

Management Discussion and Analysis

This MD&A contains forward-looking statements. Forward-looking statements are based on current expectations that involve a number of risks and uncertainties that could cause actual events or results to differ materially from those reflected in the MD&A. Forward-looking statements are based on the estimates and opinions of AMS' management at the time the statements were made. AMS assumes no obligation to update forward-looking statements, should circumstances or management's estimates change.

This MD&A is dated November 16, 2007.

Overview

AeroMechanical Services Ltd. is a designer, developer, and service provider of innovative solutions to the global aerospace business. The Company's solutions are designed to improve the productivity and profitability of our customers.

The major products of the Company are Automated Flight Information Reporting System (afirs), Uptime, and Underfloor Stowage Unit. These products are marketed globally by a team of individuals: five based in Calgary, one in Ontario, one in Florida, one in Singapore, and two in Switzerland. One of the Calgary staff is currently spending 90% of his time in China dealing with opportunities there. AMS has sales coverage in many countries around the world.

Financing Activities

During the third quarter employees, directors, and consultants exercised stock options totaling 152,000 common shares at a weighted average exercise price of \$0.51 for gross proceeds of \$77,644.

Warrants were exercised during the third quarter totaling 3,914,999 common shares at a weighted average exercise price of \$0.58 for gross proceeds of \$2,259,392.

Results of Operations – Nine Months Ended September 30, 2007

During the nine months ending September 30, 2007 the Company:

Revenue

As shown in the following tables the afirs UpTime Rental Revenue and Unearned Revenue are showing the results forecasted. AMS' long term investment in marketing and relationship building has given the Company a strong pipeline of prospective clients around the world. The ongoing revenue streams from our existing client base will continue to expand throughout this and future years.

AMS has adopted a conservative revenue recognition policy, whereby, network access fees are capitalized as unearned revenue and revenue is recognized over the term of the initial contracts. This has the effect of normalizing the revenue through the life of the contract, which in the early stages will show less booked revenue than cash received.

The effect in the quarter is that we received \$484,738 in cash revenues with \$312,684 reported as revenue and \$172,054 being included in unearned revenue which compares to \$296,442 in cash revenue in the same quarter of 2006.

Recognized revenue increased \$53,871 in the third quarter compared to the third quarter of last year. Rental revenues increased by \$122,313 over the third quarter of 2006. Sales revenue decreased by \$68,442 as the result of a decrease in the demand and marketing of Under Floor Stowage Units, which was partially offset by an increase in interest revenue. Revenues are expected to grow at a significantly higher rate than our costs because the Company has the infrastructure, sales people, and support organization in place to support revenue growth.

The recognition of the afirs UpTime product superiority and innovation has allowed us to be key note speakers at several leading industry events. This shows that AMS' products are being recognized as leading edge in this industry.

Cost of Sales and Gross Margins

Percentage Cost of Sales in the third quarter of 2007 is 59% of Sales compared to 75% in 2006. This decrease is due to increased installations on existing contracts and aircraft types and the resulting decrease in the cost of sales of non-routable parts and travel expenses of our engineers on initial installations of aircraft. As part of our service we assist new clients with engineering support on their initial installations. This cost is covered in our access fee. Non-routable parts are parts involved in the installation process that are non-reusable (such as cables) and do not form part of the rental asset; they would remain on the aircraft if the afirs unit was extracted. Travel and support costs form part of the non-routable parts and are expensed in the period. The effect is an increase in cost of sales. As we move forward with

Management Discussion and Analysis

more clients and the corresponding recurring revenue streams, we will see the cost of sales decline and our margins increase.

Third quarter 2007 Gross Margin was 41% compared to first quarter of 2007 of 77%, the second quarter of 2007 of 22% and third quarter 2006 of 25%.

Net Loss, General Administrative and Marketing Expenses

The net loss in the quarter ending September 30, 2007 was \$1,693,258 (2006—\$1,176,113) which is an increased loss of \$517,145 over the same period in 2006. This increase is primarily due to increased salaries and benefits of \$513,817 and increased marketing expenses of \$188,384, which are offset by a decrease in professional fees of \$162,333.

Included in General Administrative Expenses are increased marketing costs. Marketing expenses increased by \$188,384 to \$357,078 over the third quarter in 2006. These figures do not include salaries, and are indicative of the increased activity in the marketing and sales area of our company. We expect that expenses in marketing will remain the same or increase into the future as the Company's focus is on generating new customers. Our plans are to continue to attend shows globally that focus on market places we want our products to penetrate. The costs of the shows are relatively high because of the specific nature of these shows and are consistently held in distant locations. Because our product is a very niche product, attendance at the shows is mandatory as traditional advertising does not yield significant results.

Stock based compensation in the third quarter of 2007 was \$26,417 versus \$14,650 in the corresponding period of 2006. This was the result of a timing difference and numbers of options granted in 2007 versus the third quarter in 2006. Stock based compensation continues to be an effective non-cash method to attract the senior experienced management that AMS requires to drive the Company forward.

AMS' Professional Fees decreased by \$162,333 in third quarter 2007 over 2006, primarily due to reduced audit fees for 2006. Computer Services was \$33,225 in the third quarter of 2006 versus \$68,100 for the same period of 2007 and increase of \$34,875. This increase was due to the upgrading of office computer systems and increased staff levels. Interest and bank charges were \$4,678 during the third quarter of 2007 versus a recovery of \$9,123 during the same period of 2006. The increase was largely due to a \$12,137 interest reversal in the second quarter of 2006.

Salaries continue to be the main cost of doing business for AMS. We are hiring good qualified personnel on an ongoing basis as our customer base grows and AMS is preparing for the growth of the company as a result of our strategic business alliances that are opening many opportunities for rapid growth in sales. As a result, Salaries and benefits increased from \$489,848 in the third quarter of 2006 to \$1,003,665 in the third quarter of 2007.

All other expenses are tracking as planned.

Research and Development

Research and development costs are being expensed as incurred. The third quarter development costs for 2007 were \$72,374 as compared to \$108,562 in 2006, a decrease of \$36,188 which is a result of decreased direct research and development activity in the quarter versus the previous year and increased emphasis on product delivery. However, the Company continues its ongoing design, testing, and certification of afirs and the design and testing of UpTime to add aircraft types to its approved installation list. We do not anticipate this trend to continue. There are also minor expenses being incurred in the preliminary phases of AeroQ.

Foreign Exchange

All international sales of the Company's products and services are denominated in U.S. dollars. Accordingly, the Company is susceptible to foreign exchange fluctuations. The strength of the Canadian dollar and the fact that a majority of the Company's accounts receivable are denominated in United States dollars would have resulted in foreign exchange losses but purchases of U.S. dollar denominated services and supplies offsets these losses creating foreign exchange gain of \$5,168 in the third quarter of 2007 as compared to foreign exchange loss of \$2,853 for the same period in 2006.

Liquidity and Capital Resources

At September 30, 2007 the Company had working capital of \$4,527,745 compared to a working capital of \$4,656,127 in the same period in 2006, a decrease of \$128,382. The decrease in the working capital is attributed primarily to decreased cash of \$133,952 due to increased sales and afirs box shipments which led to increased receivables of \$15,934 and increased unearned revenue of \$76,906. Also, inventory has increased by \$894,853 offset by increased accounts payable of \$919,349, which is the result of the stocking up of inventories to meet customer installation schedules for the coming quarters, the movement of assembly in-house from third parties to reduce costs, and turn around times. Other factors are an increase in prepaid expenses of \$131,916, an increase in deferred lease inducement of \$13,687 and obligation under capital lease increase of \$23,725.

Management Discussion and Analysis

The Company's ability to continue is dependent upon attaining and sustaining profitable operations and obtaining additional financing in order to fund its working capital requirements and on-going operations. The Company's ability to attain profitable operations and positive cash flow in the future is dependent upon various factors, including its ability to acquire new customer contracts, the success of management's continued cost controls, and general economic conditions.

The Company currently has no bank debt and has an operating line of \$250,000 which bears an interest rate of Canadian chartered bank prime plus 1.0%, and is secured by assignment of cash collateral and a general security agreement.

Summary of Quarterly Results

	Q2-05	Q3-05	Q4-05	Q1-06	Q2-06	Q3-06	Q4-06	Q1-07	Q2-07	Q3-07
Revenue	\$ 115,582	\$ 107,271	\$ 132,669	\$ 218,328	\$ 298,852	\$ 258,813	\$ 318,473	\$ 837,218	\$ 473,122	\$ 312,684
Loss	687,659	600,000	1,127,856	1,166,402	965,349	1,176,113	1,231,842	809,265	1,978,629	1,693,258
Loss/Share \$	0.04	\$ 0.03	\$ 0.05	\$ 0.04	\$ 0.03	\$ 0.03	\$ 0.02	\$ 0.01	\$ 0.03	\$ 0.03

Contingencies

During the third quarter of 2007 AMS was served with two legal actions instigated by the same plaintiff. As well, the same party instituted a patent re-examination with the United States Patent Office to have the AMS patent re-examined. The Company strongly believes that the actions are without merit and it will defend itself vigorously, that the patent issued by the United States Patent Office in 2007 is valid and that the re-examination request will be refused. Since the amount of liability is undermined at this time, no liability has been accrued for claims on these actions and any amounts awarded as a result of the actions will be reflected in the year the amounts become reasonably estimable. The details are as follows.

In September 2007, the Company among others were served with a counterclaim alleging that the Company induced a breach of contract and interfered with economic relationships. Subsequent to September 30, 2007 the Company filed a Statement of Defense and a counterclaim in the amount of \$15,000,000 against three parties for their interference with legally binding contracts, disrupted business, attacks on the Company's reputation, and costs.

In September 2007, the Company was served with a claim of patent infringement seeking unspecified damages. AMS is working with patent experts in Washington D.C and its Canadian patent attorney to have the matter resolved.

AMS takes intellectual property rights and contractual arrangements of both its own, and other parties very seriously, and will defend and uphold them as required.

Commitments

The Company has entered into various leases for its operating premises and equipment. Future minimum annual payments under these operating leases are as follows:

	Premises	Equipment	Total
2007	\$ 47,758	\$ 4,261	\$ 52,019
2008	\$ 191,033	\$ 17,043	\$ 208,076
2009	\$ 44,801	\$ 7,081	\$ 51,882
	<u>\$ 283,592</u>	<u>\$ 28,385</u>	<u>\$ 311,977</u>

In addition, the Company has repayment obligations related to two Government of Canada loan programs. Under the Industrial Research Assistance Program (IRAP), the Company has received \$334,436, which is to be repaid as a percentage of gross revenues over a five to ten year period commencing in October 2006. Under the Technology Partnerships Canada (TPC) program, the Company has received \$104,523 to be repaid over a ten year period commencing in April 2006.

Management Discussion and Analysis

Looking Forward

The Company has been developing a sales network around the world to leverage its marketing and delivery capabilities. In January, Meggitt Aerospace, a world leader and supplier of aerospace sensor and monitoring equipment, finalized a licensing agreement with AMS to jointly market our product and services. Meggitt has equipment installed on nearly every jet aircraft in the world with its engine sensor, monitoring systems, and other products. Since the initial signing of an agreement in June 2006, Meggitt has opened doors into the OEM market. AMS is currently completing an RFP for a major manufacturer to be included on their new jets. This is a significant move forward in our current projected marketing timeline.

Various strategic relationships leverage our marketing capability worldwide, as these leading organizations have completed their due diligence on AMS' product and service capabilities. The inclusion of AMS as a strategic relationship with Meggitt provides AMS a higher standard of credibility with all customers around the world. We are seeing the results through increased activity in airlines contacting our sales group and being asked to visit and speak with the major OEMs around the world.

The Company is working with a number of end user application developers and Electronic Flight Bag (EFB) providers to provide a one-stop solution for a number of our current and new clients. These providers are world leaders in their space and we continue to win contracts because of these relationships.

The Company, in conjunction with its intense sales efforts, during the third quarter has continued to build on second quarter initiatives to focus resources on customer installations and deliverables. This will enable AMS to fully maximize the revenue per installed afirs and reduce the time from initial installation of an afirs unit on an aircraft to maximum billing. In addition, these efforts will enhance the ability to grow the revenue base of existing installations through additional service offerings.

With the addition of a VP Sales & Marketing during the quarter who has extensive experience in solution based sales and the addition of a senior major airline operations and engineering executive as interim Chief Operating Officer subsequent to the end of the quarter, AMS has the depth of knowledge and experience to expand its market penetration and take the Company to a higher level of integration within an airline.

Changes in Accounting Policy

Effective January 1, 2007, the Company adopted the new recommendation of the Canadian Institute of Chartered Accountants (CICA) under CICA Handbook Section 1530 Comprehensive Income, Section 3251 Equity, Section 3855 Financial Instruments – Recognition and Measurement, and Section 3861 Financial Instruments – Disclosure and Presentation. These new Handbook sections, which apply to fiscal years beginning on or after January 1, 2007, provide requirements for the recognition and measurement of financial instruments. Section 1530 establishes standards for reporting and presenting comprehensive income, which is defined as the change in equity from transaction and other events from non-owner sources. Other comprehensive income refers to items recognized in comprehensive income but are excluded from net income calculated in accordance with Canadian Generally Accepted Accounting Principles (GAAP).

Under Section 3855, all financial instruments are classified into one of five categories: held-for trading, held-to-maturity investments, loans and receivables, available-for-sale financial assets, or other financial liabilities. All financial instruments are measured in the balance sheet either at fair value except for loans and receivables, held-to-maturity investments, and other financial liabilities, which are measured at amortized cost. Subsequent measurement and changes in fair value will depend on their initial classification, as follows: held-for-trading financial assets are measured at fair value, and changes in fair value are recognized in net income. Available-for-sale financial instruments are measured at fair value with changes in fair value recorded in other comprehensive income until the instrument is derecognized or impaired.

The adoption of these new standards had no impact on the Company's accounts and deficit position as at January 1, 2007. As a result of the adoption of these new standards, the Company has classified its cash and cash equivalents as held-for-trading. Accounts receivable are classified as loans and receivables. Accounts payable, certain accrued liabilities and notes payable are classified as other liabilities all of which are measured at amortized cost.

Management Discussion and Analysis

Internal Control over Financial Reporting and Disclosure Control

The Company's Chief Executive Officer and Chief Financial Officer have designed or caused to be designed under their supervision internal controls over financial reporting to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with Canadian GAAP.

Please see page 28 of the Company's Annual Report for the fiscal year ended December 31, 2006 for a discussion of internal controls over financial reporting and disclosure controls. We reported that management had identified three areas of disclosable weakness in internal controls related to financial reporting system, segregation of duties, controls over information systems, and steps that would be taken to remediate each of these weaknesses during the current year.

During the quarter ended September 30, 2007, the Company did not make any changes to its internal control over financial reporting that would have materially affected, or would likely materially affect, such controls. We will take steps to address the weaknesses identified during the remainder of fiscal 2007 where feasible and cost effective. During the quarter the addition of a designated accountant as Controller to fill the position vacated as the result of a retirement, will allow for some changes to remediate the weaknesses.

