



QUALITY THROUGH
INTEGRITY AND TECHNOLOGY



QUARTERLY REPORT

For the thirteen weeks
ended August 26, 2016

ENVIRONMENTAL TECTONICS CORPORATION

Quarterly Report
For the thirteen weeks ended August 26, 2016

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(Address of Issuer's Principal Executive Office)

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Item numbers above refer to the OTC Pink Basic Disclosure Guidelines created by the OTC Markets Group. The OTC Pink Basic Disclosure Guidelines are available on the Internet at <http://www.otcmarkets.com/marketplaces/otc-pink>.

When used in this Quarterly Report, except where the context otherwise requires, the terms "we", "us", "our", "ETC", and the "Company" refer to Environmental Tectonics Corporation and its subsidiaries.

Item 3. Security Information

Trading symbol: ETCC
CUSIP: 294092

Title of class of securities outstanding:	Common Stock	Preferred Stock, Series E
Par value:	\$0.05	\$0.05
Total shares authorized:	50,000,000 as of August 26, 2016	25,000 as of August 26, 2016
Total shares outstanding:	9,185,161 as of August 26, 2016	12,127 as of August 26, 2016

Transfer Agent:

American Stock Transfer & Trust Company, LLC
6201 15th Avenue
Brooklyn, NY 11219
Toll Free: (800) 937-5449
Telephone: (718) 921-8124
Website: www.amstock.com

List any restrictions on the transfer of security: N/A

Describe any trading suspension: N/A

List any stock split, stock dividend, recapitalization, merger, acquisition, spin-off, or reorganization either currently anticipated or that occurred within the past twelve months:

We have never paid any cash dividends on our Common Stock and do not anticipate that any cash dividends will be declared or paid on our Common Stock in the foreseeable future.

Dividends on the Company's Preferred Stock, as declared, are accrued according to the terms of the Preferred Stock and when paid, are paid in cash. The Preferred Stock is currently entitled to receive cumulative dividends at the rate of four percent (4%) per year in preference to the holders of the Company's Common Stock with respect to dividends. Series E Preferred Stock dividends accrued as of August 26, 2016, which totaled \$1,702 thousand, remained unpaid as of October 10, 2016, the date of issuance of the accompanying interim consolidated financial statements, per the restrictions stipulated in the October 11, 2013 amendment to the September 28, 2012 Loan Agreement with PNC Bank, National Association ("PNC Bank").

Item 4. Issuance History

- A. The nature of each offering of Common Stock in the last two fiscal years: N/A
- B. Any jurisdictions where the offering was registered or qualified: N/A
- C. The number of shares sold: N/A
- D. The price at which the shares were offered, and the amount actually paid to the issuer: N/A
- E. The trading status of the shares: N/A
- F. Whether the certificates or other documents that evidence the shares contain a legend (1) stating that the shares have not been registered under the Securities Act and (2) setting forth or referring to the restrictions on transferability and sale of the shares under the Securities Act: N/A

Item 5. Financial Statements

Environmental Tectonics Corporation
Consolidated Statements of Operations and Comprehensive Loss
(unaudited)

<i>(in thousands, except per share information)</i>	Thirteen weeks ended		Twenty-six weeks ended	
	August 26, 2016	August 28, 2015	August 26, 2016	August 28, 2015
Net sales	\$ 7,459	\$ 9,966	\$ 18,182	\$ 19,505
Cost of goods sold	5,105	7,423	12,888	13,912
Gross profit	2,354	2,543	5,294	5,593
Operating expenses	2,814	2,898	5,749	6,096
Operating loss	(460)	(355)	(455)	(503)
Other expenses:				
Interest expense, net	193	237	431	457
Other expense, net	131	253	353	284
Other expenses total	324	490	784	741
Loss before income taxes	(784)	(845)	(1,239)	(1,244)
Income tax provision (benefit)	26	(338)	50	(498)
Net loss	(810)	(507)	(1,289)	(746)
(Income) loss attributable to non-controlling interest	(1)	1	-	-
Net loss attributable to Environmental Tectonics Corporation	(811)	(506)	(1,289)	(746)
Foreign currency translation adjustment and unrealized loss on cash flow hedge	228	101	176	69
Comprehensive loss	\$ (583)	\$ (405)	\$ (1,113)	\$ (677)
Preferred Stock dividends	(121)	(121)	(242)	(242)
Loss attributable to common and participating shareholders	\$ (932)	\$ (627)	\$ (1,531)	\$ (988)
Per share information:				
Basic earnings (loss) per common and participating share:				
Distributed earnings per share:				
Common	\$ -	\$ -	\$ -	\$ -
Preferred	\$ 0.02	\$ 0.02	\$ 0.04	\$ 0.04
Undistributed loss per share:				
Common	\$ (0.06)	\$ (0.04)	\$ (0.10)	\$ (0.06)
Preferred	\$ (0.06)	\$ (0.04)	\$ (0.10)	\$ (0.06)
Diluted loss per share	\$ (0.06)	\$ (0.04)	\$ (0.10)	\$ (0.06)
Basic weighted average common and participating shares:				
Common weighted average number of shares	9,185	9,185	9,185	9,185
Participating preferred shares	6,063	6,063	6,063	6,063
Total basic weighted average common and participating shares	15,248	15,248	15,248	15,248
Diluted weighted average shares:				
Basic weighted average common and participating shares	15,248	15,248	15,248	15,248
Dilutive effect of stock warrants and options	3	43	3	50
Total diluted weighted average shares	15,251	15,291	15,251	15,298

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

Environmental Tectonics Corporation Consolidated Balance Sheets

<i>(in thousands, except share information)</i>	August 26, 2016	February 26, 2016
	(unaudited)	
ASSETS		
Current assets:		
Cash and cash equivalents	\$ 976	\$ 976
Restricted cash	5,959	6,162
Accounts receivable, net	3,078	4,222
Costs and estimated earnings in excess of billings on uncompleted long-term contracts	14,450	14,973
Inventories, net	2,465	2,600
Prepaid expenses and other current assets	1,697	1,441
Total current assets	28,625	30,374
Property, plant, and equipment, at cost, net	13,450	13,726
Capitalized software development costs, net	172	172
Other assets	10	20
Total assets	\$ 42,257	\$ 44,292
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Current portion of long-term debt obligations	\$ 19,084	\$ 13,870
Accounts payable, trade	2,371	3,224
Billings in excess of costs and estimated earnings on uncompleted long-term contracts	6,914	6,148
Customer deposits	1,121	1,061
Accrued taxes	145	410
Accrued interest and dividends	1,758	1,533
Other accrued liabilities, current	2,148	2,424
Total current liabilities	33,541	28,670
Long-term debt obligations, less current portion:		
Term Loan	-	5,569
Total long-term debt obligations, less current portion	-	5,569
Deferred tax liabilities, non-current, net	203	200
Other accrued liabilities, non-current	697	742
Total liabilities	34,441	35,181
Commitments and contingencies (Note 5)		
Shareholders' equity:		
Cumulative convertible participating Preferred Stock, Series E, \$0.05 par value, 25,000 shares authorized; 12,127 shares outstanding as of August 26, 2016 and February 26, 2016	12,127	12,127
Common Stock, \$0.05 par value, 50,000,000 shares authorized; 9,185,161 shares issued and outstanding as of August 26, 2016 and February 26, 2016	459	459
Additional paid-in capital	8,987	9,169
Accumulated deficit	(13,430)	(12,141)
Accumulated other comprehensive loss	(395)	(571)
Total shareholders' equity before non-controlling interest	7,748	9,043
Non-controlling interest	68	68
Total shareholders' equity	7,816	9,111
Total liabilities and shareholders' equity	\$ 42,257	\$ 44,292

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

Environmental Tectonics Corporation
Consolidated Statements of Cash Flows
(unaudited)

<i>(in thousands)</i>	Twenty-six weeks ended	
	August 26, 2016	August 28, 2015
Cash flows from operating activities:		
Net loss	\$ (1,289)	\$ (746)
Adjustments to reconcile net income to net cash provided by operating activities:		
Depreciation and amortization	682	805
Deferred income taxes	3	(483)
Decrease in allowance for doubtful accounts and inventory obsolescence	(7)	(8)
Accretion of loan origination deferred charge and deferred financing costs	17	25
Stock compensation expense	60	85
Changes in operating assets and liabilities:		
Accounts receivable	1,149	777
Costs and estimated earnings in excess of billings on uncompleted long-term contracts	523	1,517
Inventories	137	(299)
Prepaid expenses and other assets	(250)	(286)
Accounts payable, trade	(853)	1,967
Billings in excess of costs and estimated earnings on uncompleted long-term contracts	766	2,128
Customer deposits	60	1,129
Accrued taxes	(265)	(130)
Accrued interest and dividends	(17)	(27)
Other accrued liabilities	(321)	(607)
Net cash provided by operating activities	395	5,847
Cash flows from investing activities:		
Acquisition of property, plant, and equipment	(355)	(670)
Capitalized software development costs	(51)	(69)
Net cash used in investing activities	(406)	(739)
Cash flows from financing activities:		
Decrease (increase) in restricted cash	203	(3,700)
Borrowings (repayments) under lines of credit	7,464	(1,454)
Payments on the Term Loan	(7,819)	-
Payments of deferred financing costs	(13)	(14)
Net cash used in financing activities	(165)	(5,168)
Effect of exchange rate changes on cash	176	70
Net increase in cash and cash equivalents	-	10
Cash and cash equivalents at beginning of period	976	611
Cash and cash equivalents at end of period	\$ 976	\$ 621
Supplemental schedule of cash flow information:		
Interest paid	\$ 436	\$ 443
Income taxes paid	\$ 55	\$ -
Supplemental information on non-cash operating and investing activities:		
Preferred Stock dividends accrued during each respective fiscal period	\$ 242	\$ 242
Unrealized loss on cash flow hedge	\$ -	\$ (1)

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

Environmental Tectonics Corporation

Notes to the Consolidated Financial Statements

(unaudited)

(Dollars in thousands, except per share information)

Item 6. Description of Business Operations

ETC was incorporated in 1969 in Pennsylvania. For over four decades, we have provided our customers with products, services, and support. Innovation, continuous technological improvement and enhancement, and product quality are core values that are critical to our success. We are a significant supplier and innovator in the following areas: (i) software driven products and services used to create and monitor the physiological effects of flight, including high performance jet tactical flight simulation, upset recovery and spatial disorientation, and both suborbital and orbital commercial human spaceflight, collectively, Aircrew Training Systems (“ATS”); (ii) altitude (hypobaric) chambers; (iii) hyperbaric chambers for multiple persons (multiplace chambers); (iv) Advanced Disaster Management Simulators (“ADMS”); (v) steam and gas (ethylene oxide) sterilizers; (vi) environmental testing and simulation devices; and (vii) hyperbaric (100% oxygen) chambers for one person (monoplace chambers). We operate in two primary business segments, Aerospace Solutions (“Aerospace”) and Commercial/Industrial Systems (“CIS”).

Aerospace encompasses the design, manufacture, and sale of: (i) ATS products; (ii) altitude (hypobaric) chambers; (iii) hyperbaric chambers for multiple persons (multiplace chambers); and (iv) ADMS, as well as integrated logistics support (“ILS”) for customers who purchase these products or similar products manufactured by other parties. These products and services provide customers with an offering of comprehensive solutions for improved readiness and reduced operational costs. Sales of our Aerospace products are made principally to United States and foreign government agencies and to civil aviation organizations. We offer integrated ATS products to commercial, governmental, and military defense agencies, and training devices, including altitude (hypobaric) and multiplace chambers (“Chambers”), to governmental and military defense agencies and civil aviation organizations both in the U.S. and internationally. We sell our ADMS line of products to federal, state, and local governments, fire and emergency training schools, universities, and airports. We also provide integrated logistics support for customers who purchase these products or similar products manufactured by other parties.

CIS encompasses the design, manufacture, and sale of: (i) steam and gas (ethylene oxide) sterilizers; (ii) environmental testing and simulation devices; and (iii) hyperbaric (100% oxygen) chambers for one person (monoplace chambers), as well as parts and service support for customers who purchase these products or similar products manufactured by other parties. Sales of our CIS products are made principally to the healthcare, pharmaceutical, and automotive industries. We sell our sterilizers to pharmaceutical and medical device manufacturers. We sell our environmental testing and simulation devices primarily to commercial automobile and heating, ventilation, and air conditioning (“HVAC”) manufacturers. We sell our hyperbaric products (primarily “monoplace” chambers) to hospitals and wound care clinics. We also provide upgrade, maintenance, and repair services for our products and similar products manufactured by other parties.

The Company’s fiscal year is the fifty-two week or fifty-three week annual accounting period ending the last Friday in February. References to the 2017 second quarter are references to the thirteen week period ended August 26, 2016. References to the 2016 second quarter are references to the thirteen week period ended August 28, 2015. References to the 2017 first half are references to the twenty-six week period ended August 26, 2016. References to the 2016 first half are references to the twenty-six week period ended August 28, 2015. References to fiscal 2017 are references to the fifty-two week period ending February 24, 2017. References to fiscal 2016 are references to the fifty-two week period ended February 26, 2016. Certain amounts from prior consolidated financial statements have been reclassified to conform to the presentation in fiscal 2017.

Note 1. Summary of Significant Accounting Policies

Basis of Presentation

The accompanying interim consolidated financial statements include the accounts of ETC, our 95%-owned subsidiary in Warsaw, Poland, ETC-PZL Aerospace Industries Sp. z o.o. (“ETC-PZL”), and our 99%-owned subsidiary, Environmental Tectonics Corporation (Europe) Limited (“ETC-Europe”). The Company’s corporate headquarters and main production plant (“ETC-SH”) are located in Southampton, Pennsylvania, USA. ETC-PZL manufactures certain simulators and provides software to support products manufactured domestically within our Aerospace segment. ETC-Europe, which we are winding down, functioned as a sales office in the United Kingdom. All significant intercompany accounts and transactions have been eliminated in consolidation.

The accompanying interim consolidated financial statements have been prepared by ETC, without audit, in conformity with accounting principles generally accepted in the United States of America, consistently applied, and reflect all adjustments which, in the opinion of management, are necessary for a fair presentation of the results for the interim periods presented. All such adjustments are of a normal recurring nature.

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements, continued

(Dollars in thousands, except per share information)

In accordance with industry practices, costs and estimated earnings in excess of billings on uncompleted long-term contracts are classified as current even though a portion of these amounts may not be realized within one year.

Certain information in footnote disclosures normally included in financial statements prepared in conformity with accounting principles generally accepted in the United States of America has been condensed or omitted and the financial results for the periods presented may not be indicative of the full year's results; however, the Company believes that the disclosures are adequate to make the information presented not misleading. These interim consolidated financial statements should be read in conjunction with the audited financial statements and the notes thereto included in the Company's Annual Report to Shareholders for fiscal 2016.

Significant Accounting Policies

There have been no material changes in the Company's significant accounting policies during fiscal 2017 as compared to what was previously disclosed in the Company's Annual Report to Shareholders for fiscal 2016.

Note 2. Earnings per Share

The Company utilizes the two-class method for computing and presenting earnings per share. The Company currently has one class of Common Stock (the "Common Stock") and one class of cumulative convertible participating Preferred Stock currently outstanding, Series E (the "Preferred Stock"). Under its terms, the Preferred Stock is entitled to participate in any cash dividends on a one-for-one basis for the equivalent converted common shares if the Preferred Stock were to be converted by the holder by the dividend record date; therefore, the Preferred Stock is considered a participating security requiring the two-class method for the computation and presentation of net income per share – basic.

The two-class computation method for each period segregates basic earnings per common and participating share into two categories: distributed earnings per share (i.e., the Preferred Stock stated dividend) and undistributed earnings per share, which allocates earnings after subtracting the Preferred Stock dividend to the total of weighted average common shares outstanding plus equivalent converted common shares related to the Preferred Stock. Basic earnings per common and participating share excludes the effect of Common Stock equivalents, and is computed using the two-class computation method.

Diluted earnings per share reflects the potential dilution that could result if securities or other contracts to issue Common Stock were exercised or converted into Common Stock. Diluted earnings per share continues to be computed using the if-converted method. Diluted earnings per share assumes the exercise of stock options and warrants using the treasury stock method. If the effect of the conversion of any financial instruments would be anti-dilutive, it is excluded from the diluted earnings per share calculation.

As of both August 26, 2016 and August 28, 2015, there was \$12,127 of cumulative convertible participating Series E Preferred Stock convertible at an exercise price of \$2.00 per share, equating to 6,063,321 shares of Common Stock, issued in July 2009.

On February 28, 2009, in connection with the issuance of a \$2,000 promissory note, the Company issued 200,000 warrants to purchase 143,885 shares of the Company's Common Stock at \$1.39 per share. As of February 28, 2016, these warrants have expired. Additionally, on July 2, 2009, in consideration of an increase of the guarantee on the 2007 PNC Credit Facility, the Company issued 500,000 warrants to purchase 450,450 shares of the Company's Common Stock at \$1.11 per share. As of July 2, 2016, these warrants have expired.

As of August 26, 2016 and August 28, 2015, there were outstanding options to purchase the Company's Common Stock totaling 585,427 and 642,813 shares at an average price of \$1.24 and \$1.25 per share, respectively. Due to the conversion price of the Common Stock options, 575,427 and 642,813 shares were excluded from the calculation of diluted earnings per share as of August 26, 2016 and August 28, 2015, respectively, because the effect of their conversion would be antidilutive; further, all 143,885 shares of the Company's Common Stock pertaining to the 200,000 warrants issued on February 20, 2009 were excluded from the calculation of diluted earnings per share as of August 28, 2015 because the effect of their conversion would also be antidilutive. Due to the expiration of all warrants during the 2017 first half, all shares pertaining to warrants were excluded from the calculation of diluted earnings per share as of August 26, 2016.

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements, continued

(Dollars in thousands, except per share information)

Note 3. Long-Term Obligations

On June 10, 2016, the Company received a waiver as of the fiscal quarter ended February 26, 2016 for failing to exceed the permitted minimum Consolidated Tangible Net Worth. The waiver also provides that ETC must maintain at all times a minimum Consolidated Tangible Net Worth of \$7,500; further, commencing with the fiscal quarter ending May 26, 2017, ETC must maintain as of the end of each fiscal quarter a Fixed Charge Coverage Ratio of at least 1.00 to 1. This ratio will increase to 1.10 to 1 on August 25, 2017, and will remain at that level at all times thereafter. The waiver extended the maturity date of the existing PNC Line of Credit to August 10, 2016, during which time the Company entered into an amendment to the September 28, 2012 Loan Agreement with PNC Bank that provided for, among other things, the following:

- (i) The PNC Line of Credit and the Term Loan were consolidated into a \$21,000 Revolving Line of Credit (the “Revolving Line of Credit”). Amounts borrowed under the Revolving Line of Credit may be borrowed, repaid, and re-borrowed from time to time until December 31, 2017.
- (ii) The existing Committed Line of Credit is capped at \$8,600, an amount equivalent to the total outstanding standby letters of credit under which the Committed Line of Credit covered as of May 27, 2016.
- (iii) A new \$1,000 FX Equivalent Line of Credit (the “FX Equivalent Line of Credit”) for potential future foreign exchange obligations.
- (iv) The Revolving Line of Credit, the Committed Line of Credit, and the FX Equivalent Line of Credit (collectively, the “2016 PNC Credit Facilities”) have a maturity date of December 31, 2017.
- (v) The interest rate on the 2016 PNC Credit Facilities will be based on the PNC Daily LIBOR Rate (0.531% as of October 1, 2016, the date of our most current Revolving Line of Credit statement) plus a margin of 3.00%.
- (vi) The 2016 PNC Credit Facilities are collateralized by a combination of the Company’s pledged restricted cash (\$5,959 as of August 26, 2016), substantially all of the Company’s additional assets, and the pledged cash collateral of H.F. Lenfest (“Mr. Lenfest”), a major shareholder and member of the Company’s Board of Directors (the “Board of Directors”).

Summary of Long-Term Debt Obligations

Long-term debt obligations consist of the following:

	August 26, 2016	February 26, 2016
	(unaudited)	
Credit facility payable to bank	\$ 19,084	\$ 11,620
Term Loan	-	7,819
Borrowed under the ETC-PZL Line of Credit	-	-
Total long-term debt obligations	19,084	19,439
Less: current portion of long-term debt obligations	(19,084)	(13,870)
Total long-term debt obligations, less current portion	\$ -	\$ 5,569

Note 4. Income Taxes

Deferred income taxes reflect the net tax effects of temporary differences between the carrying amounts of assets and liabilities for financial and tax reporting purposes as well as the valuation of net operating loss carryforwards. Valuation allowances are reviewed each fiscal period to determine whether there is sufficient positive or negative evidence to support a change in judgment about the potential realization of the related deferred tax asset. Deferred tax liabilities and assets are offset and presented as a single non-current liability.

Generally, accounting standards require companies to provide for income taxes each quarter based on their estimate of the effective tax rate for the full year. The authoritative guidance for accounting for income taxes allows use of the discrete method when, in certain situations, the actual interim period effective tax rate may be used if it provides a better estimate of income tax expense.

Environmental Tectonics Corporation
Notes to the Consolidated Financial Statements, continued

(Dollars in thousands, except per share information)

An income tax provision of \$26, primarily related to an increase in unrecognized tax benefits, was recorded in the 2017 second quarter compared to an income tax benefit of \$338 recorded in the 2016 second quarter. Effective tax rates were -3.3% and 40.0% for the 2017 second quarter and the 2016 second quarter, respectively. An income tax provision of \$50, primarily related to an increase in unrecognized tax benefits, was recorded in the 2017 first half compared to an income tax benefit of \$498 recorded in the 2016 first half. Effective tax rates were -4.0% and 40.0% for the 2017 first half and the 2016 first half, respectively. Our effective tax rates for the 2017 second quarter and the 2017 first half were negative and significantly lower compared to the tax rates for the 2016 second quarter and the 2016 first half due primarily to the continued need for a full valuation allowance for such deferred tax assets relating to our federal net operating loss carryforwards that we do not expect to realize. As of August 26, 2016, the Company had approximately \$21,048 of federal net loss carryforwards available to offset future income tax liabilities, which begin to expire in 2025. The unrecognized tax benefits, which are recorded on the Company's balance sheet within other accrued liabilities, are primarily associated with U.S. federal tax issues such as the amount of research and development tax credits claimed and taxation of foreign earnings. Also included in these amounts are accruals for domestic state tax issues such as the allocation of income among various state tax jurisdictions.

Note 5. Commitments and Contingencies

Legal Proceedings

Orbit Movers & Erectors, Inc.

Orbit Movers & Erectors, Inc. ("Orbit") filed suit in the Court of Common Pleas in Montgomery County, Ohio, seeking damages for alleged additional costs that Orbit claims to have incurred under a contract (the "Orbit Contract") pursuant to which Orbit was to fabricate and install certain piping systems for an ETC Aerospace product (the "Orbit Litigation"). The amount of the alleged additional costs claimed by Orbit is approximately \$500. The litigation was removed to federal district court in Ohio, after which the Company filed its answer and counterclaim for breach of contract. Following a pre-trial conference, the Court scheduled a jury trial in 2017. Earlier this year, the Company filed a Motion for Leave to Amend Answer With Affirmative Defenses and Amended Counterclaims ("Amended Answer"), which was granted. The Amended Answer was subsequently filed and Orbit has replied to ETC's Amended Answer. On July 26, 2016, the Company settled the Orbit Litigation in its entirety. The final terms of the settlement, as approved by the Court, will not have a material adverse effect on the Company's financial position or results of operations.

Other Matters

Certain claims, suits, and complaints arising in the ordinary course of business have been filed or are pending against us. We believe, after consultation with legal counsel handling these specific matters, all such matters are reserved for or adequately covered by insurance or, if not so covered, are without merit or are of such kind, or involve such amounts, as would not be expected to have a significant effect on our financial position or results of operations if determined adversely against us.

Note 6. Subsequent Events

The Company has evaluated subsequent events through October 10, 2016, the date of issuance of the accompanying interim consolidated financial statements, and determined that there were no material subsequent events requiring adjustment to, or disclosure in, the accompanying interim consolidated financial statements for the thirteen weeks ended August 26, 2016.

Management's Discussion and Analysis

Forward-looking Statements

Discussions of some of the matters contained in this Quarterly Report include forward-looking statements that may involve risks and uncertainties. Some of these discussions are contained under the caption "Management's Discussion and Analysis". We have based these forward-looking statements on our current expectations and projections about future events or future financial performance, which include implementing our business strategy, developing and introducing new technologies, obtaining, maintaining and expanding market acceptance of the technologies we offer, and competition in our markets. These forward-looking statements are subject to known and unknown risks, uncertainties and assumptions about ETC and its subsidiaries that may cause actual results, levels of activity, performance, or achievements to be materially different from any future results, levels of activity, performance, or achievements expressed or implied by these forward-looking statements.

These forward-looking statements include statements with respect to the Company's vision, mission, strategies, goals, beliefs, plans, objectives, expectations, anticipations, estimates, intentions, financial condition, results of operations, future performance, and business of the Company, including, but not limited to, (i) projections of revenues, costs of materials, income or loss, earnings or loss per share, capital expenditures, growth prospects, dividends, capital structure, other financial items, and the effects of foreign currency fluctuations, (ii) statements of our plans and objectives of the Company or its management or the Board of Directors, including the introduction of new products, or estimates or predictions of actions of customers, suppliers, competitors, or regulatory authorities, (iii) statements of future economic performance, (iv) statements of assumptions and other statements about the Company or its business, (v) statements made about the possible outcomes of litigation involving the Company, (vi) statements regarding the Company's ability to obtain financing to support its operations and other expenses, and (vii) statements preceded by, followed by, or, that include, words such as "may", "will", "should", "expect", "plan", "anticipate", "believe", "estimate", "future", "predict", "potential", "intend", or "continue", and similar expressions. These forward-looking statements involve risks and uncertainties that are subject to change based on various important factors. Some of these risks and uncertainties, in whole or in part, are beyond the Company's control.

Results of Operations

Thirteen weeks ended August 26, 2016 compared to thirteen weeks ended August 28, 2015

Due to the nature of our business, we have historically experienced significant variability in our quarterly revenues, earnings, and other operating results, and our performance may fluctuate significantly in the future.

Summary Table of Results

(unaudited)

<i>(in thousands, except per share information)</i>	Thirteen weeks ended		Variance (\$)	Variance (%)
	August 26, 2016	August 28, 2015		
Net sales	\$ 7,459	\$ 9,966	\$ (2,507)	(25.2)
Cost of goods sold	5,105	7,423	(2,318)	(31.2)
Gross profit	2,354	2,543	(189)	(7.4)
<i>Gross profit margin %</i>	<i>31.6%</i>	<i>25.5%</i>	<i>6.1%</i>	<i>23.9%</i>
Operating expenses	2,814	2,898	(84)	(2.9)
Operating loss	(460)	(355)	(105)	29.6
<i>Operating margin %</i>	<i>(6.2%)</i>	<i>(3.6%)</i>	<i>(2.6%)</i>	<i>72.2%</i>
Interest expense, net	193	237	(44)	(18.6)
Other expense, net	131	253	(122)	(48.2)
Loss before income taxes	(784)	(845)	61	(7.2)
<i>Pre-tax margin %</i>	<i>(10.5%)</i>	<i>(8.5%)</i>	<i>(2.0%)</i>	<i>(23.5%)</i>
Income tax provision (benefit)	26	(338)	364	(107.7)
(Income) loss attributable to non-controlling interest	(1)	1	(2)	200.0
Net loss attributable to ETC	\$ (811)	\$ (506)	\$ (305)	60.3

Per share information:

Basic earnings (loss) per common and participating share:

Distributed earnings per share:

Common	\$ -	\$ -	\$ -	
Preferred	\$ 0.02	\$ 0.02	\$ -	0.0
Undistributed loss per share:				
Common	\$ (0.06)	\$ (0.04)	\$ (0.02)	50.0
Preferred	\$ (0.06)	\$ (0.04)	\$ (0.02)	50.0
Diluted loss per share	\$ (0.06)	\$ (0.04)	\$ (0.02)	50.0

Environmental Tectonics Corporation
Management's Discussion and Analysis, continued

Net Loss Attributable to ETC

Net loss attributable to ETC was \$0.8 million, or \$0.06 diluted loss per share, in the 2017 second quarter, compared to a net loss attributable to ETC of \$0.5 million during the 2016 second quarter, equating to \$0.04 diluted loss per share. The \$0.3 million variance is comprised of a \$0.1 million decrease in gross profit and a \$0.4 million variance between the income tax provision recorded in the 2017 second quarter and the income tax benefit recorded in the 2016 second quarter, offset in part, by a \$0.1 million decrease in operating expenses and a \$0.1 million decrease in other expense.

Net Sales

Net sales in the 2017 second quarter were \$7.5 million, a decrease of \$2.5 million, or 25.2%, compared to 2016 second quarter net sales of \$10.0 million. The decrease reflects a reduction in overall sales related to ATS products including Chambers and our ADMS line of products within the Aerospace segment, as well as decreased sales of Sterilization Systems to Domestic customers within the CIS segment, offset in part, by increased sales of Environmental Testing and Simulation Systems and monoplace chambers to Domestic customers within the CIS segment.

Gross Profit

Gross profit for the 2017 second quarter was \$2.4 million compared to \$2.5 million in the 2016 second quarter, a decrease of \$0.1 million, or 7.4%. Despite the \$2.5 million, or 25.2%, decrease in revenue compared to the 2016 second quarter, a similar gross profit was achieved in the 2017 second quarter primarily related to consideration (approximately \$0.6 million) realized from the termination of a software license. Gross profit margin as a percentage of net sales increase to 31.6% for the 2017 second quarter compared to 25.5% for the 2016 second quarter.

Operating Expenses

Operating expenses, including sales and marketing, general and administrative, and research and development, for the 2017 second quarter were \$2.8 million, a slight decrease of \$0.1 million, or 2.9%, compared to \$2.9 million for the 2016 second quarter. The decrease is due primarily to a reduction in commission expense related to the decrease in revenue and a reduction in research and development expenses, offset in part, by a \$0.2 million one-time non-cash expense associated with the winding down of ETC-Europe in an effort to continue to reduce non-revenue generating expenses.

Other Expense, Net

Other expense, net, for the 2017 second quarter was \$0.1 million compared to \$0.2 million in the fiscal 2016 second quarter, a decrease of \$0.1 million, or 48.2%, due to the combination of a decrease in realized foreign currency exchange net losses and a decrease in letter of credit fees coupled with the absence of a one-time increase in other expense related to ETC-PZL that occurred in the fiscal 2016 second quarter.

Environmental Tectonics Corporation
Management's Discussion and Analysis, continued

Twenty-six weeks ended August 26, 2016 compared to twenty-six weeks ended August 28, 2015

Due to the nature of our business, we have historically experienced significant variability in our quarterly revenues, earnings, and other operating results, and our performance may fluctuate significantly in the future.

Summary Table of Results

(unaudited)

<i>(in thousands, except per share information)</i>	Twenty-six weeks ended		Variance (\$)	Variance (%)
	August 26, 2016	August 28, 2015		
Net sales	\$ 18,182	\$ 19,505	\$ (1,323)	(6.8)
Cost of goods sold	12,888	13,912	(1,024)	(7.4)
Gross profit	5,294	5,593	(299)	(5.3)
<i>Gross profit margin %</i>	29.1%	28.7%	0.4%	1.4%
Operating expenses	5,749	6,096	(347)	(5.7)
Operating loss	(455)	(503)	48	(9.5)
<i>Operating margin %</i>	(2.5%)	(2.6%)	0.1%	3.8%
Interest expense, net	431	457	(26)	(5.7)
Other expense, net	353	284	69	24.3
Loss before income taxes	(1,239)	(1,244)	5	(0.4)
<i>Pre-tax margin %</i>	(6.8%)	(6.4%)	(0.4%)	(6.3%)
Income tax provision (benefit)	50	(498)	548	(110.0)
(Income) loss attributable to non-controlling interest	-	-	-	-
Net loss attributable to ETC	\$ (1,289)	\$ (746)	\$ (543)	72.8

Per share information:

Basic earnings (loss) per common and participating share:

Distributed earnings per share:

Common	\$ -	\$ -	\$ -	
Preferred	\$ 0.04	\$ 0.04	\$ -	0.0
Undistributed loss per share:				
Common	\$ (0.10)	\$ (0.06)	\$ (0.04)	66.7
Preferred	\$ (0.10)	\$ (0.06)	\$ (0.04)	66.7
Diluted loss per share	\$ (0.10)	\$ (0.06)	\$ (0.04)	66.7

Net Loss Attributable to ETC

Net loss attributable to ETC was \$1.3 million, or \$0.10 diluted loss per share, in the 2017 first half, compared to a net loss attributable to ETC of \$0.8 million during the 2016 first half, equating to \$0.06 diluted loss per share. The \$0.5 million variance is comprised of a \$0.3 million decrease in gross profit and a \$0.5 million variance between the income tax provision recorded in the 2017 first half and the income tax benefit recorded in the 2016 first half, offset in part, by a \$0.3 million decrease in operating expenses.

Net Sales

Net sales in the 2017 first half were \$18.2 million, a decrease of \$1.3 million, or 6.8%, compared to 2016 first half net sales of \$19.5 million. The decrease reflects a reduction in sales related to ATS products including Chambers to the U.S. Government and overall sales of our ADMS line of products within the Aerospace segment, as well as decreased sales of Sterilization Systems to Domestic customers within the CIS segment, offset in part, by increased sales related to ATS products including Chambers to International customers within the Aerospace segment and increased overall sales of monoplace chambers within the CIS segment. Given the current progress made on U.S. Government contracts in the Company's sales backlog, coupled with significant fiscal 2016 International bookings, the Company anticipates that the concentration of sales to the U.S. Government will decrease in fiscal 2017 as International sales increase.

Environmental Tectonics Corporation
Management's Discussion and Analysis, continued

Gross Profit

Gross profit for the 2017 first half was \$5.3 million compared to \$5.6 million in the 2016 first half, a decrease of \$0.3 million, or 5.3%. The decrease in gross profit was due primarily to the decrease in revenue as the gross profit margin as a percentage of net sales of 29.1% for the 2017 first half was comparable to the gross profit margin as a percentage of net sales of 28.7% for the 2016 first half.

Operating Expenses

Operating expenses, including sales and marketing, general and administrative, and research and development, for the 2017 first half were \$5.8 million, a decrease of \$0.4 million, or 5.7%, compared to \$6.1 million for the 2016 first half. The decrease is due primarily to a reduction in commission expense related to the decrease in revenue, the on-going effort to reduce non-revenue generating general and administrative expenses, and a reduction in research and development expenses.

Other Expense, Net

Other expense, net, for the 2017 first half was \$0.4 million compared to \$0.3 million in the fiscal 2016 first half, an increase of \$0.1 million, or 24.3%, due primarily to an increase in realized foreign currency exchange net losses.

Cash Flows from Operating, Investing, and Financing Activities

During the 2017 first half, as a result of a decrease in accounts receivable, a decrease in costs and estimated earnings in excess of billings on uncompleted long-term contracts, and an increase in billings in excess of costs and estimated earnings on uncompleted long-term contracts, offset in part, by a decrease in accounts payable, the Company generated \$0.4 million of cash from operating activities compared to the \$5.8 million of cash provided by operating activities during the 2016 first half. Under percentage-of-completion ("POC") revenue recognition, these accounts represent the timing differences of spending on production activities versus the billing and collecting of customer payments.

Cash used for investing activities primarily relates to funds used for capital expenditures of equipment and software development. The Company's investing activities used \$0.4 million in the 2017 first half compared to \$0.7 million in the 2016 first half.

The Company's financing activities used \$0.2 million of cash in the 2017 first half on payments on the Term Loan, offset in part, by borrowings under the Company's various lines of credit and a decrease in restricted cash. In the 2016 first half, the Company's financing activities used \$5.2 million of cash to increase restricted cash and on repayments under the Company's various lines of credit.

Item 7. Description of Facilities

We are an ISO 9001 certified manufacturer. We are also ISO 13485 certified for our medical devices. We operate in four major locations consisting of manufacturing facilities, product development, and administration. A summary of square footage and use is presented below:

Location	Approximate Square Footage	Function	Owned/ Leased	Segment
Southampton, Pennsylvania	83,800	Manufacturing (36,000 sq. ft), NASTAR Center (22,100 sq. ft.), and Corporate Headquarters (25,700 sq. ft.)	Owned	Aerospace CIS
Orlando, Florida	8,700	Product development and administration	Leased	Aerospace
Warsaw, Poland	28,000	Manufacturing, product development, and administration	Leased	Aerospace
Ankara, Turkey	5,700	Software development	Leased	Aerospace CIS
Total	126,200			

The Southampton owned property is encumbered by an Open-End Mortgage and Security Agreement with PNC Bank, which secures the 2016 PNC Credit Facilities. We consider our machinery and plant to be in satisfactory operating condition, and adequate given our expected operations. Significant increases in the level of operations beyond what we expect in the current fiscal year might require us to obtain additional facilities and equipment.

The NASTAR Center, which is included in the Company's Southampton, Pennsylvania owned property, includes the following aerospace training and research equipment:

- ATFS-400-25 PHOENIX High Performance Human Centrifuge;
- GYROLAB GL-2000 Advanced Spatial Disorientation Trainer;
- Altitude (Hypobaric) Chamber;
- Ejection Seat Simulator; and
- Night Vision Training System and Night Vision Goggle Training System.

Item 8. Officers, Directors, and Control Persons

	Name / Address **	Title	Ownership Percentage
Directors and Executive Officers:	George K. Anderson, M.D.	Chairman of the Board of Directors	*
	Michael D. Malone	Vice Chairman of the Board of Directors	*
	Linda J. Brent, Ed.D.	Director	*
	Roger Colley	Director	*
	Robert L. Laurent, Jr.	Chief Executive Officer, President, and Director	*
	H.F. Lenfest c/o The Lenfest Group Five Tower Bridge-Suite 460 300 Barr Harbor Drive West Conshohocken, PA 19428	Director	*** 56.0%
	Winston E. Scott	Director	*
	Mark Prudenti	Chief Financial Officer and Treasurer	*
	James D. Cashel	Vice President, General Counsel, Corporate Secretary, and Chief Compliance Officer	*
	Thomas G. Loughlin	Chief Operating Officer	*
Control Persons:	William F. Mitchell, Sr. 2355 Fairway Road Huntingdon Valley, PA 19006		14.5%
	T. Todd Martin, III 50 Midtown Park East Mobile, AL 36606		11.3%
	3K Limited Partnership		7.1%
	Estate of Pete L. Stephens		6.4%

* less than 1%

** address listed for all persons beneficially owning more than ten percent (10%)

*** the denominator for this ownership percentage calculation includes all participating preferred shares

Information is accurate as of October 10, 2016. None of the foregoing Directors and Executive Officers in the last five years has had a legal/disciplinary issue.

Item 9. Third Party Providers

Legal Counsel:

Stradley Ronon Stevens & Young, LLP
2005 Market Street
Philadelphia, PA 19103
(215) 564-8120

Independent Auditor:

RSM US LLP
751 Arbor Way
Blue Bell, PA 19422
(215) 641-8600

Item 10. Management's Certification

I, Mark Prudenti certify that:

- 1 I have reviewed this Quarterly Report of Environmental Tectonics Corporation;
- 2 Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and
- 3 Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations, and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.



Mark Prudenti
Chief Financial Officer
Date: October 10, 2016

I, Robert L. Laurent, Jr. certify that:

- 1 I have reviewed this Quarterly Report of Environmental Tectonics Corporation;
- 2 Based on my knowledge, this disclosure statement does not contain any untrue statement of a material fact or omit to state a material fact necessary to make the statements made, in light of the circumstances under which such statements were made, not misleading with respect to the period covered by this disclosure statement; and
- 3 Based on my knowledge, the financial statements, and other financial information included or incorporated by reference in this disclosure statement, fairly present in all material respects the financial condition, results of operations, and cash flows of the issuer as of, and for, the periods presented in this disclosure statement.



Robert L. Laurent, Jr.
Chief Executive Officer and President
Date: October 10, 2016

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