DIRTT Environmental Solutions Ltd.

Unaudited Condensed Consolidated Financial Statements

For the three and six months ended June 30, 2016 and 2015

INDEX

DIRTT Environmental Solutions Ltd.
Condensed Consolidated Statements of Financial Position
(Unaudited - Stated in thousands of Canadian dollars)

As at	Notes	June 30, 2016	December 31, 2015
		$	$
ASSETS			
Current Assets			
Cash and cash equivalents		93,872	91,405
Trade and other receivables		15,617	23,574
Inventory		18,796	21,619
Prepaids and other current assets		1,849	1,614
		130,134	**138,212**
Non-current Assets			
Property, plant and equipment		52,322	48,236
Intangible assets		17,399	15,225
Note receivable	9	431	443
Deferred tax assets		8,054	7,279
Goodwill		1,845	1,845
Other assets		880	1,010
Total Assets		**211,065**	**212,250**
LIABILITIES			
Current Liabilities			
Trade accounts payable and other liabilities		21,202	23,597
Customer deposits		6,423	7,094
Current portion of long-term debt	5	2,476	3,663
		30,101	**34,354**
Non-current Liabilities			
Deferred tax liabilities		1,224	1,559
Long-term debt	5	9,280	5,498
Total Liabilities		**40,605**	**41,411**
SHAREHOLDERS' EQUITY			
Common share capital		194,421	193,984
Warrants		37	37
Share-based payment reserve		9,084	6,865
Accumulated other comprehensive income		7,332	9,277
Accumulated deficit		(40,414)	(39,324)
		170,460	**170,839**
Total Liabilities and Shareholders' Equity		**211,065**	**212,250**
Commitments	12		

The accompanying notes are an integral part of these condensed consolidated financial statements.

DIRTT Environmental Solutions Ltd.

Condensed Consolidated Statements of (Loss) Income and Comprehensive (Loss) Income

(Unaudited - Stated in thousands of Canadian dollars)

		For the three months ended June 30,		For the six months ended June 30,	
		2016	**2015**	**2016**	**2015**
	Notes	$	$	$	$
Revenue		61,252	52,866	117,175	109,567
Cost of goods sold		33,925	31,453	65,782	64,353
Gross profit		**27,327**	**21,413**	**51,393**	**45,214**
Expenses					
Selling, general and administrative		27,543	22,544	50,689	42,615
Operating (loss) income		**(216)**	**(1,131)**	**704**	**2,599**
Other expenses (income)					
Foreign exchange loss (gain)		341	(2)	1,006	(1,215)
Interest income		(148)	(118)	(308)	(177)
Finance costs		62	107	138	205
		255	**(13)**	**836**	**(1,187)**
(Loss) income before tax		**(471)**	**(1,118)**	**(132)**	**3,786**
Income taxes					
Current tax expense		1,680	8	2,219	52
Deferred tax (recovery) expense		(693)	237	(1,261)	415
		987	**245**	**958**	**467**
Net (loss) income for the period		**(1,458)**	**(1,363)**	**(1,090)**	**3,319**
Other comprehensive (loss) income					
Items that will be reclassified to profit or loss:					
Exchange differences on translation of foreign operations		1	(316)	(1,945)	2,702
Comprehensive (loss) income for the period		**(1,457)**	**(1,679)**	**(3,035)**	**6,021**
(Loss) income per share					
Basic and diluted		(0.02)	(0.02)	(0.01)	0.04
Weighted average number of shares outstanding					
Basic	7	84,597,751	79,725,135	84,564,661	78,268,013
Diluted	7	84,597,751	79,725,135	84,564,661	80,401,165

The accompanying notes are an integral part of these condensed consolidated financial statements.

DIRTT Environmental Solutions Ltd.

Condensed Consolidated Statements of Changes in Equity

(Unaudited - Stated in thousands of Canadian dollars)

	Common share capital	Warrants	Share-based payment reserve	Accumulated other comprehensive income	Accumulated deficit	Total equity
	$	$	$	$	$	$
As at December 31, 2014	**143,386**	**526**	**5,440**	**3,661**	**(57,216)**	**95,797**
Net income for the period	-	-	-	-	3,319	3,319
Other comprehensive income for the period	-	-	-	2,702	-	2,702
Issued upon completion of bought deal	43,211	-	-	-	-	43,211
Share capital issuance costs	(2,598)	-	-	-	-	(2,598)
Stock-based compensation	-	-	1,243	-	-	1,243
Issued on exercise of stock options	2,949	-	(857)	-	-	2,092
Issued on exercise of warrants	3,031	(489)	-	-	-	2,542
As at June 30, 2015	**189,979**	**37**	**5,826**	**6,363**	**(53,897)**	**148,308**
As at December 31, 2015	**193,984**	**37**	**6,865**	**9,277**	**(39,324)**	**170,839**
Net loss for the period	-	-	-	-	(1,090)	(1,090)
Other comprehensive loss for the period	-	-	-	(1,945)	-	(1,945)
Stock-based compensation	-	-	2,343	-	-	2,343
Issued on exercise of stock options	437	-	(124)	-	-	313
As at June 30, 2016	**194,421**	**37**	**9,084**	**7,332**	**(40,414)**	**170,460**

The accompanying notes are an integral part of these condensed consolidated financial statements.

DIRTT Environmental Solutions Ltd.
Condensed Consolidated Statements of Cash Flows
(Unaudited - Stated in thousands of Canadian dollars)

	For the three months ended June 30,		For the six months ended June 30,	
	2016	**2015**	**2016**	**2015**
	$	$	$	$
Cash flows from operating activities:				
Net (loss) income for the period	(1,458)	(1,363)	(1,090)	3,319
Adjustments:				
Depreciation included in cost of goods sold	899	812	1,642	1,522
Depreciation and amortization included in selling, general and administrative	2,806	2,121	5,531	4,135
Stock-based compensation	1,171	614	2,343	1,243
Interest income	(148)	(118)	(308)	(177)
Finance costs	62	107	138	205
Income tax provision	987	245	958	467
Non-cash foreign exchange loss (gain) on debt revaluation	11	(94)	(306)	299
Non-cash foreign exchange loss (gain)	261	(268)	183	(584)
Net change in non-cash working capital relating to operating activities	9,864	10,612	8,450	6,569
Cash interest received	148	118	308	177
Cash taxes paid	(990)	(102)	(2,968)	(230)
Other non-cash adjustments	55	-	55	-
Net cash flows provided by operating activities	**13,668**	**12,684**	**14,936**	**16,945**
Cash flows from investing activities:				
Purchase of property, plant and equipment	(5,707)	(5,952)	(10,575)	(8,097)
Capital expenditures on internally generated intangible assets	(1,822)	(1,252)	(4,245)	(3,507)
Other	10	8	16	13
Net cash flows used in investing activities	**(7,519)**	**(7,196)**	**(14,804)**	**(11,591)**
Cash flows from financing activities:				
Issuance of share capital on bought deal offering	-	43,211	-	43,211
Share capital issuance costs	-	(2,598)	-	(2,598)
Issuance of share capital on exercise of stock options	186	1,048	313	2,092
Issuance of share capital on exercise of warrants	-	1,625	-	2,542
Proceeds of long-term debt	5,349	-	5,349	2,079
Repayment of long-term debt	(1,116)	(979)	(2,267)	(1,619)
Interest paid on long-term debt	(62)	(107)	(138)	(205)
Net cash flows provided by financing activities	**4,357**	**42,200**	**3,257**	**45,502**
Effect of foreign exchange on cash and cash equivalents	(157)	149	(922)	1,974
Net increase in cash and cash equivalents	10,349	47,837	2,467	52,830
Cash and cash equivalents, beginning of period	83,523	44,829	91,405	39,836
Cash and cash equivalents, end of period	**93,872**	**92,666**	**93,872**	**92,666**
Cash and cash equivalents consists of:				
Cash	11,373	11,533	11,373	11,533
Short-term investments	82,499	81,133	82,499	81,133
	93,872	**92,666**	**93,872**	**92,666**

The accompanying notes are an integral part of these condensed consolidated financial statements.

1. GENERAL INFORMATION

DIRTT Environmental Solutions Ltd. ("DIRTT" or the "Company") is a leading technology-driven manufacturer of highly customized interiors. DIRTT combines its proprietary 3D design, configuration and manufacturing software ("ICE®" or "ICE Software") with integrated in-house manufacturing of its innovative prefabricated interior construction solutions and an extensive Distribution Partner ("DP") network. ICE provides accurate design, drawing, specification, pricing and manufacturing process information, allowing rapid production of high-quality custom solutions using fewer resources than traditional manufacturing methods. ICE was developed by Ice Edge Business Solutions Ltd. ("Ice Edge"), a wholly owned subsidiary of DIRTT, and its wholly owned subsidiary, Ice Edge Business Solutions, Inc.

ICE is also licensed to unrelated companies and DPs through Ice Edge.

The address of DIRTT's registered office is 7303 - 30th Street S.E., Calgary, AB, Canada T2C 1N6.

DIRTT trades on the Toronto Stock Exchange ("TSX") under the symbol "DRT".

2. SIGNIFICANT ACCOUNTING POLICIES

The principal accounting policies applied in the preparation of these condensed consolidated financial statements are set out below. These policies have been consistently applied to all the periods presented, unless otherwise stated.

Statement of compliance
These condensed consolidated financial statements have been prepared in accordance with International Accounting Standard 34 Interim Financial Reporting ("IAS 34"). Accordingly, certain information and footnote disclosure normally included in annual financial statements prepared in accordance with International Financial Reporting Standards ("IFRS") have been omitted or condensed, and should be read in conjunction with the Consolidated Financial Statements of the Company for the year ended December 31, 2015.

The condensed consolidated financial statements were approved by the Board of Directors and authorized for issue on August 3, 2016.

Basis of measurement
These condensed consolidated financial statements have been prepared using the same policies and methods as those used in the audited consolidated financial statements for the year ended December 31, 2015.

The effect of foreign exchange on cash and cash equivalents held in foreign currencies in the condensed consolidated statements of cash flows for the comparative period has been reclassified to conform with the financial statement presentation adopted for the current year.

3. ADOPTION OF NEW AND REVISED IFRS

The Company has reviewed the impact of the new and revised accounting pronouncement outlined below, and has determined these standards did not have a material impact upon adoption on January 1, 2016.

In September 2014, the International Accounting Standards Board ("IASB") issued narrow-scope amendments to a total of four standards as part of its annual improvements process, "Annual Improvements to IFRS (2012-2014)". The IASB uses the annual improvements process to make non-urgent but necessary amendments to IFRS. These amendments will apply prospectively for annual periods beginning on or after January 1, 2016; earlier application is permitted, in which case the related consequential amendments to other IFRSs would also apply.

4. RECENT ACCOUNTING PRONOUNCEMENTS

The Company has reviewed new and revised accounting pronouncements that have been issued but are not yet effective and management is assessing the potential impact, if any, on the Company:

In January 2016, the IASB issued amendments to IAS 12 "Income Taxes". The amendments were related to the recognition of deferred tax assets for unrealized losses, which clarified how to account for deferred tax assets related to debt instruments measured at fair value. The amendments are effective for annual periods beginning on or after January 1, 2017, with earlier application permitted.

In January 2016, the IASB also issued amendments to IAS 7 "Statement of Cash Flows". The amendments will require entities to provide disclosures that enable users of financial statements to evaluate changes in liabilities arising from financing activities, including changes arising from cash flows and non-cash changes. The amendments are effective for annual periods beginning on or after January 1, 2017, with earlier application permitted.

In April 2016, the IASB issued amendments to IFRS 15 "Revenue from Contracts with Customers". The amendments clarified three aspects of the standard (identifying performance obligations, principal versus agent considerations and licensing) and provided some transition relief for modified contracts and completed contracts. The amendments are effective for annual periods beginning on or after January 1, 2018 (same effective date as IFRS 15 itself), with earlier application permitted.

In June 2016, the IASB issued amendments to IFRS 2 "Share-based Payment". The amendments clarified the standard in relation to the accounting for cash-settled share-based payment transactions that include a performance condition, the classification of share-based payment transactions with net settlement features and the accounting for modifications of share-based payment transactions from cash-settled to equity-settled. The amendments are effective for annual periods beginning on or after January 1, 2018, with earlier application permitted.

5. LONG-TERM DEBT

As at	June 30, 2016	December 31, 2015
	($ thousands)	
Capital financing facility, secured by a charge on all assets including manufacturing equipment, with 30 monthly payments of $143 plus interest at floating rates, which is based on the lender's Canadian prime rate minus 0.25% and 30 monthly payments of US$18 plus interest at floating rates, which is based on the lender's US prime rate minus 0.25%. Prior to March 31, 2016, the interest rate was prime plus 0.5%. The entire balance was repaid by June 30, 2016.	-	1,011
Capital financing facility, secured by a charge on all assets including manufacturing equipment, with 36 monthly payments of US$139 plus interest at floating rates, which is based on the lender's US prime rate minus 0.25%. Prior to March 31, 2016, the interest rate was prime plus 0.5%.	3,947	5,382
Term loan, secured by a charge on all assets including manufacturing equipment, with 60 monthly payments of US$21 plus interest at floating rates, which is based on the lender's US prime rate minus 0.25%. Prior to March 31, 2016, the interest rate was prime plus 0.5%.	2,422	2,768
Capital financing facility, secured by a charge on all assets including manufacturing equipment, with 48 monthly payments, commencing on April 1, 2017, plus interest at floating rates, which is based on the lender's US prime rate minus 0.25%.	5,387	-
	11,756	9,161
Less: Current portion of long-term debt	(2,476)	(3,663)
Long-term debt	9,280	5,498

In March 2016, the Company signed a fourth amendment to the amended and restated loan agreement with its lender, which included a reduction of interest rates on outstanding advances from prime plus 0.5% to prime minus 0.25% and a new capital financing facility of US$10.0 million. Debt covenants were adjusted to increase the minimum tangible net worth from $60.0 million to $135.0 million and to add a maximum capital expenditure limit of $40.0 million for 2016.

At June 30, 2016, $5.4 million (US$4.2 million) had been borrowed against the new US$10.0 million capital financing facility. At June 30, 2016 and December 31, 2015, $nil had been borrowed against the revolving operating facility. Advances under the revolving operating facility are subject to interest at the lender’s prime rate minus 0.25% for Canadian dollar advances and the US prime rate minus 0.25% for US dollar advances and are repayable at any time.

6. SHARE-BASED TRANSACTIONS

The Company has a stock option plan which is approved by the Board of Directors and by its shareholders at the most recent annual and special meeting of shareholders held on May 5, 2016, whereby the aggregate number of shares reserved for issuance shall not exceed 10% of the issued and outstanding common shares as at the time of grant of any options. Options granted under the plan generally have a term of five years and vest 1/3 every year over a three-year period from the date of grant. For the six months ended June 30, 2016, 2,500 options were granted (June 30, 2015 – nil), 133,641 options were exercised (June 30, 2015 – 894,956) and 69,485 options were forfeited (June 30, 2015 – 52,502).

The following summarizes options granted, exercised and forfeited during the period:

	Number of options	Weighted average exercise price $
Outstanding at December 31, 2015	**5,752,419**	**4.68**
Granted	2,500	6.62
Exercised	(133,641)	2.34
Forfeited	(69,485)	5.31
Outstanding at June 30, 2016	**5,551,793**	**4.73**
Exercisable at June 30, 2016	**1,846,950**	**3.12**

Range of exercise prices outstanding at June 30, 2016:

	Options outstanding			Options exercisable		
Range of exercise prices	Number outstanding	Weighted average remaining contractual years	Weighted average exercise price $	Number exercisable	Weighted average remaining contractual years	Weighted average exercise price $
$1.50 - $3.49	509,400	1.3	1.83	469,934	1.2	1.74
$3.50 - $5.49	2,170,393	3.0	3.59	1,377,016	3.0	3.59
$5.50 - $7.01	2,872,000	4.1	6.10	-	-	-
Total	**5,551,793**			**1,846,950**		

7. BASIC AND DILUTED (LOSS) INCOME PER SHARE

The calculation of basic and diluted (loss) income per share for the three and six months ended June 30, 2016 was based on the net loss of $1.5 million and $1.1 million, respectively (June 30, 2015 – net loss of $1.4 million and net income of $3.3 million, respectively), and a weighted average number of common shares outstanding of 84.6 million (June 30, 2015 – 79.7 million and 78.3 million, respectively).

	For the three months ended June 30,		For the six months ended June 30,	
	2016	2015	2016	2015
Weighted average shares outstanding	84,597,751	79,725,135	84,564,661	78,268,013
Stock options	-	-	-	1,897,575
Convertible warrants	-	-	-	235,577
Diluted shares outstanding	84,597,751	79,725,135	84,564,661	80,401,165

As the Company was in a loss position for the three and six months ended June 30, 2016 and the three months ended June 30, 2015, all convertible securities were excluded from the diluted weighted average number of common shares calculation as their effect would have been anti-dilutive. For the six months ended June 30, 2015, all convertible securities were included in the diluted weighted average number of common shares calculation as none were anti-dilutive.

8. SEGMENT REPORTING

The Company operates in two principal geographic locations, Canada and the United States ("US"), and has one operating segment. Currently, all revenue from international projects are included in the US revenue amount as these projects are sold by US-based DPs. The Company's revenue from operations from external customers, based on location of operations, and information about its non-current assets, are detailed below.

Revenue from external customers

	For the three months ended June 30,		For the six months ended June 30,	
	2016	2015	2016	2015
		($ thousands)		
Canada	4,984	7,730	13,056	17,456
US	56,268	45,136	104,119	92,111
	61,252	52,866	117,175	109,567

Selected Condensed Consolidated Statement of Financial Position Information – Non-current assets

As at	June 30, 2016	December 31, 2015
	($ thousands)	
Canada	51,813	44,290
US	20,633	22,026
	72,446	66,316

The amounts above exclude note receivable and deferred tax assets.

9. TRANSACTIONS AND BALANCES WITH RELATED PARTIES

Note receivable is due from an individual who is a shareholder and an officer and director of the Company, bears interest at 5% with monthly payments of $3,750 including interest, and is secured by 250,000 common shares of the Company. At June 30, 2016, the balance outstanding was $431,109 (December 31, 2015 - $442,662).

One of the Company's DPs is owned by a director of the Company. The Company reported the following activities with this DP during the respective periods:

	For the three months ended June 30,		For the six months ended June 30,	
	2016	2015	2016	2015
		($ thousands)		
Revenue earned	3,063	1,119	5,129	2,833
Rebates paid	7	16	26	60
As at			**June 30, 2016**	**December 31, 2015**
Outstanding accounts receivable			804	370
Outstanding deposits received			190	237

All transactions with related parties have occurred in the normal course of operations at arm's length, except for the note receivable, and are measured at the exchange amounts, which are the amounts of consideration established and agreed to by the related parties.

10. CAPITAL MANAGEMENT

As at June 30, 2016, the Company has $170.5 million (December 31, 2015 - $170.8 million) of total capital resources, comprised of Shareholders' Equity. The Company also has total debt of $11.8 million (December 31, 2015 - $9.2 million).

The Company aims to manage its capital resources to ensure financial strength and to maximize its financial flexibility by maintaining strong liquidity and by utilizing alternative sources of capital including equity, debt and bank loans or lines of credit to fund continued growth.

In March 2016, the Company signed a fourth amendment to the amended and restated loan agreement with its lender, which included a reduction of interest rates on outstanding advances from prime plus 0.5% to prime minus 0.25% and a new capital financing facility of US$10.0 million. Debt covenants were adjusted to increase the minimum tangible net worth from $60.0 million to $135.0 million and to add a maximum capital expenditure limit of $40.0 million for 2016. As at June 30, 2016 and December 31, 2015, the Company's tangible net worth was $157.9 million and $156.6 million, respectively. As at June 30, 2016 and December 31, 2015, the Company was in compliance with all of its lender's covenants.

11. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

The Company's activities expose it to a variety of financial risks: credit risk, liquidity risk, market risk, interest rate risk, foreign exchange risk and commodity price risk. The Company's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Company's financial performance. The Company considers credit risk to be one of its main financial risks.

Credit risk

The Company's principal financial assets are cash and cash equivalents, trade and other receivables, and note receivable.

The Company's credit risk is primarily concentrated in its trade receivables. The amounts disclosed in the condensed consolidated statement of financial position are net of allowances for doubtful accounts, estimated by the management of the Company based on previous experience with customers and their assessment of the current economic environment and specific customer circumstances. In order to reduce its risk, management maintains credit policies that include regular review of credit limits of individual customers and the use of accounts receivable insurance (see below) for a significant portion of trade receivables. Aging of trade receivables is systematically monitored by management. Trade balances are spread amongst a broad customer base which is geographically dispersed. The Company does not have significant exposure to any individual customer. A number of factors are considered in determining the likelihood of impairment. The Company had minimal bad debt expense for the three and six months ended June 30, 2016 and 2015.

The Company also has a contract with Export Development Canada ("EDC"), Canada's export credit agency, whereby some of its trade receivables are insured. EDC determines the coverage amount, if any, on a customer-by-customer basis. Based on the Company's trade receivables balance as at June 30, 2016, 67.3% (December 31, 2015 - 64.1 %) of that balance is covered by EDC. Substantially all of the remaining balance is less than 90 days old and is owed by a small number of DIRTT's strong-performing DPs, on which the Company has a high level of confidence of collectability, and government sales that are not covered by EDC. The Company considers trade receivables greater than 90 days as past due and as at June 30, 2016, the amount outstanding was $1.1 million, net of allowance for doubtful accounts of $0.7 million (December 31, 2015 - $1.6 million, $0.7 million). The Company only provides for balances it considers to be at risk of collection. As a result, the Company believes that its exposure to credit risk is limited.

The credit risk on cash and cash equivalents is limited because the counterparties are chartered banks with high credit ratings assigned by national credit-rating agencies.

11. FINANCIAL INSTRUMENTS AND RISK MANAGEMENT (CONTINUED)

Fair value of financial instruments

The fair values of the Company's financial instruments were determined as follows:

a) The carrying amounts of cash and cash equivalents; trade and other receivables; trade accounts payable and other liabilities; and customer deposits approximate fair value due to their short-term nature;
b) The carrying amount of note receivable approximates fair value as it bears interest at a market rate, and have reasonable repayment terms;
c) Included in other assets in 2015 was an insignificant convertible note receivable amount that did not have a quoted market price. The carrying amount of this convertible note receivable was carried at fair value using the Black-Scholes method and the value of the underlying entity by employing the best information available at each measurement date. The convertible note receivable was repaid in full in May 2016; and
d) The Company's current and long-term debts are carried at amortized cost. The fair values of these instruments are estimates made at a specific point in time, based on relevant market information. These estimates are based on quoted market prices for the same or similar issues or on the current rates offered to the Company for similar financial instruments subject to similar risks and maturities. The carrying amounts of these instruments approximates fair value due to their respective floating interest rates.

12. COMMITMENTS

As at June 30, 2016, the Company has unpaid capital expenditure commitments of approximately $2.3 million for manufacturing equipment to be delivered by early 2017.