

Management's Discussion and Analysis

The Company and its representatives periodically make written and oral statements, including those contained in the Annual Report and Management's Discussion and Analysis, which may pertain to the Company or the environment in which Automodular operates. These statements should be read in conjunction with the Consolidated Financial Statements and the accompanying notes.

By their nature, forward-looking statements are subject to risks and uncertainties, which could result in actual performance or conditions being materially different from anticipated results. Readers should not place undue reliance on these forward-looking statements when making decisions and should consider the date on which the statements were made. Except as required by applicable securities law, management disclaims any intention or obligation to publicly update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

OVERVIEW

Automodular Corporation is a sequencer and sub-assembler of modules that are installed in cars and trucks assembled by General Motors at plants in Canada and the United States. Following the acquisition of Tec-Mar Distribution Services, Inc. in January 2003, Automodular now operates through three plants in Canada and five in the United States employing more than 1,000 people. The following information does not reflect financial results for Tec-Mar.

SALES AND NET INCOME

Automodular Corporation's net sales for the year ended December 31, 2002 were \$56 million—an increase of \$3 million, or 6% over the year ended December 31, 2001. Net income was \$4.6 million or \$0.25 per share, versus \$4.3 million or \$0.29 per share in the prior year, owing to more shares outstanding in 2002. Automodular's 2002 income statement ratios compare to 2001 as follows:

	2002	2001
Sales	100.0%	100.0%
Operating income	15.8%	16.7%
Other income	2.3%	3.4%
Depreciation and amortization	6.0%	6.7%
EBIT	12.2%	13.4%
Interest expense	0.1%	1.0%
Income tax	3.8%	4.1%
Net income	8.3%	8.2%

OPERATING INCOME

Operating income declined from 16.7% of sales to 15.8% of sales as a result of contractual price declines and annual wage rate increases, which could not be fully offset by productivity improvements. Automodular generally shares productivity gains with its customer by reducing prices by an amount equal to two-thirds of cost improvement realized.

OTHER INCOME

Other income declined by 1.1% of sales, reflecting lower securities gains. Automodular no longer maintains an investment portfolio, and does not expect material amounts of other income in future years.

DEPRECIATION AND AMORTIZATION

Depreciation and amortization declined from 6.7% of sales in 2001 to 6.0% of sales in 2002. These expenses are expected to rise in 2003 owing to higher capitalized expenditures in 2002 than in 2001. The higher capitalized expenditures arose in part from the move from two Pickering locations to the newly constructed Whitby plant, which took place in January 2002.

EARNINGS BEFORE INTEREST AND TAX

2002 EBIT of 12.2% was down slightly from 13.4% in 2001. Lower depreciation and amortization expense did not fully offset lower margin ratios.

INTEREST EXPENSE

Automodular eliminated bank indebtedness during 2002, resulting in lower interest charges. Automodular borrowed approximately \$17.5 million in early 2003 to fund the Tec-Mar acquisition, and expects commensurately higher interest charges in 2003.

INCOME TAXES

Income tax ratios fell in 2002 as a result of lower tax rates and a larger mix of non-taxable gains included in other income. Automodular expects 2003 income tax rates to be slightly lower than 2002 on operating income, but anticipates no material amounts of non-taxable gains.

NET INCOME

Net income as a percentage of sales grew to 8.3% in 2002 from 8.2% in 2001. For 2003, Automodular expects this ratio to decline as a result of the consolidation of the lower-margin Tec-Mar acquisition and the absence of any material amounts of non-operating income. On a pro forma basis, net income as a percentage of sales would have been 5.5% in 2002 had Tec-Mar been consolidated throughout that year.

LIQUIDITY AND CAPITAL RESOURCES

\$11.0 million cash was generated from operating activities in the current fiscal period compared to \$4.7 million in 2001, largely as a result of improved management of non-cash working capital. At year end, the Corporation had \$18 million cash or equivalent on hand. However, the Tec-Mar acquisition in early 2003 consumed approximately \$36.8 million cash, funded by the usage of available cash and a \$17.5 million term loan. The Corporation also has a \$5 million operating line and believes it has sufficient liquidity to meet all plans and programs contemplated for 2003, while continuing to pay regular quarterly dividends.

CAPITAL EXPANSION

In the current period, the Company expended \$3.2 million on capital and other assets, compared to \$1.9 million in the prior period. The increased capital outlays reflect the capitalized costs arising from the consolidation of two Pickering plants in the new Whitby plant in January 2002.

DIVIDENDS

Dividends paid in the current year were \$5.3 million compared with \$6.8 million in the prior period. The Directors of Automodular approved a policy of paying regular quarterly dividends and set the current rate at \$0.28 annually. Automodular's operations are expected to generate sufficient cash flow to fund this dividend while meeting all operating requirements and the terms of the Corporation's banking agreements.

EQUITY

Shareholders' equity remained unchanged at \$39 million, reflecting the Corporation's dividend policy.

OUTLOOK

The automotive parts industry faces lower volumes in 2003. The Tec-Mar acquisition broadens and strengthens Automodular as it will more than double our annual sales and will make a meaningful contribution to net income and cash flow despite the industry slowdown. The Company's balance sheet reflects management's judgment on the valuation of the assets, and management feels the Company is poised for further growth through expansion of its automotive parts sub-assembly and sequencing operations and other opportunistic acquisitions in the automotive sector. The capital requirements for any expansion will be met initially through internally generated funds and selectively through issuance of additional shares.

As set out in Note 15 to the Corporation's financial statements, the Corporation has prepared a pro forma income statement as though the Tec-Mar acquisition had taken place January 1, 2002. This analysis provides a benchmark for investors to analyze the impact of this acquisition. The pro forma shows Automodular would have earned \$6.5 million or \$0.35 per share on sales of \$120 million in 2002 had Tec-Mar been included. Management believes the combined operations in 2003 will be more profitable than the pro forma 2002 results, tempered somewhat by the soft automotive market environment.