics manufacturers ("CEMs"), also known as electronic manufacturing services ("EMS"). The Company targets its sales efforts on market leaders in the most technologically demanding segments of the electronics industry; namely telecommunications, computer, industrial and government (military/aerospace). Recent trends in the PCB market include short electronic life cycles, increasing complexity of electronic products and increasing competition from Asian manufacturers. As an exporter of PCB's, the Company has also been additionally challenged by changes in the value of the Canadian dollar vis-à-vis other currencies.

The Company's sales are derived primarily from the manufacture and sale of PCB's custom designed and produced for each customer. Principal expenses are materials, labour and depreciation. According to IPC, an industry trade association, the PCB market in North America has contracted by approximately 60% since its high in the year 2000. The interim period has shown persistent weakness in the telecommunications, computer and electronic manufacturing services sector both in terms of demand and pricing. As a result, the Company has continuously pursued cost reduction opportunities, including facility consolidation, introduced new and higher technology products and executed value-added services as a means of combating market related pricing pressures. In addition, the Company has also increased its focus on the high reliability end of the market, such as military/aerospace, medical and instrumentation end markets and on the prototype and quick turn service segment of the market. As a result, the Company believes it has been less subject to pricing pressures than conventional (standard lead-time) or volume PCB manufacturers. It also believes that the markets it has focused on are less susceptible to import competition from lower cost, offshore jurisdictions. As a result of the overall weakness in the North American market over the past two years, the unit average selling price of the Company's products has declined which combined with lower production throughput, has led to declines in the Company's overall gross profit.

The appreciation of the Canadian dollar vis-à-vis the US dollar since the start of 2003 has also served to reduce the Canadian dollar equivalent of market pricing the Company offers to US customers. Offsetting the effect of exchange rate movements on revenue are the Company's operating and capital costs denominated in US dollars, which provide a significant natural hedge to changes in the value of the US dollar. In addition to this, the Company also hedges foreign exchange movements through the purchase of foreign exchange forward contracts.

The Company has recently been encouraged by its improved operating and cash flow trends through 2003, with net loss and free cash flow improving sequentially on a quarterly basis throughout the year.

## 2003 BUSINESS HIGHLIGHTS

- The Company experienced its first year-over-year sequential growth in three years as revenue for 2003 increased 6% from the prior year period. This was achieved despite the 18% decline in the exchange rate of the US dollar in 2003. Approximately 60% of the Company's sales are denominated in US dollars.
- Gross profit for 2003 increased 38% over 2002 reaching 22.4% of sales.
- In the second quarter of 2003, the Company made significant reductions to its work force through the substantial consolidation of its Toronto production into one main facility, to better position its cost structure for future periods. In the second quarter, the Company recorded a restructuring charge of \$0.5 million for severance and termination costs related to these reductions.
- During the year, the Company put up for sale its non-operational, 93,000 square foot Sheppard facility, located on 9 acres of land in Toronto, of which, approximately, 20,000 square feet is currently occupied by administrative staff.
- The Company continued to expand its customer base, increasing its active account base to approximately 700 customer accounts.
- In 2003, the Company increased its product offering by establishing a value added offshore brokerage service. Revenues from this activity reached \$2.1 million in the last six months of 2003.
- As at December 31, 2003, the Company had cash balances of \$1.3 million and total working capital of \$8.0 million and an unutilized bank line of \$6.4 million.
- Capital additions for the year were limited to a total of \$1.5 million as the Company continues to benefit from the substantial equipment additions made over the prior two years, which have enhanced the Company's technology platform for future production demands. The Company also made \$2.5 million of deferred payments related to equipment received in prior periods.
- The Company has recorded foreign exchange translation losses of \$0.7 million, related primarily to the translation of the Company's foreign denominated net assets, due to the decline in the value of the US dollar in 2003.
- Subsequent to the 2003 year end, the Company purchased 100% of the equity and secured debt of Proto-Circuit, Inc., a manufacturer of high reliability rigid and rigid-flex PCB's primarily for the military/aerospace sector, based outside of Cleveland, Ohio. The acquisition includes the purchase of a 40,000 square foot manufacturing facility on five acres of land built in 2000. The total cost of the transaction was approximately \$4.5 million. To help finance the acquisition, the Company's principal bank has agreed to provide an addition term loan, under its existing credit facility, in the amount of US \$3.4 million. The Company will use CDN \$0.8 million of the loan proceeds to pay down a portion of the principal outstanding on its Canadian dollar term loan with the bank.

## SELECTED ANNUAL INFORMATION

Year ended December 31	2003	2002	2001
<i>(in thousands)</i>	\$	\$	\$
Total revenues	73,466	69,497	76,416
Net loss	(5,110)	(16,595)	(1,194)
Net loss per share (basic and diluted)	(0.27)	(0.90)	(0.08)
Total assets	51,607	61,495	72,738
Total long-term financial liabilities	5,349	6,600	1,900

The following analysis will discuss the operating and financial results of the years 2003 and 2002. For detailed analysis on the operating and financial results of 2001, please refer to the Company's 2002 and 2001 annual reports which are publicly filed with Sedar and available through [www.sedar.com](http://www.sedar.com) or available through the Company's web site at [www.coretec-inc.com](http://www.coretec-inc.com). Additional information including press releases and the Company's Annual Information Form (AIF) may also be found at [www.sedar.com](http://www.sedar.com).

### RESULTS OF OPERATIONS FOR THE YEAR ENDED DECEMBER 31, 2003

Sales for 2003 increased \$4.0 million or 6% to \$73.5 million, compared to \$69.5 million 2002. In the 2003 period, 58% of sales were to the US, 28% to Canada and 14% to Europe as compared to 58%, 25% and 17% respectively in the comparative period for 2002. The increase in total sales for 2003 compared to 2002 is a result of market share gains made by the Company, increased sales from the Company's UK subsidiary and increased brokerage sales, offset by a lower foreign exchange conversion rate for the Company's US denominated sales. Brokerage sales in 2003 totaled \$2.1 million compared to no such sales in 2002.

The Company's sales by segment for 2003 were 33% EMS, 21% aerospace/military, 23% instruments, 22% communications and 1% computer. In 2002, the amounts were 28% EMS, 24% aerospace/military, 18% instruments, 24% communications and 6% computers.

The Company's 10 largest customers accounted for 28% of sales in 2003 compared to 28% in 2002.

Gross profit in 2003 increased by \$4.5 million or 37.7% to \$16.4 million, compared to \$11.9 million in 2002. Gross profit as a percentage of sales increased to 22.4% from 17.2% in 2002. The increase in gross profit as a percentage of sales is a result of reduced labour costs from staff reductions, increased materials utilization and cost savings from the substantial consolidation of the Company's Lawrence facility activities into the Ellesmere facility, which was expanded to a 24-hour, seven-day operation in 2003. This facility consolidation, combined with increased production, has resulted in higher capacity utilization in 2003 compared to 2002, decreasing the relative portion of the Company's fixed operating cost component in gross profit. In addition, gross profit in 2002 was negatively affected by approximately \$1.0 million of charges related to inventory obsolescence and equipment cancellation fees.

Selling, General and Administrative ("SG&A") expenses in 2003 decreased \$2.0 million to \$12.4 million, compared to \$14.4 million in 2002. As a percentage of sales, SG&A expenses decreased to 16.9%, compared to 20.8% in the 2002 prior period. The decrease in SG&A expense was principally due to reductions in selling expenses and sales personnel and reduced expenditures in administrative costs for the Company's subsidiaries as a result of centralizing certain administrative functions.

Depreciation and amortization expense decreased \$0.5 million in 2003 to \$7.2 million compared to \$7.7 million in the 2002 prior period. The decrease in depreciation is principally a result of a full year's decreased depreciation on the Company's UK assets, which were written down at the end of the second quarter of 2002.

In 2002, the Company recorded an \$8.1 million impairment charge related to the write down of the Sheppard facility (\$6.3 million) and the write down of certain capital assets in its UK subsidiary (\$1.8 million). There is no comparable charge in 2003.

Restructuring charges in 2003 were \$0.5 million compared to no charges in 2002. The charge represents the termination and severance costs associated with the reduction of approximately 8% of the Company's production and administrative staff in the second quarter of 2003.

Loss from operations in 2003 was reduced by \$14.6 million to a loss of \$3.7 million, compared to a loss from operations of \$18.4 million in 2002.

Interest and other expenses increased \$0.1 million to \$0.7 million in 2003 compared to \$0.6 million in 2002 as the Company had higher average net debt balances compared to the 2002 prior period.

Foreign exchange translation cost increased \$0.9 million to a loss of \$0.7 million in 2003 compared to a gain of \$0.2 million in 2002. The increased costs are principally a result of the reported translation of the Company's US dollar denominated net working capital balances at a lower exchange rate compared to the prior year due to the fall in the value of the US dollar vis-à-vis the Canadian dollar. This loss was offset by a gain \$0.2 million on the market valuation of the Company's US dollar forward exchange contracts held at the end of the 2003.

Income tax expense recovery in 2003 was not material and the Company's effective tax rate was nil due to valuation allowances booked against tax benefited losses for 2003. In 2002, the effective tax rate was different from the statutory rate primarily due to tax rate differences on earnings (losses) in foreign jurisdictions, valuation allowances against tax benefited losses and certain non-deductible expenses.

### RESULTS OF OPERATIONS FOR THE QUARTER ENDED DECEMBER 31, 2003

In the quarter ended December 31, 2003, sales increased \$0.9 million or 5% to \$19.5 million compared to sales of \$18.6 million in the fourth quarter of 2002. A portion of the increase in sales is a result of an increase in the Company's brokerage/project management activity, in which the Company purchases and resells PCB's manufactured by the Company's third party offshore supply partners. This activity accounted for approximately 7% of sales in the fourth quarter of 2003 compared no such activity in the prior year period. Gross profit increased \$1.1 million or 31% to \$4.6 million compared to \$3.5 million in the prior year period. Gross profit as a percentage of sales increased to 23.4% of sales compared to 18.9% in the fourth quarter of 2002. The Company attributes this increase in gross profit to increased sales activity combined with lower operating costs as a result of facility consolidation and other cost reduction initiatives undertaken during 2003. Loss from operations in the fourth quarter of 2003 was reduced by \$7.9 million to essentially break even as a result of higher gross profit, lower selling general and administrative ("SG&A") costs and the fact the comparable 2002 quarter recorded an asset impairment charge of \$6.3 million which was non-recurring. SG&A costs decreased by \$0.5 million to \$2.8 million compared to \$3.3 million in the prior year period principally as a result of personnel reductions. Depreciation and amortization expense was \$1.8 million in the fourth quarter of 2003, essentially unchanged from the prior year period. Interest expense in the fourth quarter of 2003 decreased \$0.1 million to \$0.2 million compared to \$0.3 million in the prior year period. Net loss in the fourth quarter of 2003 was \$0.2 million or \$(0.01) per share compared to a loss of \$8.3 million or \$(0.44) per share in the fourth quarter of 2002.



### DISCUSSION OF FINANCIAL POSITION

Summary of Financial position:

	December 31, 2003	December 31, 2002
<i>(in thousands)</i>	\$	\$
<b>ASSETS</b>		
Cash	1,342	4,196
Accounts receivable	12,148	11,840
Inventories	3,996	4,882
Income taxes recoverable	451	1,193
Prepaid expenses	1,099	1,066
<b>Total current assets</b>	<b>19,036</b>	<b>23,177</b>
Long term assets	32,571	38,318
<b>Total assets</b>	<b>52,076</b>	<b>61,495</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
Bank indebtedness	863	177
Current liabilities	10,192	14,199
<b>Total current liabilities</b>	<b>11,055</b>	<b>14,376</b>
Future income taxes	-	86
Long term debt	5,349	6,600
<b>Total liabilities</b>	<b>16,404</b>	<b>21,062</b>
Shareholders' equity	35,203	40,433
<b>Total liabilities and shareholders' equity</b>	<b>52,076</b>	<b>61,495</b>



#### CAPITAL ADDITIONS

Excluding deferred payments on capital additions from prior periods, capital additions for 2003 decreased \$3.0 million to \$1.5 million, compared to \$4.5 million in 2002. Capital additions in 2003 consisted principally of investments in design software and information technology of \$0.5 million and advanced technology manufacturing equipment of \$0.5 million. In 2003 the Company also made payments of \$2.5 million representing deferred payments on equipment delivered in the prior period. Deferred payments remaining on all equipment delivered to date represent less than \$0.2 million as at the end of 2003. As of December 31, 2003, the Company still had approximately \$3.5 million of new, fully paid for, advanced equipment in storage, which is expected to be deployed in 2004. To date, no depreciation has been taken on this equipment which is currently not in use.

Subsequent to the 2003 year end, the Company purchased 100% of the equity and the secured debt of Proto-Circuit, Inc., a manufacturer of high reliability rigid and rigid-flex PCB's primarily for the military/aerospace sector, based outside of Cleveland, Ohio. The acquisition includes the purchase of a 40,000 square foot manufacturing facility, on five acres of land, built in 2000. The total cost of the transaction was approximately \$4.5 million.

#### LONG-LIVED ASSETS HELD FOR SALE

In 2003, the Company put its Sheppard facility up for sale and for reporting purposes has segregated its \$5.1 million carrying value as a long-lived asset held for sale on the balance sheet. The 93,000 square foot facility, located on approximately 9 acres of land in Toronto, contains the Company's administrative offices, however the remaining 75,000 square feet of manufacturing area has not been completed or fitted out with equipment. In the fourth quarter of 2002 the carrying value of the building and improvements on the Sheppard facility was written down \$6.3 million to its estimated net recoverable amount. Upon the sale of the facility the Company will relocate its administrative offices, although no specific location has been identified as of this date. The facility serves as principal collateral for a \$4.2 million mortgage which the Company expects to pay down in full with the proceeds of the sale. The Company can give no assurances, however, as to when the sale will actually take place, if ever, or the extent of the proceeds upon sale.

#### LIQUIDITY AND CAPITAL RESOURCES

At December 31, 2003, the Company's principal source of liquidity included cash of \$1.3 million and trade accounts receivable of \$12.1 million. As at December 31, 2003, net working capital decreased \$0.8 million to \$8.0 million compared to \$8.8 million at December 31, 2002. However, net working capital increased \$1.7 million over the second half of 2003 compared to the first half end balance in 2003.

The Company has a credit facility with a Canadian chartered bank's asset based lending group to provide a three year credit facility, maturing November 15, 2005, consisting of an \$8.0 million revolving credit facility collateralized by the Company's accounts receivable and inventory and a \$3.0 million term loan facility collateralized by the Company's equipment. The credit facility is also collateralized by a general security agreement against all of the Company's assets. Funds advanced under the revolving credit facility accrue interest at the rate of prime plus 1.50%. As of December 31, 2003, the Company had drawn funds of \$0.9 million and issued letters of credit of \$0.2 million against the revolving credit facility. On November 15, 2002, \$3.0 million was advanced to the Company under the term loan facility. The term loan requires a principal repayment of \$1.8 million amortized on a straight-line basis over 36 months and a final payment for the remaining principal outstanding at the end of the three-year term. Funds outstanding under the term loan accrue interest at the rate of prime plus 1.75%. The combined facility requires the Company to maintain a minimum consolidated tangible net worth of \$28.5 million over the term of the loan. As at December 31, 2003 the consolidated tangible net worth of the Company, as measured under the terms of the credit facility, was \$32.2 million. Subsequent to the 2003 year end, the bank agreed to provide the Company with an additional US \$3.4 million term loan maturing November 15, 2005, with principal repayments of \$40,476 per month, to finance the acquisition of Proto-Circuit, Inc. The Company will use CDN \$0.8 million of the proceeds from the loan to pay down a portion of the principal outstanding on its Canadian dollar term loan with the bank.

On March 4, 2002 the Company completed a term loan agreement with the Business Development Bank of Canada ("BDC") in the amount of \$5.0 million. The term loan is collateralized by two properties owned by the Company, including the Sheppard facility which is currently held for sale, and a general security agreement. The loan has a term to June 30, 2011, with principal fully repaid on a straight-line amortization over the loan term and bears interest at a rate of 7.4% over the first seven years after which the Company may choose a floating or fixed rate based on the corresponding BDC lending rate less 1.5%. The loan contains a financial covenant requiring the Company to maintain a minimum consolidated tangible equity of \$30.7 million over the life of the loan. As at December 31, 2003 the consolidated tangible equity of the Company, as measured under the terms of the term loan agreement, was \$35.2 million.

On January 31, 2002, the Company completed a private placement offering of 2.5 million common shares for gross proceeds of \$8.5 million less costs of the offering of approximately \$0.6 million.

In 2001, the Company entered into a \$1.9 million, promissory note maturing October 2003, with the vendors of its UK subsidiary, collateralized by a letter of credit from the Company's credit facility. The note bears interest at the rate of Canadian prime less 0.5%. The note was paid, in full, by the Company on October 6, 2003 and the collateral letters of credit were returned and cancelled.

The following is a summary of the Company's contractual obligations as at December 31, 2003. These obligations are also disclosed in the Consolidated Financial Statements of the Company for the year 2003 in Note 11 and Note 12.

<b>Payments Due by Period</b>	<b>Total</b>	<b>Less than 1 year</b>	<b>1-3 years</b>	<b>4-5 years</b>	<b>After 5 years</b>
<i>(in thousands)</i>	\$	\$	\$	\$	\$
<b>Contractual Obligation</b>					
Long Term Debt	6,504	1,155	2,860	1,110	1,378
Operating Leases	7,255	995	1,422	1,374	3,464
<b>Total Obligations</b>	<b>13,759</b>	<b>2,150</b>	<b>4,282</b>	<b>2,484</b>	<b>4,842</b>

The Company's management believes that current cash and cash equivalent balances, current available borrowing capacity and anticipated cash flow from operations will provide it with sufficient liquidity and capital resources to meet its current and future financial obligations, as well as provide funds for its working capital, capital expenditures and other needs, for the foreseeable future. There can be no assurance, however, that near term operating activities will provide the Company with positive cash flow. In addition, to the extent the Company experiences growth in the future, its operating, investing and acquisition activities may require significant additional cash. Consequently, any such future operations or future growth may require the Company to obtain additional equity or debt financing. There can be no assurance that such financing will be available to the Company on favourable terms or at all. The sale of debt or equity securities may cause dilution to existing shareholders.

#### **CASH FLOWS FOR THE YEAR ENDED DECEMBER 31, 2003**

Operating activities for the year ended December 31, 2003 provided cash of \$3.9 million compared to cash used of \$0.9 in the prior year period. The net loss for the year adjusted for non-cash items provide cash of \$3.1 million in 2003, a \$5.0 million increase compared to cash used by the net loss adjusted for non-cash items of \$2.0 million in 2002. This increase in cash provided was off set by a \$0.3 million reduction in cash provided by working capital changes in 2003 compared to 2002. The \$0.8 million in cash provided by changes in working capital for 2003 is principally a result of cash provided by decreases in income taxes receivable of \$0.7 million and inventory of \$0.6 million and an increase in accounts payable and accrued liabilities of \$1.1 million offset by an increase in accounts receivable of \$1.8 million. In 2002, changes in non-cash working capital balances resulted in cash provided of \$1.1 million and related principally to a decrease in inventory of \$1.1 million and prepaid expenses of \$0.5 million off set by an increase in income taxes receivable of \$0.4 million.

Cash used in investing activities in 2003 amounted to \$4.2 million, compared to cash used in investing activities of \$5.4 million in 2002. The 2003 amount includes \$1.5 million of investments in design software, information technology and advanced manufacturing equipment. Also included in capital expenditures for 2003 are \$2.5 million of deferred payments for capital assets acquired in prior periods, which were carried on the balance sheet in accounts payable at the end of 2002. Cash used in investing activities in 2002 includes \$4.0 million of investment in machinery and equipment, \$0.3 million in information and design technology and \$0.2 million in leasehold improvements. Also included in 2002 expenditures are payments for assets acquired in prior periods of \$2.1 million and carried on the balance sheet in accounts payable at the end of 2002, offset by amounts due for capital purchases in 2002 but not payable until 2003 of \$0.7 million, carried on the balance sheet in accounts payable at the end of 2003.

Cash used by financing activities amounted to \$2.3 million in 2003 compared to cash provided of \$9.8 million in 2002. The 2003 period includes a decrease of \$1.9 million in notes payable and \$1.1 million in principal repayments on long term debt offset by an increase in bank indebtedness of \$0.7 million. Cash provided in 2002 principally represents proceeds from long term debt of \$8.0 million less \$0.4 million in principal repayments, proceeds from shares issued, net of costs, of \$7.9 million and proceeds of \$0.2 million from advances from Coretec Limited's bank facility in the UK. From the 2002 share issuance proceeds, \$5.9 million was used to repay bank indebtedness in the first quarter of 2002.

#### CASH FLOWS FOR THE QUARTER ENDED DECEMBER 31, 2003

Cash provided from operating activities in the fourth quarter of 2003 increased \$2.7 million to \$2.6 million compared to cash used of \$0.1 million in the fourth quarter of 2002. The increase in cash provided is principally the result of an increase in cash provided from the reduced net loss in the period adjusted for non-cash items and an increase in cash provided from a net decrease in working capital balances in the quarter.

Cash used in investing activities decreased \$0.6 million to \$0.3 million compared to \$0.9 million in the prior year period. The decrease in cash used is principally the result of reduced capital expenditures in the fourth quarter of 2003 compared to the prior year period.

Cash used in financing activities increased \$4.6 million to cash used of \$1.8 million compared to cash provided of \$2.8 million in the prior year period. In the fourth quarter of 2003, the Company repaid \$0.3 million of long term debt and repaid a promissory note in the amount of \$1.9 million. In the fourth quarter of 2002, the Company had net cash provided from the issuance of \$3.0 million of long term debt under a new bank facility.

#### QUARTERLY COMPARISON

(\$ thousands except EPS amounts, unaudited)	2003				2002			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Revenues	19,472	17,522	17,727	18,745	18,586	17,239	17,330	16,342
Loss from operations	(29)	(422)	(1,445)	(1,812)	(7,948)	(2,262)	(5,954)	(2,215)
Net loss	(190)	(548)	(1,908)	(2,464)	(8,252)	(1,728)	(4,884)	(1,731)
EBITDA <sup>1</sup>	1,715	1,457	81	(487)	157	(161)	(2,078)	(235)
Loss per share								
Basic and Diluted	\$(0.01)	\$(0.03)	\$(0.10)	\$(0.13)	\$(0.44)	\$(0.09)	\$(0.26)	\$(0.10)

<sup>1</sup>EBITDA is calculated as earnings before interest and certain other expenses, provision for income taxes, depreciation and amortization and impairment of capital assets. EBITDA is not a measure recognized under Canadian generally accepted accounting principles ("GAAP"). Management believes that many of the Company's shareholders, creditors, other stakeholders and analysts prefer to assess the Company's performance using EBITDA in addition to the GAAP measures. The Company's method of calculating EBITDA may differ from other companies and accordingly may not be comparable to measures used by other companies.

#### ACCOUNTING CHANGES

Effective January 1, 2003, in accordance with the Canadian Institute of Chartered Accountants (“CICA”) standard on “Stock-based Compensation and Other Stock-based Payments”, the Company has changed its accounting policy to account for stock-based compensation using the fair value method. This change in accounting policy has been adopted prospectively. In accordance with the CICA Handbook, section 3870, only stock options issued on, or after, the initial adoption date of section 3870 are recognized in the financial statements. Accordingly, no compensation expense is recorded for stock options awarded and outstanding prior to January 1, 2003.

The fair value of the options granted is estimated using the Black Scholes option-pricing model and recognized over the option vesting period. For the year ended December 31, 2003, the fair value of employee options granted was estimated using the following assumptions for 2003: risk-free rate of 5.0 percent; expected life of 5 years; volatility of 60% and dividend yield of nil. The fair value of the options is recognized over the vesting period of the options granted as compensation expense and contributed surplus. The contributed surplus balance is reduced as the options are exercised and credited to capital stock.

The net impact of the change on accounting policy for the year ended December 31, 2003, resulted in a charge of approximately \$56,000 for employee stock-based compensation.

#### CHANGES IN ACCOUNTING POLICIES

With the exception of the accounting change relating to Stock-based Compensation, described above, the Company made no changes in its accounting policies during 2003. These policies are disclosed in Note 2 of the Company’s Consolidated Financial Statements.

#### CRITICAL ACCOUNTING ESTIMATES

As at December 31, 2003, the Company carried a warranty reserve of \$0.9 million. This reserve is estimated by using the Company’s past historical experience with respect to the cost of warranty and applying a reserve based on a percentage of sales. The amount reserved on a percentage of sales basis is adjusted periodically by the Company based on changes in past experience or any evidence that would cause a material change in expected future experience.

#### FINANCIAL INSTRUMENTS

At December 31, 2003, 59% of the Company’s trade accounts receivable were denominated in U.S. dollars and the Company believes a significant part of its sales will likely continue to be received in U.S. dollars while a substantial portion of its costs and expenses are denominated in Canadian dollars. The Company enters into foreign exchange forward contracts to help minimize the unexpected currency fluctuations in the value of the U.S. dollar relative to the Canadian dollar. As at December 31, 2003, the Company held foreign exchange forward contracts to exchange a total principal amount of \$4.0 million US dollars into Canadian dollars at varying intervals over the next eight months at an average exchange rate of 1.36. The fair market value of these contracts as of December 31, 2003 was approximately \$0.2 million and has been recorded in the Company’s accounts. The value of these contracts will fluctuate in future periods based on movements in the exchange rate of the Canadian dollar vis-à-vis the US dollar. The Company has historically held each contract to its full maturity date.

#### SHARES OUTSTANDING

At December 31, 2003 there were 18,626,221 shares outstanding. No additional shares have been issued as of the filing of this document.

#### SUBSEQUENT TRANSACTIONS

Subsequent to the 2003 year end, the Company purchased 100% of the equity and secured debt of Proto Circuit, a manufacturer of high reliability rigid and rigid-flex PCB’s primarily for the military/aerospace sector, based outside of Cleveland, Ohio. The acquisition includes the purchase of a 40,000 square foot manufacturing facility on five acres of land built in 2000. The total cost of the transaction was approximately \$4.5 million. The Company’s principal bank has agreed to provide an additional term loan under its existing credit facility, in the amount of US \$3.4 million. The Company will use CDN \$0.8 million of the loan proceeds to pay down a portion of the principal balance outstanding on its Canadian dollar term loan with the bank.



## RISKS

The primary factors affecting Coretec's operating results are the level and timing of customer orders, fluctuations in materials costs and the mix of materials costs versus labour and manufacturing overhead costs resulting from the mix and complexity of products manufactured.

Other factors affecting the Company's annual and quarterly operating results include price competition, the Company's experience manufacturing a particular product, the efficiencies achieved by the Company in managing inventories, capital assets and manufacturing capacity, the timing of expenditures in anticipation of increased sales, the timing of acquisitions and related integration costs, customer product delivery requirements, the ability to amortize set up costs over the total production of a part number, the incidence of product defects, availability of raw materials or labour, retention and training of key personnel, expenditures or write-offs related to acquisitions, distribution and marketing costs, expenses relating to expanding existing manufacturing facilities, continued appreciation of the Canadian dollar and overall economic conditions in the electronics industry. Any one of these factors or a combination thereof could have a material adverse effect on the Company's results of operations, business, prospects and financial condition and could cause variability of results from period to period.

Although the Company's management believes that it has a strategy that will allow for continued "better-than-market" growth, Coretec's ability to manage its growth effectively will require it to continue to develop and improve its operational, financial and other internal systems as well as its business development capabilities and to attract, train, motivate, manage and retain its employees.

PCB complexity and sophistication is increasing as end products become faster, smaller, lighter and more versatile. The future success of the Company's business will depend in large part upon its ability to maintain and enhance its technological capabilities, develop and market manufacturing services that meet changing customer needs and successfully anticipate or respond to technological changes in manufacturing processes on a cost-effective and timely basis.

The Company is focused on the quick turn around and prototype segment of the PCB market and as a result, does not maintain a significant order backlog beyond 15 business days at any given time. The resulting lack of a meaningful order backlog beyond this 15 business day period provides the Company with little visibility into its potential activity in future periods. The Company continues to monitor the effectiveness and profitability of each of its operating facilities, each of which perform at varying levels of capacity and contribution. As a result of the Company's lack of visibility, no assurance can be given as to whether further facility consolidation or even closures will or will not occur in the future.

Although the Company invests heavily in advanced equipment and processes as well as staff training, manufacturing yields may be negatively affected by advancing technologies and thereby cause reductions in operating margins. Furthermore, the Company may be subject to potential liabilities and expenses associated with possible product defects. The Company maintains product liability and other insurance coverage, which it believes to be generally in accordance with industry practices. The Company also maintains reserves for product defects, which are believed to be adequate based on past experience. The Company's increased activity in the purchase and re-sale of PCB's manufactured off-shore will also bring increased potential liabilities for product defects which may or may not be recoverable from the Company's off-shore suppliers.

The PCB industry is intensely competitive, highly fragmented and rapidly changing. During a downturn in the electronics industry, such as the current one, OEMs and CEMs become more price sensitive. The introduction of lower priced competition, most notably from off-shore competitors in low cost jurisdictions and significant price reductions by the Company's competitors has resulted and could further result in price reductions that would adversely affect the Company's business, financial condition and results of operations, as could the introduction of new technologies that would render the Company's manufacturing process technology less competitive or obsolete.

A significant part of the Company's sales will likely continue to be received in currencies other than Canadian dollars. Fluctuations in the value of foreign currencies relative to the Canadian dollar have caused and will continue to cause currency transaction gains and losses. Risk related to currencies could have a material adverse effect on the results of the Company's operations as well as on the cost of acquisitions and capital equipment. As at

December 31, 2003, the Company held foreign exchange forward contracts to exchange a total principal amount of \$4.0 million US dollars into Canadian dollars at varying intervals over the next ten months at an average exchange rate of 1.36. The fair market value of these contracts as of December 31, 2003 was approximately \$0.2 million. At December 31, 2003, 59% of the Company's trade accounts receivable were denominated in U.S. dollars.

Coretec achieved ISO14001 registration in 2000 in Canada, indicating an industry leading commitment to environmental responsibility. Compliance with federal, provincial, state and municipal environmental laws are major considerations in the fabrication of PCBs because metals, solvents and other hazardous materials are used in the manufacturing process. Management expects that regulations will become more stringent in the future and compliance may adversely affect operating results. Furthermore, the Company is a generator of hazardous wastes, and as a result may be subject to potential financial exposure for costs associated with the investigation and remediation of sites at which it has arranged for the disposal of hazardous wastes, if such sites become contaminated.

The Company has been experiencing losses from operations for the past 30-month reporting period. Although the Company believes it will return to profitability in the future, there can be no assurance given that this will be the case. Continued losses from operations may restrict the Company's ability to attract favourable financing and may limit its ability to make continued investment in production capital and technology.

## OUTLOOK

After a North American market contraction of over 60% from the production high point in the year 2000 to the end of 2003, the current climate in the printed circuit board industry, and in fact the electronics industry in general, is showing some modest signs of recovery. According to December 2003 data from the IPC, a leading PCB industry trade association, while 2003 year-to-date shipments of PCB's are down 17% compared to the prior year period and total bookings are down 6%, the three month moving average book-to-bill ratio, as of December 2003, had been above parity for the last seven months in a row – for the first time in over two years. While the Company is encouraged by recent signs of stability, there continues to be limited visibility into the current cycle, which has seen dramatic drops in industry volumes, not only in the PCB industry, but the electronics industry in general. The industry may continue to experience potential pricing pressures as high volume production continues to shift to more attractive global production jurisdictions. Although Coretec's management believes that the Company's positioning in the prototype and quick turn service segment of the PCB market and the military/aerospace and high reliability end market segments of the PCB market, coupled with its continued investment in state of the art production and testing equipment, will allow it to continue to outperform the overall PCB industry, prolonged demand softness or recessionary periods would likely have a material adverse affect on the Company's business, financial condition and results of operations.

## FORWARD LOOKING STATEMENTS

Certain statements contained in this Management's Discussion and Analysis (MD&A) contain forward-looking statements that reflect the expectations of Coretec's management regarding results of operations, performance and business prospects and opportunities. These statements reflect management's current beliefs and are based on information currently available to management. Forward-looking statements involve significant risk, uncertainties and assumptions. A number of factors could cause actual results, performance or achievements to differ materially from the results discussed or implied in the forward-looking statements. These factors include and are not restricted to the risks identified in this MD&A. Coretec's Annual Information Form is filed with the Canadian securities regulatory authorities and risk factors included in this filed document are incorporated herein by reference. These factors should be considered carefully and readers should not place undue reliance on the forward-looking statements. Although the forward looking statements contained in this MD&A are based upon what management believes to be reasonable assumptions, there is no assurance that actual results will be consistent with these forward-looking statements. Coretec disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

# Management's Responsibility | Auditors' Report

## MANAGEMENT'S RESPONSIBILITY

The accompanying consolidated financial statements of Coretec Inc. and all information in the annual report are the responsibility of management and have been approved by the Board of Directors.

The financial statements have been prepared by management in conformity with Canadian generally accepted accounting principles. The financial statements include some amounts that are based on best estimates and judgements. Financial information used elsewhere in the annual report is consistent with that in the financial statements.

Management and the Corporation, in furtherance of the integrity and objectivity of the financial statements, have developed and maintained a system of internal controls. Management believes the internal controls provide reasonable assurance that financial records are reliable and form a proper basis for the preparation of financial statements, and that assets are properly accounted for and safeguarded. The internal control process includes management's communication to employees of policies that govern ethical business conduct.

The Board of Directors carries out its responsibility for the financial statements in this annual report principally through its Audit Committee, consisting of four outside directors. The Audit Committee reviews the Corporation's annual consolidated financial statements and recommends their approval by the Board of Directors. The shareholders' auditors have full access to the Audit Committee, with and without management being present.

These financial statements have been examined by the shareholders' auditors, Ernst & Young LLP, Chartered Accountants, and their report follows.



PAUL COLIN LANGSTON  
*President, CEO and Chairman*



MARK THORNLEY  
*Chief Financial Officer*

## AUDITORS' REPORT

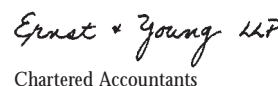
To the Shareholders of Coretec Inc.

We have audited the consolidated balance sheets of Coretec Inc. as at December 31, 2003 and 2002 and the consolidated statements of operations, deficit and cash flows for the years then ended. These financial statements are the responsibility of the Company's management. Our responsibility is to express an opinion on these financial statements based on our audits.

We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the Company as at December 31, 2003 and 2002 and the results of its operations and its cash flows for the years then ended in accordance with Canadian generally accepted accounting principles.

Toronto, Canada,  
February 6, 2004, except as to note 2.4  
which is as of March 30, 2004.



Chartered Accountants

## Consolidated Balance Sheets

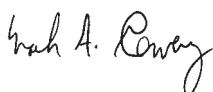
As at December 31	2003	2002
(in thousands)	\$	\$
<b>ASSETS</b> [note 9]		
<b>Current</b>		
Cash	1,342	4,196
Accounts receivable	12,148	11,840
Inventories [note 4]	3,996	4,882
Income taxes recoverable	451	1,193
Prepaid expenses	1,099	1,066
<b>Total current assets</b>	<b>19,036</b>	<b>23,177</b>
Long-lived assets held for sale [note 6]	5,146	–
Capital assets, net [notes 5 and 7]	26,441	37,269
Other assets [note 8]	984	1,049
	<b>51,607</b>	<b>61,495</b>
<b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>		
<b>Current</b>		
Bank indebtedness [note 9]	863	177
Accounts payable and accrued liabilities	9,037	11,270
Current portion of long-term debt [note 11]	1,155	1,029
Current portion of notes payable [note 10]	–	1,900
<b>Total current liabilities</b>	<b>11,055</b>	<b>14,376</b>
Future income taxes [note 12]	–	86
Long-term debt [note 11]	5,349	6,600
<b>Total liabilities</b>	<b>16,404</b>	<b>21,062</b>
Commitments and contingencies [note 13]		
<b>Shareholders' equity</b>		
Share capital [note 14]	60,979	61,155
Contributed surplus [note 3]	56	–
Deficit	(25,832)	(20,722)
<b>Total shareholders' equity</b>	<b>35,203</b>	<b>40,433</b>
	<b>51,607</b>	<b>61,495</b>

See accompanying notes

Approved by the Board:



ROBERT OLSEN  
Lead Director



MARK A. CONVERY  
Director

## Consolidated Statements of Operations

Year ended December 31	2003	2002
<i>(in thousands)</i>	\$	\$
<b>Sales</b>	73,466	69,497
Cost of sales	57,041	57,572
<b>Gross profit</b>	16,425	11,925
<b>Expenses</b>		
Selling, general and administrative	12,443	14,445
Depreciation	7,158	7,684
Impairment of capital assets <i>[note 5]</i>	-	8,146
Restructuring costs <i>[note 17]</i>	531	-
	20,132	30,275
Loss from operations	(3,707)	(18,350)
Interest and other expenses <i>[note 16]</i>	744	594
Foreign exchange (gain) loss <i>[note 18]</i>	685	(203)
Loss before income taxes	(5,136)	(18,741)
Recovery of income taxes <i>[note 12]</i>	(26)	(2,146)
<b>Net loss for the year</b>	(5,110)	(16,595)
<b>Loss per share <i>[note 15]</i></b>		
Basic and diluted	\$(0.27)	\$(0.90)

*See accompanying notes*

## Consolidated Statements of Deficit

Year ended December 31	2003	2002
<i>(in thousands)</i>	\$	\$
Deficit, beginning of year	(20,722)	(4,127)
Net loss for the year	(5,110)	(16,595)
<b>Deficit, end of year</b>	(25,832)	(20,722)

*See accompanying notes*

## Consolidated Statements of Cash Flows

Year ended December 31	2003	2002
<i>(in thousands)</i>	\$	\$
<b>OPERATING ACTIVITIES</b>		
Net loss for the year	(5,110)	(16,595)
Non-cash items		
Depreciation	7,158	7,684
Stock-based compensation	56	-
Unrealized foreign exchange (gain) loss	970	(232)
Impairment of capital assets	-	8,146
Amortization of deferred finance charges	88	73
Future income taxes	(86)	(1,179)
Loss on disposal of capital assets	-	130
	3,076	(1,973)
Net change in non-cash working capital balances related to operations <i>[note 20]</i>	804	1,115
<b>Cash provided by (used in) operating activities</b>	<b>3,880</b>	<b>(858)</b>
<b>FINANCING ACTIVITIES</b>		
Increase of long-term debt	-	8,000
Repayments of long-term debt	(1,125)	(371)
Repayment of notes payable	(1,900)	-
Increase (decrease) in bank indebtedness	686	(5,699)
Proceeds of shares issued, net of share issue costs	-	7,892
<b>Cash provided by (used in) financing activities</b>	<b>(2,339)</b>	<b>9,822</b>
<b>INVESTING ACTIVITIES</b>		
Purchase of capital assets <i>[note 20]</i>	(3,995)	(5,947)
Proceeds on disposal of capital asset	-	130
Increase (decrease) in other assets	(199)	380
<b>Cash used in investing activities</b>	<b>(4,194)</b>	<b>(5,437)</b>
Effect of exchange rate changes on cash	(201)	6
<b>Net increase (decrease) in cash during the year</b>	<b>(2,854)</b>	<b>3,533</b>
Cash, beginning of year	4,196	663
<b>Cash, end of year</b>	<b>1,342</b>	<b>4,196</b>
<b>Supplemental cash flow information</b>		
Interest paid	730	492
Income taxes paid	144	111
Capital asset purchases included in accounts payable and accrued liabilities	-	698

*See accompanying notes*

# Notes to Consolidated Financial Statements

*(tabular amounts in thousands except share amounts)*

## 1. NATURE OF OPERATIONS

Coretec Inc. [the "Company"] designs and manufactures printed circuit boards ["PCBs"] with principal operations in Toronto, Canada.

## 2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

The financial statements of the Company have been prepared in accordance with Canadian generally accepted accounting principles. Outlined below are those accounting policies considered particularly significant.

### Principles of consolidation

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiaries, 1239401 Ontario Limited, Coretec Denver Inc., Coretec (UK) Limited, Tayvin 159 Limited, Coretec Limited, Coretec Holdings Inc. and Coretec Global Financing LLC. All significant intercompany balances and transactions have been eliminated upon consolidation.

### Revenue recognition

The Company recognizes revenue from product manufacturing and design services at the time of product and design shipment and when collectability is reasonable assured. All shipments are supported by customer purchase orders or supply agreements. Where appropriate, provisions are made at that time for estimated warranty and return costs.

### Inventories

Inventories are valued on a first-in, first-out basis at the lower of cost and market. Cost includes direct material, direct labour and overhead. Market is defined as net realizable value for finished goods, net realizable value less costs to complete for work-in-process and replacement cost for raw materials.

### Capital assets

Capital assets are recorded at cost, including capitalized interest where applicable, and are depreciated or amortized on a straight-line basis over the estimated useful lives of the assets as follows:

Buildings	20 years
Machinery and equipment	4-7 years
Office equipment	7 years
Leasehold improvements	Over the term of the lease
Computer hardware and software	3-5 years

Depreciation and amortization is charged on equipment and facilities used in production once the assets are placed into service generating revenue.

### **Deferred finance charges**

Deferred finance charges consist of issue costs incurred in connection with debt financing. Such costs are amortized on a straight-line basis over the term of the related debt.

### **Income taxes**

The Company follows the liability method of tax allocation accounting. Under this method, future tax assets and liabilities are determined based on differences between the financial reporting and tax bases of assets and liabilities and are measured using the substantively enacted tax rates that are expected to be in effect when the differences are expected to reverse.

### **Stock-based compensation**

The Company has a stock-based compensation plan for employees. Under this plan, options are awarded to purchase common shares at prices equal to the closing market price of the shares on the date of the grant subject to vesting provisions. For stock options issued prior to January 1, 2003, no expenses have been recorded when the stock options were issued. As of January 1, 2003, the Company adopted the accounting standard on stock-based compensation and has elected to adopt the fair value method of accounting for stock options on a prospective basis. Under this method the Company recognizes a compensation expense based on the fair value of the options granted using an option pricing model. The fair value of the options is recognized over the vesting period of the options granted as compensation expense and contributed surplus. The contributed surplus balance is reduced as the options are exercised and credited to capital stock.

### **Government assistance**

The Company records the benefit related to investment tax credits ["ITCs"] as a reduction of the cost of capital assets where the ITC relates to capital assets and as a reduction in the related expenses in the case of ITCs related to non-capital expenditures. The benefit of ITCs is recorded when qualified expenditures are made and recovery is reasonably assured.

Government assistance related to various employee-training programmes is applied to reduce the cost of these expenses as expenses eligible for this assistance are incurred.

### **Foreign currency translation**

The Company translates transactions in foreign currencies as well as operations of foreign subsidiaries into Canadian dollars using the temporal method. Under this method, monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the rates of exchange prevailing at the consolidated balance sheet dates, except where hedged. Non-monetary amounts are translated at the rates of exchange prevailing on the transaction date. Foreign exchange gains or losses are included in the determination of net income for the year. Monetary liabilities that are hedged are translated at the rate implicit in the foreign exchange contract.

### **Use of estimates in the preparation of financial statements**

The preparation of financial statements in conformity with Canadian generally accepted accounting principles requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and the disclosure of contingent assets and liabilities at the consolidated balance sheet dates and the reported amounts of revenues and expenses during the reporting periods. Due to the inherent uncertainty in making estimates, actual results could differ from those estimates.

### 3. ACCOUNTING CHANGE

#### Stock-Based Compensation Plans

Effective January 1, 2003, in accordance with the Canadian Institute of Chartered Accountants (“CICA”) standard on “Stock-based Compensation and Other Stock-based Payments”, the Company has changed its accounting policy to account for stock-based compensation using the fair value method. This change in accounting policy has been adopted prospectively, and as such, only stock options issued on, or after, January 1, 2003, are recognized in the financial statements. Accordingly, no compensation expense is recorded for stock options awarded and outstanding prior to January 1, 2003.

The fair value of the options granted is estimated using the Black Scholes option-pricing model and recognized over the option vesting period. For the year ended December 31, 2003, the fair value of employee options granted was estimated using the following assumptions for 2003: risk-free rate of 5.0 percent; expected life of 5 years; volatility of 60% and dividend yield of nil.

The net impact of the change on accounting policy for the year ended December 31, 2003, resulted in a charge of approximately \$56,000 for employee stock-based compensation.

### 4. INVENTORIES

Inventories consist of the following:

	2003	2002
	\$	\$
Raw materials	2,191	2,644
Work-in-process	1,603	1,955
Finished goods	202	283
	<u>3,996</u>	<u>4,882</u>

### 5. CAPITAL ASSET IMPAIRMENT

In 2002 the Company took a \$6.3 million charge related to the write down of the carrying value of building and improvements for the Company's Sheppard facility. The facility was originally purchased in 2000, and shortly thereafter the Company began development of a 93,000 square foot production and administrative facility. While the administration component was completed and occupied in the spring of 2001, construction was halted on the production facility in the fall of 2001. The Company wrote the facility down in the fourth quarter of 2002 to its estimated net recoverable amount of \$5.2 million, a value which reflects the real estate market value of the facility based on third party appraisals. The Company has decided not to complete the facility and put it up for sale in the third quarter of 2003 *[note 6]*.

Also during 2002 the Company performed a test on the recoverability of the capital assets of Coretec Limited, the Company's UK subsidiary, based on estimates of future period's cash flows, and believed that the capital assets of the subsidiary were impaired. Accordingly, the Company took a charge of \$1.8 million against certain capital assets in the subsidiary. This charge was partially offset by the reversal of a \$0.4 million future tax liability associated with these assets.

## 6. LONG-LIVED ASSETS HELD FOR SALE

In the third quarter of 2003 the Company announced it had placed its Sheppard facility up for sale. The facility is located in Toronto and consists of a 93,000 square foot building located on approximately 9 acres of land. The building, originally purchased in 2000, was intended as a head office and manufacturing facility. No manufacturing equipment has been installed in the facility. Approximately 20,000 square feet of the facility is currently in use for administrative offices and the Company expects to relocate administrative personnel to other premises upon the sale of the building. The Company continues to actively market the facility for sale however no assurance can be made as to the net proceeds of the sale or when, if ever, the sale will be transacted. The facility's book value as at December 31, 2003 was \$5.2 million. The facility serves as collateral for a \$4.2 million loan from the Business Development Bank of Canada [note 12]. The Company expects this loan to be repaid in full upon the sale of the facility.

## 7. CAPITAL ASSETS

Capital assets consists of the following:

	2003		
	\$	\$	\$
	Cost	Accumulated depreciation/ amortization	Net book value
Land	352	—	352
Building	2,753	707	2,046
Machinery and equipment	46,228	27,381	18,847
Office equipment	992	494	498
Leasehold improvements	7,551	4,695	2,856
Computer hardware and software	6,570	4,728	1,842
	<u>64,446</u>	<u>38,005</u>	<u>26,441</u>

At December 31, 2003, the Company held approximately \$3.6 million (2002 – \$3.9 million) of equipment at its Sheppard facility that was not in use.

	2002		
	\$	\$	\$
	Cost	Accumulated depreciation/ amortization	Net book value
Land	2,058	—	2,058
Building	6,323	701	5,622
Machinery and equipment	45,983	22,575	23,408
Office equipment	979	383	596
Leasehold improvements	7,521	4,095	3,426
Computer hardware and software	6,072	3,913	2,159
	<u>68,936</u>	<u>31,667</u>	<u>37,269</u>

The cost of building and machinery and equipment has been adjusted for writedowns recorded during 2002 of \$6.3 million and \$1.8 million, respectively [note 5].

## 8. OTHER ASSETS

	2003	2002
	\$	\$
Rent deposit	790	592
Deferred finance charges	182	281
Advances to shareholders	—	176
Deposits on capital assets	12	—
	984	1,049

The Company was committed to fund a rent deposit of 334,000 British pounds in connection with the Coretec Limited acquisition in 2001. The Company made the final payment of 84,424 British pounds relating to this commitment during the current year.

In accordance with the CICA's Emerging Issues Committee (EIC) abstract 132 entitled "Share Purchase Financing", the Company has re-classed shareholder loans on a prospective basis to share capital [note 14].

## 9. BANK INDEBTEDNESS

On November 15, 2002 the Company entered into a new credit facility with a Canadian chartered bank's asset based lending group to provide a three year credit facility consisting of an \$8.0 million revolving credit facility collateralized by the Company's accounts receivable and inventory and a \$3.0 million term facility collateralized by the Company's equipment. The credit facility is also collateralized by a general security agreement against all of the Company's assets. Funds advanced under the revolving credit facility accrue interest at the rate of prime plus 1.50%. At December 31, 2003, there were \$863,000 in funds advanced (2002 – nil) and \$168,000 (2002 –\$2.3 million) in letters of credit issued against the revolving credit facility. The combined bank facility requires the Company to maintain a minimum consolidated tangible net worth of \$28.5 million over the term of the loan. The Company's consolidated tangible net worth as of December 31, 2003 as calculated based upon the terms of the credit facility was \$32.2 million. In addition, the terms of the bank facility also contain restrictions with respect to certain operating aspects of the Company including but not limited to its ability to pay dividends, make capital expenditures or incur additional indebtedness.

In 2003, the Company's UK subsidiary fully repaid and cancelled its operating line credit facility with a UK based bank. There was the Canadian equivalent of \$177,000 outstanding on the facility at the end of 2002. The operating line was collateralized by accounts receivable of the Company and bore interest at the U.K. Bank Base Rate of prime plus 1.75% and was repayable on demand.

## 10. NOTES PAYABLE

Notes in the amount of \$1,882,000 [860,000 British pounds] were payable to the former shareholders of the Company's UK subsidiary in connection with the 2001 acquisition. The notes bear interest at prime less one half percent payable semi-annually, and were collateralized by a letter of credit. The notes were hedged through a forward contract resulting in a carrying value of \$1,900,000. The notes matured and were paid off in full during October 2003.

## II. LONG-TERM DEBT

	2003	2002
	\$	\$
Business Development Bank of Canada	4,154	4,679
Bank of Montreal	2,350	2,950
Less:		
Current portion	(1,155)	(1,029)
	<u>5,349</u>	<u>6,600</u>

On March 4, 2002, a \$5.0 million term loan was provided by the Business Development Bank of Canada ("BDC") and is collateralized by two properties of the Company and a general security agreement. The loan requires monthly principal repayments of \$46,283 amortized straight line over the loan term, and bears interest, payable monthly, for the first seven years at 7.4% after which the Company may choose a floating rate or fixed rate based on the corresponding BDC lending rate less 1.5%. The loan matures on June 30th, 2011. The loan contains a financial covenant requiring the Company to maintain a minimum consolidated tangible equity of \$30.7 million over the term of the loan. As of December 31, 2003, the minimum consolidated tangible equity of the Company as calculated based on the terms of the loan was approximately \$35.7 million. The fair value of this loan at December 31, 2003 was \$4.4 million.

On November 15, 2002, a \$3.0 million term loan was advanced to the Company under a new credit facility with the Bank of Montreal. The term loan requires a principal repayment of \$1.8 million amortized on a straight-line basis over 36 months and a payment for the remaining principal outstanding at the end of the three-year term with interest payable monthly. Funds outstanding under the term loan accrue interest at the rate of prime plus 1.75%. Accordingly, the rate of interest paid on the term loan as of December 31, 2003, was 6.25%. The fair value of this loan at December 31, 2003 was not significantly different from its recorded amount.

Principal repayments on the term loans due within each of the next five years are as follows:

	\$
2004	1,155
2005	2,305
2006	555
2007	555
2008	555
	<u>5,125</u>

## 12. INCOME TAXES

A reconciliation of the Company's income tax expense is as follows:

	2003		2002	
	s	%	s	%
Income taxes expected at average statutory tax rate	(1,881)	(36.6)	(7,234)	(38.6)
Temporary differences not benefited	1,038	20.3	2,961	15.8
Tax losses of Canadian company not benefited	970	18.8	678	3.6
Tax losses of foreign subsidiary not benefited	408	7.9	669	3.6
Expenses not deductible for tax	44	0.8	412	2.2
Large corporation tax	45	0.9	65	0.3
Other	(650)	(12.6)	303	1.6
<b>Provision for income taxes</b>	<b>(26)</b>	<b>(0.5)</b>	<b>(2,146)</b>	<b>(11.5)</b>

Significant components of the Company's future tax assets and liabilities are as follows:

	2003	2002
	s	s
<b>Future income tax assets</b>		
Non-capital operating losses	3,855	2,063
Capital assets	1,816	1,138
Financing costs	538	835
Other, net	546	113
Valuation allowance	(6,636)	(3,763)
	119	386
<b>Future income tax liabilities</b>		
Capital assets	119	472
<b>Net future income tax liabilities</b>	<b>-</b>	<b>86</b>

Significant components of the provision for income taxes are as follows:

	2003	2002
	s	s
Current tax expense (recovery)	45	(967)
Future income tax benefit		
related to origination and reversal of temporary differences	(452)	(1,524)
Future income tax expense from		
amortization of deferred share issue costs	381	345
<b>Provision for (recovery of) income taxes</b>	<b>(26)</b>	<b>(2,146)</b>

At December 31, 2003, the Company has accumulated operating tax loss carryforwards in various tax jurisdictions which expire as follows:

Country	Tax loss carryforward	Expiry
	\$	
Canada	7,148	2007
United States	2,104	2022
England	1,789	No expiry

### 13. COMMITMENTS AND CONTINGENCIES

The Company has total minimum rental commitments under operating leases for equipment and premises having initial or remaining non-cancelable terms in excess of one year as follows:

	\$
2004	995
2005	760
2006	662
2007	675
2008	699
Thereafter	3,464
<b>Total minimum lease payments</b>	<b>7,255</b>

The Company is subject to various laws, regulations and government policies relating to environmental matters. The Company believes that it is in compliance with such laws, regulations and government policies in all material respects.

### 14. SHARE CAPITAL

#### Authorized

Authorized share capital is comprised of an unlimited number of voting common shares.

#### Issued and outstanding

<i>Transactions</i>	2003		2002	
	Number of shares	Cost of shares	Number of shares	Cost of shares
		\$		\$
Opening balance	18,626,221	61,155	16,115,924	53,052
Issued for cash	—	—	2,510,297	8,103
Total share capital issued	18,626,221	61,155	18,626,221	61,155
Less: Shareholder loans		176		—
Closing balance	18,626,221	60,979	18,626,221	61,155

As per EIC abstract 132 entitled "Share Purchase Financing", the Company has re-classified shareholder loans on a prospective basis to share capital [note 8]. The advances to shareholders at December 31, 2003 are non-interest bearing and are due July 20, 2011. The fair value of these advances as at December 31, 2003 was \$126,000. The shares pledged as collateral for these advances had a fair market value of \$82,222 at December 31, 2003.

On January 31, 2002, the Company completed a private placement of 2.5 million common shares at \$3.40 per common share, for proceeds, net of costs, of \$8,072,000. The costs of the issue, including underwriters' commissions amounted to \$639,000 and are recorded net of tax benefits associated with these costs of \$211,000.

During 2002, the Company issued 10,297 common shares on the exercise of stock options at \$3.00 per share for total proceeds of \$30,891.

### Share options

The Company has established a share option plan [the "Share Option Plan"]. Under the Share Option Plan, the Company may grant up to 1,900,000 options to purchase Common Shares to full-time employees, officers, directors and designated consultants of the Company. Options are granted at a price that is not less than the fair market value at the date of the grant. As at December 31, 2003, there were 1,721,200 options granted since inception of the Share Option Plan.

The options granted to date under the Share Option Plan will become exercisable on a cumulative basis, as to one-third per year upon each of the first, second and third anniversaries of their issue. The options expire five years from the date of issue.

Set out below are the details of all the options granted under the Share Option Plan:

	2003		2002	
	Shares	Weighted-average	Shares	Weighted-average
	#	exercise price (\$)	#	exercise price (\$)
Outstanding, beginning of year	1,151,286	3.94	772,050	3.92
Granted	280,000	2.22	537,500	4.00
Exercised	—	—	(10,297)	3.00
Forfeited	(117,468)	(4.24)	(147,967)	(4.12)
<b>Outstanding, end of year</b>	<b>1,313,818</b>	<b>3.55</b>	<b>1,151,286</b>	<b>3.94</b>
<b>Exercisable, end of year</b>	<b>699,788</b>	<b>3.80</b>	<b>397,017</b>	<b>3.77</b>

The following summarizes information about stock options outstanding and exercisable at December 31, 2003.

Exercise prices	Number outstanding	Weighted-average remaining contractual life (years)	Number exercisable
\$1.00	120,000	4.35	—
\$2.00	60,000	3.85	19,999
\$3.00	416,818	1.60	412,818
\$3.15	150,000	4.85	—
\$4.25	430,000	3.16	143,307
\$6.00	107,000	1.66	103,666
\$7.60	30,000	2.18	19,998
	<b>1,313,818</b>	<b>3.55</b>	<b>699,788</b>

The Company's stock price at December 31, 2003, was \$2.80 per share.

### Stock based compensation

Had compensation cost for the Company's Share Option Plan been determined using the fair value method of accounting for options granted during 2002, net loss and basic and diluted loss per share would have been increased to the pro forma amounts noted below:

	2003	2002
	\$	\$
<b>Net loss</b>		
As reported	(5,110)	(16,595)
Pro forma	(5,526)	(17,180)
<b>Basic and diluted loss per share</b>		
As reported	\$(0.27)	\$(0.90)
Pro forma	\$(0.30)	\$(0.93)

The fair value of the options granted in 2002 is estimated at \$2.37 per share using the Black-Scholes option pricing model based on the following assumptions for 2002: risk-free interest rate of 5.0 percent; expected life of 5 years; volatility of 60% and dividend yield of nil.

### 15. LOSS PER SHARE

In accordance with the CICA Section 3500, "Earnings per Share", loss per share is computed by dividing income available to common shareholders by the weighted average number of common shares outstanding during the year. The calculation for all years presented is as follows:

	2003	2002
	\$	\$
<b>Basic loss per share</b>		
Net loss	(5,110)	(16,595)
Weighted average number of common shares outstanding	18,626,221	18,416,919
Basic loss per share	\$(0.27)	\$(0.90)

For all years presented, stock options were excluded from the calculation of diluted loss per share because the effect would have been anti-dilutive.

### 16. INTEREST AND OTHER EXPENSES

Interest and other expenses comprise the following:

	2003	2002
	\$	\$
Interest expense and bank charges	697	598
Amortization of deferred finance charges	88	73
Interest income	(41)	(77)
	744	594

Interest on long term debt for 2003 was \$0.5 million [2002 - \$0.4 million].

## 17. RESTRUCTURING AND OTHER COSTS

During the year, the Company commenced restructuring activities which resulted in the reduction of approximately eight percent of its workforce. As a result, the Company recorded a charge of \$531,000 representing the severance costs related to the reduction of the number of employees.

## 18. FINANCIAL INSTRUMENTS

### Fair value

The carrying values of cash, accounts receivable, income taxes recoverable, bank indebtedness and accounts payable and accrued liabilities approximate their fair values due to the relatively short periods to maturity of these instruments. Where estimable, the fair values of other financial assets and liabilities have been disclosed in notes which further describe the attributes of these items.

### Concentration of credit risk

Financial instruments that potentially subject the Company to concentrations of credit risk consist principally of trade receivables. During 2003 and 2002 the largest single customer comprised less than 10% of sales. At December 31, 2003, the largest single customer represented less than 10% of trade receivables (December 31, 2002 – 12%).

### Foreign exchange risks and commitments

The Company is exposed to market risk in foreign currency rates as a substantial portion of the Company's revenues are denominated in U.S. dollars while a substantial portion of its costs and expenses are denominated in Canadian dollars. Accordingly, to minimize currency exposure, the Company converts a portion of its U.S. dollar flows to Canadian dollars through forward contracts. As at December 31, 2003, the Company had entered into forward exchange contracts to sell \$4.0 million U.S. dollars at varying intervals during 2004 at an average exchange rate of 1.362. The change in fair market valuation of these contracts to market rates in effect at December 31, 2003, resulted in a gain of approximately \$230,000 which is included in foreign exchange on the consolidated statement of operations.

At December 31, 2003, 59% [2002 – 65%] of trade accounts receivable are denominated in U.S. dollars.

## 19. GOVERNMENT ASSISTANCE

The Company recognized a benefit of nil [2002 – \$40,000] related to ITCs on research and development activities carried out during the year as a reduction in cost of sales. The Company has \$702,000 [2002 – \$415,000] in investment tax credits arising from scientific research and development expenditures available for carry forward to reduce income taxes payable in the future, the benefit of which has not been recorded in the accounts.

## 20. SUPPLEMENTAL CASH FLOW INFORMATION

The components of the net change in non-cash working capital balances related to operations consist of the following:

	2003	2002
	\$	\$
Accounts receivable	(2,038)	(68)
Inventories	646	1,062
Prepaid expenses	159	528
Income taxes recoverable/payable	756	(356)
Accounts payable and accrued liabilities	1,281	(51)
	804	1,115

Capital asset purchases disclosed under investing activities for the year ended December 31, 2003, include payments for capital assets acquired in prior periods in the amount of \$2.5 million (December 31, 2002 – \$2.1 million). These amounts were included in accounts payable and accrued liabilities at December 31, 2002.

## 21. SEGMENT INFORMATION

The Company has one reportable business segment – the design and manufacture of PCBs. Geographic sales information has been provided to distinguish sales to customers in the U.S. and Europe from sales to customers in Canada.

	2003	2002
	\$	\$
Sales to customers in		
Canada	20,591	17,620
United States	42,508	40,430
Europe	10,367	11,447
	73,466	69,497

The majority of the Company's capital assets are located in Canada. At December 31, 2003 approximately \$4,526,435 [2002 – \$5,298,000] and \$1,145,307 [2002 – \$1,231,217] of the Company's capital assets were located in the United States and the United Kingdom respectively.

## 22. RELATED PARTY TRANSACTIONS

Selling, general, and administrative costs in 2002 include \$110,000 paid to CCFL Mezzanine Partners of Canada, an organization related to a Board member of the Company. The payment is in respect to charges to the Company relating to a discontinued financing initiative.

## 23. COMPARATIVE INFORMATION

Certain comparative figures have been reclassified to conform with the financial statement presentation adopted in the current period.

## 24. SUBSEQUENT EVENT

On March 4, 2004 the Company purchased all the equity and secured debt of Proto Circuit, a manufacturer of high reliability rigid and ridged-flex PCB's primarily for the military/ aerospace sector, based outside of Cleveland, Ohio. The acquisition includes the purchase of a 40,000 square foot manufacturing facility on five acres of land built in 2000. The total cost of the transaction was approximately \$4.5 million. The Company's principal bank has agreed to provide an additional term loan, under its existing credit facility, in the amount of US \$3.4 million. The Company will use CDN \$0.8 million of the loan proceeds to pay down a portion of the principal balance outstanding on its Canadian dollar term loan with the bank.

# Corporate Information

## Board of Directors

PAUL COLIN LANGSTON  
*President, CEO and Chairman*  
Coretec Inc.

JOHN F. BANKES♦♦▲  
*Managing Director*  
Artemis Management Group Inc.

MARK A. CONVERY♦+  
*Partner*  
Ogilvy Renault

WALTER D. CUSTER+  
*President*  
Custer Consulting Group

SENATOR J. TREVOR EYTON, O.C.  
*Director*  
Brascan Corporation

ROBERT LORD♦♦▲  
*Chartered Accountant, Past Chair*  
CICA

ROBERT C. OLSEN♦▲  
*Lead Director, Coretec Inc.*  
*Co-President*  
CCFL Mezzanine Partners of Canada Ltd.

FRANK RICCIUTI♦♦▲+  
*President*  
Ejray Consulting Ltd.

## Officers

PAUL COLIN LANGSTON  
*President, CEO and Chairman*

BARRY A. BRISTOW  
*Chief Operating Officer*

MARK A. CONVERY  
*Corporate Secretary*

GARETH J. PARRY  
*Chief Technology Officer*

MARK THORNLEY  
*Chief Financial Officer*

- ♦ Audit Committee
- Governance Committee
- + Environmental and Safety Committee
- ▲ Compensation and Nominating Committee

## Shareholder Information

### ANNUAL MEETING

The annual meeting of shareholders will be held at 4:30 pm, Thursday May 6, 2004, in the Sheraton Centre Toronto Hotel Conference Room G, Toronto, Ontario.

T 416.361.1000 F 416.947.4854

### STOCK TRADING

The Toronto Stock Exchange, Canada  
**Stock Symbol: CYT**

### INVESTOR RELATIONS

For a copy of the annual report, interim reports and other investor-related material, contact:

VITTORIA ALBANO

*Executive Assistant*

Coretec Inc.

T 416.208.2157

E valbano@coretec-inc.com

### TRANSFER AGENT

Computershare

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Toronto, Ontario M5J 2Y1

T 416.263.9505

### LEGAL COUNSEL

Ogilvy Renault

77 King Street West

Suite 2100, Box 141

Toronto, Ontario M5K 1H1

Contact: Mark A. Convery

### AUDITORS

Ernst & Young LLP

222 Bay Street, TD Centre

Toronto, Ontario M5K 1J7

Contact: Don Linsdell

### OUTSTANDING SHARES

As at March 25, 2004, Coretec had outstanding 18,626,221 common shares. In addition, there were 1,356,318 options to purchase common shares outstanding as of such date.

## Facilities

### CANADIAN FACILITIES

#### Sheppard Facility

8150 Sheppard Avenue East  
Toronto, Ontario M1B 5K2  
T 416.208.2100  
F 416.208.2196

#### Lawrence Facility

6530 Lawrence Avenue East  
Toronto, Ontario M1C 4A7  
T 416.208.2100  
F 416.283.3588

#### Ellesmere Facility

2020 Ellesmere Road  
Toronto, Ontario M1H 2Z8  
T 416.208.2100  
F 416.439.2643

#### Design Group Canada

1770 King Street East, Unit 3  
Kitchener, Ontario N2G 2P1  
T 519.489.2142  
F 519.489.2140

### U.S.A. FACILITIES

#### Ascot Parkway Facility

7 Ascot Parkway  
Cuyahoga Falls, OH 44223  
T 330.572.3400  
F 330.572.3434

#### Bradford Facility

10570 Bradford Road  
Littleton, Colorado 80127  
T 303.972.4105  
F 303.972.3917

#### Design Group U.S.A.

10570 Bradford Road  
Littleton, Colorado 80127  
T 303.904.6120  
F 303.904.6180

### U.K. FACILITIES

#### Montgomery Way Facility

Montgomery Way  
Stratton Business Park  
Biggleswade, Bedfordshire  
SG18 8QB  
T 44.1767.602.800  
F 44.1767.602.802

## Coretec Approvals & Certifications

### CANADIAN FACILITIES

#### Lawrence Facility

ISO9002  
ISO14001  
MIL-PRF-5511OF  
QS9000  
UL

#### Ellesmere Facility

ISO9002  
ISO14001  
MIL-PRF-5511OF  
QS9000  
UL

#### Sheppard Facility

ISO9002  
QS9000  
UL

### U.S.A. FACILITIES

#### Bradford Facility

ISO9001  
MIL-PRF-31032  
MIL-PRF-5511OF  
UL

#### Ascot Parkway Facility

MIL-PRF-31032  
MIL-PRF-5511OF  
MIL-PRF-50884  
UL

### U.K. FACILITY

#### Montgomery Way Facility

ISO9001  
MIL-PRF-5511OF  
UL  
BS 9761  
BS 9762  
BS 9763  
CECC 23000  
IECQ

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