

Covalon Announces Second Quarter Results for Fiscal 2023

MISSISSAUGA, Ontario – May 25, 2023 – (BUSINESS WIRE) – Covalon Technologies Ltd. (the "Company" or "Covalon") (TSXV: COV; OTCQX: CVALF), an advanced medical technologies company, today announced its second quarter fiscal 2023 results.

Brian Pedlar, Covalon's President and CEO, said, "I am pleased to announce another strong financial quarter for Covalon. Revenue for the three months ended March 31, 2023 increased 120% to \$7.2 million versus prior year and we've also seen improvements to our gross margins during the quarter. We are in a much stronger position in our key markets compared to last year, and we are seeing the results of investments made in 2022 continue to positively impact us in 2023. With our strong product and technology portfolio, Covalon is focused on becoming the leading provider of compassionate care solutions that help patients heal faster and live better. We are on track with our growth plan, and we have made strong progress in the first half of 2023 towards reaching our goals.

"Our efforts to grow our customer base in the United States and strengthening our brand world-wide have led to significant growth in revenue over the first six months of this fiscal year. Revenue for the first six months was up 63% to \$13.4 million compared to 2022. We have, and continue to engage, with major hospitals in the United States that are evaluating our infection prevention products in their intensive care units. We have seen positive impacts in our product sales through our distributors in the United States, increased orders from our international channels, and stronger services revenue from our medical coating projects. We anticipate continued growth in revenue this year, compared to fiscal 2022.

"Gross margins were significantly improved in the first six months of 2023. As part of the Company's customer focus initiatives, we improved our supply chain operations and invested in upgrading both business systems and infrastructure. Additional ongoing investments to allow us to better serve customers and drive growth in key markets going forward include expanding Covalon's in-house manufacturing capabilities and medical coating services. The full positive impact on our margins from our supply chain improvement initiatives are expected to be further realized over time.

"We continue to align our operating costs to growth prospects, as we see the results of our improved sales and marketing initiatives and as we realize the benefits of our efforts to transform our supply chain. Operating costs from continuing operations for the quarter ended March 31, 2023 increased over the same period last year. In 2022, our team executed on deliberate and well-planned strategic decisions to re-position Covalon to be able to unlock value from our lifesaving, patented products and technology by investing in our people, our commercial capabilities, and our infrastructure. We are confident that the changes we have made to Covalon will allow us to consistently achieve our objectives.

"The momentum we have, and the certainty of purpose we have in our products and mission, will allow Covalon to succeed. This quarter demonstrates that we are moving in the right direction with respect to investments made last year in several key business areas, including sales and marketing, operations, and IT infrastructure. We are excited about our progress in transforming Covalon into a patient-driven medical device company, built on the relentless pursuit to help the most vulnerable patients have a better chance at healing," concluded Mr. Pedlar.

(2) See "Non-IFRS Measures" below, including for a reconciliation of the non-IFRS measures used in this release to the most comparable IFRS measures



Conference Call Scheduled

A conference call and webcast to discuss Covalon's Q2 fiscal 2023 financial results will be held Thursday, May 25th, 2023, at 9:00am EDT. To view, listen to, and participate in the live webcast, please follow the link below:

<https://events.q4inc.com/attendee/898628652>

To listen and participate via the conference call, please dial:

North American Toll-Free: 1-888-396-8049

Local (Toronto): 416-764-8646

Conference ID: 23773049

Participants will be able to ask questions of Company management during the Q&A portion of the conference call either by asking them on the call or by submitting them using the chat function on the webcast.

A recording of the call will be available on www.covalon.com under News & Events on the Investors tab.

Q2 Fiscal 2023 and Year-to-Date Financial Results

Total revenue for the three months ended March 31, 2023 increased 120% to \$7.2 million compared to \$3.3 million for the same period of the prior year. Total revenue for the six months ended March 31, 2023 increased 63% to \$13.4 million compared to \$8.2 million for the same period of the prior year.

Product revenue for the three-month period ended March 31, 2023 increased 105% to \$6.1 million compared to \$3.0 million for the same period of the prior year. Product revenue in US and international markets was up \$3.2 million due to stronger customer demand for the Company's collagen dressing and IV Clear product lines. Product revenue for the six months ended March 31, 2023 increased 52% to \$11.4 million compared to \$7.5 million for the same period of the prior year. Product revenue in US and international markets was up \$3.1 million due to stronger customer demand for the Company's collagen dressing and IV Clear product lines.

Development and consulting services revenue for the three-month period ended March 31, 2023 increased by 375% to \$1.1 million, compared to \$0.2 million for the same period of the prior year. During the quarter, we engaged in 11 customer development projects of various sizes with approximately 3 medical product companies that included the various projects underway associated with the previously announced major contract with one of the world's largest medical device companies that licensed Covalon's proprietary medical coating technologies. Development and consulting services revenue for the six months ended March 31, 2023 increased by 210% to \$1.9 million, compared to \$0.6 million for the same period of the prior year. During the six months ended March 31, 2023, we engaged in 19 customer development projects of various sizes with approximately 5 medical product companies.

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Licensing and royalty fees for the six months ended March 31, 2023 were \$0.2 million, compared to \$0.1 million for the six months ended March 31, 2022. The timing of this revenue will vary depending on length and timing of projects and discussions with customers.

Gross margin for the three-month period ended March 31, 2023 increased to 58% compared to 53% in the same period for the prior year. During the three months ended March 31, 2023, the Company released inventory provisions of \$0.2 million as a result of changes in obsolescence estimates, as compared to an inventory provision expense of \$0.07 million being recorded during the three months ended March 31, 2022. The gross margin is significantly influenced by source of revenue and by the relative mix of products sold in any given financial period.

Gross margin for the six months ended March 31, 2023 increased to 59% compared to 49% in the same period for the prior year. During the six months ended March 31, 2023, the Company recorded inventory provision reversals resulting in a gain of \$0.2 million as a result of changes in obsolescence estimates, as compared to an inventory provision expense of \$0.8 million being recorded during the six months ended March 31, 2022.

Operating expenses for the three months ended March 31, 2023 increased \$0.7 million to \$4.9 million, compared to \$4.2 million for the prior year's comparative period. Approximately \$0.6 million relates to increased sales and marketing activities primarily due to an increase in sales and marketing staffing levels, and approximately \$0.1 million in increases in operations expenses is primarily due to increased wages related to staffing for in house collagen. These increases are partially offset by approximately \$0.08 million in reduced research and development activities compared to the comparable period.

Operating expenses for the six months ended March 31, 2023 increased \$1.4 million to \$8.9 million, compared to \$7.6 million for the prior year's comparative period. Approximately \$1.5 million relates to increased sales and marketing activities primarily due to an increase in sales and marketing staffing levels. These increases are partially offset by approximately \$0.1 million in reduced operations expenses primarily due to reduced facility expense as a result of credits received in respect of prior year property tax reassessments, and approximately \$0.1 million in reduced research and development expenses due primarily to reduced activities compared to the comparable period.

Net loss for the three months ended March 31, 2023 was \$0.7 million or \$0.03 per share, compared to a net loss of \$2.5 million or \$0.09 per share for the three months ended March 31, 2022. Net loss for the six months ended March 31, 2023 was \$1.1 million or \$0.04 per share, compared to a net loss of \$4.0 million or \$0.15 per share for the six months ended March 31, 2022.

Adjusted Gross Margin for the three-month period ended March 31, 2023 was 56% compared to 56% for the same period of the prior year. Adjusted Gross Margin for the six months ended March 31, 2023 decreased to 58% compared to 60% for the same period of the prior year. Gross margin is highly influenced by the mix of collagen-based dressings, silicone-based dressings, medical coating services, passive dressings, and related service revenues generated in the periods. Gross margin fluctuates as a result of the mix of products sold in any given quarter, or year, by product type and geography. For

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further information about Adjusted Gross Margin, see “Definitions and Reconciliations of Non-IFRS Financial Measures” below.

Adjusted EBITDA⁽¹⁾ loss for the three months ended March 31, 2023 was \$0.5 million, compared to an Adjusted EBITDA loss of \$2.2 million for the three months ended March 31, 2022. Adjusted EBITDA loss for the six months ended March 31, 2023, was \$0.4 million, compared to an Adjusted EBITDA loss of \$2.5 million for the six months ended March 31, 2022.

Business outside of direct sales in the United States is primarily comprised of distributing bulk shipments of product, which result in ‘lumpy’ or uneven revenue recognition quarter-to-quarter, depending on when bulk orders are placed, shipped to distributors, and delivered to hospitals. As is typical with many companies, including many in the healthcare field, Covalon’s lumpy revenue model makes it difficult to accurately estimate revenue recognition in any given quarter or quarter-to-quarter.

Statement of Operations

The following unaudited table presents Covalon’s consolidated statements of operations for the three- and six-month periods ended March 31st, 2023 and 2022.

<i>(unaudited)</i>	Three months ended March 31,		Six months ended March 31,	
	2023	2022	2023	2022
Revenue				
Product	\$6,105,694	\$2,975,792	\$11,350,958	7,473,490
Development and consulting services	1,108,466	233,324	1,926,812	621,691
Licensing and royalty fees	30,434	84,718	152,229	134,998
Total revenue	7,244,594	3,293,834	13,429,999	8,230,179
Cost of sales	3,072,566	1,551,773	5,563,139	4,195,741
Gross profit before operating expenses	4,172,028	1,742,061	7,866,860	4,034,438
Operating expenses				
Operations	542,755	407,919	750,634	886,179
Research and development activities	279,491	357,750	565,466	671,957
Sales, marketing and agency fees	2,209,894	1,566,210	4,239,830	2,736,387
General and administrative	1,861,677	1,834,179	3,388,572	3,259,191
	4,893,817	4,166,058	8,944,502	7,553,714

(1) See “Non-IFRS Measures” below, including for a reconciliation of the non-IFRS measures used in this release to the most comparable IFRS measures



Finance expenses (income)	(23,708)	38,018	1,260	50,241
Net (loss) from continuing operations	(698,081)	\$(2,462,015)	(1,078,902)	\$(3,569,517)
Net (loss) from discontinued operations	-	-	-	(409,295)
Net (loss)	\$(698,081)	\$(2,462,015)	\$(1,078,902)	\$(3,978,812)
Other comprehensive income (loss)				
Amount that may be reclassified to profit or loss				
Foreign currency translation adjustment continued operations	(246,523)	123,032	(263,308)	(363,552)
Other comprehensive (loss)	\$(944,604)	\$(2,338,983)	\$(1,342,210)	\$(4,342,364)
(Loss) per common share of continuing operations				
Basic (loss) per share	\$(0.03)	\$(0.09)	\$(0.04)	\$(0.14)
Diluted (loss) per share	\$(0.03)	\$(0.09)	\$(0.04)	\$(0.14)
(Loss) per common share of discontinued operations				
Basic (loss) per share	\$0.00	\$0.00	\$(0.00)	\$(0.01)
Diluted (loss) per share	\$0.00	\$0.00	\$(0.00)	\$(0.01)
(Loss) per common share				
Basic (loss) per share	\$(0.03)	\$(0.09)	\$(0.04)	\$(0.15)
Diluted (loss) per share	\$(0.03)	\$(0.09)	\$(0.04)	\$(0.15)

Non-IFRS Financial Measures

This press release makes reference to certain non-IFRS measures. These measures are not recognized or defined measures under IFRS, do not have standardized meaning prescribed by IFRS and are therefore unlikely to be comparable to similar measures presented by other companies. Rather, these measures are provided as additional financial information to complement those IFRS measures by providing further understanding of our results of operations from management's perspective. Accordingly, these measures should not be considered in isolation or as a substitute for analysis of our financial information reported under IFRS. The non-IFRS financial measures, adjustments, and reasons for adjustments should be carefully evaluated as these measures have limitations as analytical tools and should not be used in substitution for an analysis of the Company's results under IFRS. We use non-IFRS measures including "Adjusted Gross Margin" and "Adjusted EBITDA" to provide investors with supplemental measures of our operating performance and thus highlight trends in our core business that may not otherwise be apparent when relying solely on IFRS measures. We believe that securities analysts, investors and other

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interested parties frequently use non-IFRS measures in the evaluation of issuers. Our management also uses non-IFRS measures in order to facilitate operating performance comparisons from period to period, to prepare annual operating budgets and forecasts and to determine components of management compensation. The following non-IFRS financial measures are presented in this news release, and a description of the calculation for each measure is included below:

- Adjusted Gross Margin is defined as gross profit before operating expenses, plus depreciation and amortization included in cost of sales, plus inventory provision amounts.
- Adjusted EBITDA is defined as net loss, plus interest expense, plus depreciation and amortization, plus stock-based compensation, less government subsidies, plus inventory provisions, plus accounts receivable write-off expenses.

You should also be aware that the Company may recognize income or incur expenses in the future that are the same as, or similar to some of the adjustments in these non-IFRS financial measures. Because these non-IFRS financial measures may be defined differently by other companies in our industry, our definitions of these non-IFRS financial measures may not be comparable to similarly titled measures of other companies, thereby diminishing their utility.

The table below provides a reconciliation of gross profit before operating expenses under IFRS in the consolidated financial statements to Adjusted Gross Margin for the three and six months ended March 31st 2023 and 2022. Management believes that Adjusted Gross Margin is useful in assessing the performance of the Company's ongoing operations and its ability to generate cash flows from period to period. The adjusting items below are considered to be outside of the Company's core operating results, and these items can distort the trends associated with the Company's ongoing performance, even though some of those expenses may recur.

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<i>(unaudited)</i>	Three months ended March 31,		Six months ended March 31,	
	<u>2023</u>	<u>2022</u>	<u>2023</u>	<u>2022</u>
Gross profit before operating expenses	\$4, 172,028	\$1,742,061	\$7,866,860	\$4,034,438
Add: Depreciation and amortization	53,050	41,530	109,083	95,825
Add: Inventory provisions (reversals)	(158,724)	73,278	(158,724)	792,969
Adjusted Gross Margin	4,066,355	1,856,869	7,817,219	4,923,232
Adjusted Gross Margin (%)	56%	56%	58%	60%

The table below provides a reconciliation of net loss under IFRS in the consolidated financial statements to Adjusted EBITDA for the three and six months ended March 31st 2023 and 2022. Management believes that these non-IFRS measures are useful in assessing the performance of the Company's ongoing operations and its ability to generate cash flows to funds its cash requirements from period to period. The adjusting items below are considered to be outside of the Company's core operating results, and these items can distort the trends associated with the Company's ongoing performance, even though some of those expenses may recur.

<i>(unaudited)</i>	Three months ended March 31,		Six months ended March 31,	
	<u>2023</u>	<u>2022</u>	<u>2023</u>	<u>2022</u>
Net income (loss)	(\$698,081)	(\$2,462,015)	(\$1,078,902)	(\$3,569,517)
Add: Finance expense (gains)	(23,708)	38,018	1,260	50,241
Add: Depreciation and amortization	233,324	92,360	483,409	202,324
Add: Stock based compensation	173,150	18,217	329,457	39,251
Add: Inventory provisions (reversals)	(158,724)	73,278	(158,724)	792,969
Adjusted EBITDA	(\$474,039)	(\$2,240,142)	(\$423,500)	(\$2,484,732)

To learn more about Covalon, please contact:

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About Covalon

Covalon Technologies Ltd. is a patient-driven medical device company, built on the relentless pursuit to help the most vulnerable patients have a better chance at healing. Through a strong portfolio of patented technologies and solutions for advanced wound care, infection prevention, and medical device coatings, we offer innovative, gentler, and more compassionate options for patients to heal with less infections, less pain, and better outcomes. Our solutions are designed for patients and made for care providers. Covalon leverages its patented medical technology platforms and expertise in two ways: (i) by developing products that are sold under Covalon's name; and (ii) by developing and commercializing medical products for other medical companies under development and license contracts. The Company is listed on the TSX Venture Exchange, having the symbol COV and trades on the OTCQX Market under the symbol CVALF. To learn more about Covalon, visit our website at www.covalon.com.

Neither the TSX Venture Exchange nor its Regulation Services Provider (as that term is defined in the policies of the TSX Venture Exchange) accepts responsibility for the adequacy or accuracy of this release.

This news release may contain forward-looking statements which reflect the Company's current expectations regarding future events. The forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "plan", "estimate", "expect", "intend", or variations of such words and phrases or state that certain actions, events, or results "may", "could", "would", "might", "will" or "will be taken", "occur", or "be achieved". In addition, any statements that refer to expectations, projections or other characterizations of future events or circumstances contain forward-looking information. Statements containing forward-looking information are not historical facts, but instead represent management's expectations, estimates, and projections regarding future events. Forward-looking statements involve risks and uncertainties, including, but not limited to, the factors described in greater detail in the "Risks and Uncertainties" section of our management's discussion and analysis of financial condition and results of operations for the year ended September 30, 2022, which is available on the Company's profile at www.sedar.com, any of which could cause results, performance, or achievements to differ materially from the results discussed or implied in the forward-looking statements. Investors should not place undue reliance on any forward-looking statements. The forward-looking statements contained in this news release are made as of the date of this news release, and the Company assumes no obligation to update or alter any forward-looking statements, whether as a result of new information, further events, or otherwise, except as required by law.

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