

**Management discussion and analysis of
operating results and
financial position**



Quarter ended June 30, 2006



MANAGEMENT DISCUSSION AND ANALYSIS

For the Second quarter ended June 30, 2006

The purpose of this Management Discussion & Analysis (“MD&A”) is to help the reader understand our development strategy, our future expectations, evaluate our performance in relation to our objectives and the manner in which we manage risks and dispose of available financial resources. The MD&A should be read in conjunction with the interim consolidated financial statements for the quarter ended June 30, 2006, the annual MD&A and the audited consolidated financial statements and related notes for the year ended December 30, 2005 which are included in the Company’s annual report. The Company’s quarterly and annual reports as well as other information documents are available on SEDAR

Company activity, profile and strategy

Roctest designs, manufactures and markets sensors and high-precision measuring instruments for the civil engineering, energy, healthcare and industrial control markets. The Company is recognized for its leading-edge technology, the quality of its technical expertise and its product development capabilities for challenging and demanding environments.

The Company’s products are mainly sold internationally. A commercial development network consisting of agents and distributors allows the Company to seize business opportunities throughout the world. During the last fiscal year, Roctest generated more than 80% of its revenues outside of Canada.

The Company is comprised of two distinct sectors, industrial and civil engineering. The industrial sector is mainly based on fiber optics technology and is an emerging sector offering numerous growth opportunities. With regards to the civil engineering sector, with approximately 10% of the world’s market for measuring

(www.sedar.com) and on the Company’s website (www.roctest.com).

In order to facilitate different business processes and maintain a comparable basis with previous years, the Company has adopted, in 2005, a new fiscal calendar consisting of four quarters of 13 weeks each.

In the present document, unless otherwise indicated, all financial information is prepared in accordance with Canadian Generally Accepted Accounting principles (GAAP). All amounts are in Canadian dollars. To facilitate reading of this MD&A, the terms “Company” “we” “our” “us” all refer to Roctest Ltd.

instruments, we will continue to deploy significant efforts in order to capitalize on the many opportunities available to innovative firms such as Roctest.

On a general basis, the Company will maintain its strategic focus on developing markets in China, the USA, Europe and South America for its products both for the civil engineering and the industrial sectors.

More specifically, the strategy for FISO Technologies Inc., a subsidiary of the Roctest Group specialized in the manufacturing and commercialization of fiber optic sensors, is to stimulate organic growth of its revenues by concluding agreements that will allow it to position itself as a preferred supplier to original equipment manufacturers (OEM). As for the civil engineering sector, its strategy will be to position itself as a consolidator in a highly fragmented and competitive market and by offering innovative products.

We continue to focus on concluding new OEM agreements in our industrial sector thereby increasing the importance of OEM clients in this sector's sales. These agreements provide numerous advantages on an operational level. Sales from OEM agreements are recurring, thereby enabling us to reduce production costs and facilitate production planning and product improvements.

In the civil engineering sector, integrating technologies based on fiber optics, such as distributed sensing, will allow us to offer complete and attractive global solutions for our clients' various needs.

To that effect, the acquisition of Smartec SA, ("Smartec"), which closed on May 19, 2006, will position us as the only manufacturer of measuring instruments for the geotechnical and civil engineering markets to offer a complete set of technologies and solutions to meet the requirements of many challenging and demanding environments.

Smartec is a Swiss-based leading developer, producer and distributor of measurement and structural health monitoring systems using technologies based on distributed fiber optic. This company sets standards for innovation, quality, ease of use and durability. This transaction was carried out through the issuance of 360,000 treasury common shares at a price of \$2.50 per share, which was the market value at the transaction date, for a total value of \$900,000, a cash consideration amounting to \$947,909 and an amount of \$92,030 payable 24 months after closing subject to any potential claims resulting from the Share Purchase Agreement.

As of June 30, 2006, the Company has identified transaction costs of \$135,513 bringing the total transaction value to \$2,075,452.

During the quarter ended June 30, 2006, consolidated results include the results of Smartec from May 19, 2006. During this period, Smartec had revenues of \$0.21 million and recorded a loss of \$0.04 million. We are confident that Smartec will contribute positively to consolidated earnings in the near future.



Results of Operations and Financial Position

	For the three month periods ended				For the six month periods ended			
	June 30, 2006		July 1, 2005		June 30, 2006		July 1, 2005	
	\$	% of sales	\$	% of sales	\$	% of sales	\$	% of sales
Consolidated earnings data								
Sales	5,250,513	100.0	5,437,892	100.0	9,695,564	100.0	10,658,590	100.0
Cost of sales	3,072,014	58.5	3,199,034	58.8	5,851,584	60.4	6,369,348	59.8
Gross profit	2,178,499	41.5	2,238,858	41.2	3,843,980	39.6	4,289,242	40.2
Sales and administration expenses	1,809,977	34.5	1,721,317	31.7	3,327,707	34.3	3,101,420	29.1
Other administration, research and development and amortization expenses	726,210	13.8	662,412	12.2	1,376,034	14.2	1,317,804	12.3
Foreign exchange loss (gain)	160,103	3.0	(50,936)	(1.0)	185,395	1.9	27,158	0.3
Loss before income taxes	(517,791)	(9.8)	(93,935)	(1.7)	(1,045,156)	(10.8)	(157,140)	(1.5)
Provision for (recovery of) income taxes	(133,488)	(2.5)	(103,057)	(1.9)	(363,351)	(3.7)	(116,971)	(1.1)
Net earnings (loss)	(384,303)	(7.3)	9,122	0.2	(681,805)	(7.1)	(40,169)	(0.4)
Earnings (loss) per share								
Diluted and Basic	(0.07)		0.00		(0.13)		(0.01)	
Weighted average number of shares outstanding	5,244,496		4,447,886		5,244,496		4,447,886	

	June 30, 2006	December 30, 2005
	\$	\$
Balance sheet data		
Working capital ⁽¹⁾	8,936,080	9,734,270
Property, plant and equipment	5,545,415	5,126,273
Total assets	26,534,627	24,401,305
Total debt	4,764,266	2,436,935

(1) Working capital is defined as current assets minus current liabilities.

ANALYSIS OF FINANCIAL RESULTS OF THE SECOND QUARTER 2006

During the second quarter ended June 30, 2006, earnings before interest, income taxes and amortization (“EBITDA”) were (\$132,582) compared to \$240,704 in the second quarter of 2005. For the six-month period ended June 30, 2006, EBITDA was at (\$353,290) while it amounted to \$533,186 in 2005

The second quarter decrease in EBITDA results mainly from a decrease of \$0.06 million in gross margin mostly related to sales volume, an increase in sales and administration costs of \$0.09 million compared to the same quarter of 2005 and by a foreign exchange loss of \$0.16 million compared with a foreign exchange gain of \$0.05 million in 2005.

The gross margin as a percentage of sales posted a slight increase of 0.3% notwithstanding the exchange rate impact. The average exchange rates for the quarter, for the US dollar and Euro, have decreased by 9.8% and 10% respectively in comparison to 2005 which also had an impact on reducing gross margins.

Had the average foreign exchange rates remained at the same level as in 2005, the gross margin of 2006 would have increased by \$0.38 million.

Revenue

For the second quarter ended June 30, 2006, consolidated revenue reached \$5.25 million, a decrease of 3.4% compared to 2005. The civil engineering sector posted sales of \$3.83 million while sales in the industrial sector were of \$1.42 million.

The quarter’s revenues from the civil engineering sector decreased by 6.4% while the industrial sector registered a 5.5% increase in revenues. Revenues from the healthcare market increased by 65% while those from the energy market declined by 20% compared to the corresponding period in 2005.

A decrease in prices due to increased competition in the energy market is the main reason for the decrease of revenues in that market.

The decrease in revenues generated by the civil engineering sector in comparison to the corresponding period in 2005 is mainly attributable to important delays in the reception of orders from the Middle-East, namely Iran, and from the report of certain projects requested by our clients in Europe.

The increase in revenues from the industrial sector, compared with the same period in 2005, derives mainly from OEM client orders, therefore confirming that the strategy implemented last year, aimed at positioning ourselves as a preferred supplier for OEM clients is showing positive results.

In addition, during the quarter, progress in the development of many products aimed at various clients from the industrial control market was achieved and showed interesting potential.

The order book of the Company and its subsidiaries stands at \$4.13 million as at June 30, 2006, compared to \$3.97 million for the corresponding period in 2005.

Sales and administration

Compared to the second quarter of 2005, sales and administration expenses increased by \$0.09 million to stand at 34.5% of revenue, while they totaled \$1.72 million and represented 31.7% of revenue in 2005.

The increase in expenses comes mainly from hiring sales personnel at the end of the previous fiscal year in order to increase our presence in the Western US market and for our Hong Kong subsidiary.

Research and Development

Research and development (“R&D”), net of grants and income tax credits, reached \$0.36 million and represents 6.9% of revenue, an increase of 7.6% compared to 2005. This increase, attributable mainly to the civil engineering sector, includes R&D expenses incurred by Smartec and reflects our strategy of higher investments in new product development for the civil engineering sector.

Amortization of Capital Assets

Amortization of capital assets stood at \$0.32 million compared to \$0.28 million in 2005, an increase of 13.4%. During the quarter ended June 30, 2006, the Company capital expenditures totaled \$0.30 million.

The new capital expenditures are comprised mainly of new drilling equipment and a truck acquired under a capital lease by one of our French subsidiaries, EN.OM.FRA, SAS.

Interest and Foreign Exchange

The Company incurred interest expenses mainly on its long term debt which remained relatively stable compared to the same period of 2005. New debt contracted at the end of the quarter, combined with the fact that previous debt balances are rapidly diminishing, had no impact on the long-term interest expenses on a comparative basis.

The Company is exposed to foreign exchange adjustment risks. During the second quarter of 2006, fluctuations of the US dollar and the Euro resulted in a loss of \$0.16 million while these fluctuations during the second quarter of 2005 had resulted in a gain of \$0.05 million.

To reduce foreign exchange risks, the Company enters into forward exchange collars for the sale of US dollars with a floor varying from \$1.0845 to \$1.1344 and a cap varying from \$1.1533 to \$1.2060. As at June 30, 2006 those contracts represented an amount of US\$3.0 million compared to US\$1.60 million at December 30, 2005.

Income Taxes

Income taxes, as a percentage of revenue, represent a recovery of 25.8% of earnings before taxes, compared with 109.7% for the second quarter of 2005. The rate reflects a mix of the various income tax rates in the Canadian provinces and foreign jurisdictions in which the Company operates. This rate fluctuates depending on the proportion of net income by jurisdiction to consolidated net income.

The recovery of the second quarter of 2005 included prospective income tax benefits from losses carried forward of a subsidiary that were not previously recorded.

Net Income (loss)

The Company incurred a loss of \$384,303, or \$0.07 per share, compared with earnings of \$0.01 million, or \$0.00 per share, for the same period in 2005. The loss is mainly attributable to a 3.4% decrease in sales, an increase in sales and administration expenses as a percentage of revenue to 34.5% of revenue, and a loss on foreign exchange of \$0.16 million. Compared to the same period of 2005, the earnings of \$0.01 million were attributable mainly to lower sales and administration costs representing 31.4% of revenues, a foreign exchange gain of \$0.05 million and an income tax recovery of \$0.1 million.

Cash Flows from Operations

Cash flow from operations was a use of \$1.22 million compared to \$0.37 million in 2005. The increase results mainly from a loss of \$0.38 million as opposed to earnings of \$0.01 million in 2005 and a negative increase in non cash working capital of \$0.46 million. The working capital decreased by \$0.80 million compared to December 30, 2005.

Liquidity and Share Capital and Stock Options

At June 30, 2006, the Company had \$2.59 million in cash and cash equivalents and temporary investments, net of bank advances, compared to \$4.18 million as at December 30, 2005. The cash and cash-equivalents are made up of cash on hand, bank balances, and short-term investments with maturity dates equal to or less than three months. During the second quarter, the Company contracted a new debt in the amount of \$1.75 million in order to finance its acquisition of Smartec, it also entered into capital lease commitments for an amount of \$0.26 million.

At the end of the second quarter of 2006, there were 5,563,071 common shares issued and outstanding. The Company issued 360,000 common shares at a price of \$2.50 per share on May 19, 2006, for the acquisition of Smartec.

During the second quarter of 2006, the Company granted 50,000 stock options. The cost of stock-based compensation, using the fair value method of accounting, was recognized in net earnings with the corresponding credit to contributed surplus for an amount of \$0.03 million compared with \$0.03 million in 2005.

Risks and uncertainties

For discussion of the risks that could affect our business, please refer to our 2005 annual MD&A.

Since December 30, 2005 there have been no significant changes to the risks and uncertainties which could affect the Company

Certain of the risk factors which could cause results or events to differ materially from current expectations include the following: the length of the sales cycle and the fact that certain contracts are subject to delay, the capacity of the Company to efficiently maintain new product development at a high level, currency fluctuations and international events

Forward-looking statements

Certain statements made in this MD&A may constitute forward-looking statements and are subject to significant risks and uncertainties which are difficult to predict and assumptions which may prove to be inaccurate. The results or events predicted in these statements may differ materially from actual results or events.

The forward-looking statements contained in this document represent the Company's expectation as of July 28, 2006 and, accordingly, are subject to change after that date. However, the Company disclaims any intention to update or revise any forward-looking statements whether as a result of new information, future events or otherwise

On behalf of Management,

(Signed)

Michel Plante
Chief Financial Officer
July 28, 2006

Quarterly Review

Financial Information (in millions of dollars, except for per share amount)

	2006				2005			
	Q1	Q2	Q3	Q4	Q1	Q2	Q3	Q4
SALES	4.44	5.25			5.22	5.44	4.93	5.28
COST OF SALES	2.78	3.07			3.17	3.20	2.55	3.34
GROSS MARGIN	1.66	2.18			2.05	2.24	2.38	1.94
EXPENSES								
Sales and administration	1.51	1.81			1.38	1.72	1.49	1.66
Scientific Research Cost	0.61	0.67			0.54	0.58	0.53	0.48
Grants and scientific tax credits	(0.26)	(0.31)			(0.24)	(0.24)	(0.24)	(0.80)
Interest on Long-term debt	0.04	0.04			0.04	0.04	0.04	0.04
Amortization	0.26	0.32			0.31	0.28	0.25	0.41
Foreign Exchange Gain (Loss)	(0.03)	(0.16)			(0.08)	0.05	(0.27)	0.05
	2.19	2.69			2.11	2.33	2.34	1.74
EARNINGS (LOSS)								
Before Income Taxes	(0.53)	(0.51)			(0.06)	(0.09)	0.04	0.20
INCOME TAXES	(0.23)	(0.13)			(0.01)	(0.10)	(0.09)	0.08
NET EARNINGS (LOSS)	(0.30)	(0.38)			(0.05)	0.01	0.13	0.12
PER COMMON SHARE								
Basic	(0.06)	(0.07)			(0.01)	0.00	0.03	0.03
Diluted	(0.06)	(0.07)			(0.01)	0.00	0.03	0.03
EBITDA	(0.22)	(0.13)			0.29	0.24	0.33	0.68
TOTAL ASSETS	23.70	26.53			22.07	21.15	21.49	24.40