Covalon Technologies Ltd.

CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS (UNAUDITED)

For the three and six months ended March 31, 2023 and 2022

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NOTICE OF NO AUDITOR REVIEW OF INTERIM FINANCIAL STATEMENTS

Under National Instrument 51-102, Part 4, subsection 4.3(3) (a), if an auditor has not performed a review of the interim financial statements, they must be accompanied by a notice indicating that the interim financial statements have not been reviewed by an auditor.

The accompanying unaudited condensed consolidated interim financial statements of Covalon Technologies Ltd. (the "Company") have been prepared by and are the responsibility of the Company's management. The unaudited condensed consolidated interim financial statements are prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board ("IFRS") and reflect management's best estimates and judgment based on information currently available. The Company's independent auditor has not performed a review of these unaudited condensed consolidated interim financial statements.

Covalon Technologies Ltd.

CONDENSED CONSOLIDATED INTERIM STATEMENTS OF FINANCIAL POSITION (UNAUDITED)

Expressed in Canadian Dollars

	March 31, 2023	September 30, 2022
Assets		
Current assets		
Cash and cash equivalents	**$10,766,955**	$14,061,631
Cash in escrow (Note 3)	**-**	1,370,700
Accounts receivable	**5,802,650**	4,732,430
Inventories (Note 4)	**6,927,226**	4,965,668
Prepaid expenses	**1,060,730**	2,097,628
Total current assets	**24,557,561**	27,228,057
Non-current assets		
Restricted cash	**135,329**	-
Property, plant and equipment (Note 6)	**1,320,172**	1,215,970
Intangible assets (Note 5)	**1,380,427**	1,277,327
Right-of-use assets (Note 8)	**528,150**	656,727
Total non-current assets	**3,364,078**	3,150,024
Total assets	**$27,921,639**	$30,378,081
Liabilities and shareholders' equity		
Current liabilities		
Accounts payable and accrued liabilities	**$3,645,619**	$3,720,208
Lease liabilities (Note 9)	**629,368**	609,578
Deferred revenue (Note 7)	**244,412**	209,070
Total current liabilities	**4,519,399**	4,538,856
Non-current liabilities		
Deferred revenue (Note 7)	**-**	51,401
Lease liabilities (Note 9)	**1,239,613**	1,559,063
Total non-current liabilities	**1,239,613**	1,610,464
Total liabilities	**5,759,012**	6,149,320
Shareholders' equity		
Share capital (Note 10)	**43,279,520**	43,843,344
Contributed surplus	**11,117,393**	11,277,493
Foreign exchange translation reserve	**2,749,901**	3,013,209
Accumulated deficit	**(34,984,187)**	(33,905,285)
Total shareholders' equity	**22,162,627**	24,228,761
Total liabilities and shareholders' equity	**$27,921,639**	$30,378,081

Contingencies and commitments (Note 18)

On behalf of the Board:

(signed) "Abe Schwartz" *Director*

(signed) "Brian Pedlar" *Director*

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

Covalon Technologies Ltd.

CONDENSED CONSOLIDATED INTERIM STATEMENTS OF OPERATIONS AND COMPREHENSIVE LOSS (UNAUDITED)

Expressed in Canadian Dollars

	Three months ended March 31, 2023	Three months ended March 31, 2022	Six months ended March 31, 2023	Six months ended March 31, 2022
Revenue				
Product	**$6,105,694**	$2,975,792	**$11,350,958**	$7,473,490
Development and consulting services	**1,108,466**	233,324	**1,926,812**	621,691
Licensing and royalty fees	**30,434**	84,718	**152,229**	134,998
Total revenue	**7,244,594**	3,293,834	**13,429,999**	8,230,179
Cost of sales	**3,072,566**	1,551,773	**5,563,139**	4,195,741
Gross profit before operating expenses	**4,172,028**	1,742,061	**7,866,860**	4,034,438
Operating expenses				
Operations	**542,755**	407,919	**750,634**	886,179
Research and development activities	**279,491**	357,750	**565,466**	671,957
Sales, marketing and agency fees	**2,209,894**	1,566,210	**4,239,830**	2,736,387
General and administrative	**1,861,677**	1,834,179	**3,388,572**	3,259,191
	4,893,817	4,166,058	**8,944,502**	7,553,714
Finance expenses (income)	**(23,708)**	38,018	**1,260**	50,241
Net (loss) from continuing operations	**(698,081)**	(2,462,015)	**(1,078,902)**	(3,569,517)
Net (loss) from discontinued operations	**-**	-	**-**	(409,295)
Net (loss)	**$(698,081)**	$(2,462,015)	**$(1,078,902)**	$(3,978,812)
Other comprehensive income (loss)				
Amount that may be reclassified to profit or loss				
Foreign currency translation adjustment - continued operations	**(246,523)**	123,032	**(263,308)**	(363,552)
Total comprehensive (loss)	**$(944,604)**	$(2,338,983)	**$(1,342,210)**	$(4,342,364)
(Loss) per common share of continuing operations				
Basic (loss) per share (Note 16)	**$(0.03)**	$(0.09)	**$(0.04)**	$(0.14)
Diluted (loss) per share (Note 16)	**$(0.03)**	$(0.09)	**$(0.04)**	$(0.14)
(Loss) per common share of discontinued operations				
Basic (loss) per share (Note 16)	**$0.00**	$0.00	**$0.00**	$(0.01)
Diluted (loss) per share (Note 16)	**$0.00**	$0.00	**$0.00**	$(0.01)
(Loss) per common share				
Basic (loss) per share (Note 16)	**$(0.03)**	$(0.09)	**$(0.04)**	$(0.15)
Diluted (loss) per share (Note 16)	**$(0.03)**	$(0.09)	**$(0.04)**	$(0.15)

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

Covalon Technologies Ltd.

CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN EQUITY (UNAUDITED)

Expressed in Canadian Dollars

	Number of shares	Share capital	Contributed surplus	Accumulated deficit	Foreign exchange translation reserve	Total
Balance at October 1, 2021	25,868,677	$44,676,999	$11,833,354	$(24,242,072)	$1,106,246	$33,374,527
Share-based payment expense (Note 11)	-	-	45,807	-	-	45,807
Exercise of stock options	30,000	178,817	(112,817)	-	-	66,000
Exercise of warrants	30,000	98,705	(38,705)			60,000
Net loss for the period	-	-	-	(3,978,812)	-	(3,978,812)
Foreign currency translation adjustment	-	-	-	-	(363,552)	(363,552)
Balance at March 31, 2022	**25,928,677**	**$44,954,521**	**$11,727,639**	**$(28,220,884)**	**$742,694**	**$29,203,970**
Balance at October 1, 2022	25,287,777	$43,843,344	$11,277,493	$(33,905,285)	$3,013,209	$24,228,761
Share-based payment expense (Note 11)	-	-	329,457	-	-	329,457
Buyback of common shares (Note 10)	(383,100)	(563,824)	(489,557)	-	-	(1,053,381)
Net loss for the period	-	-	-	(1,078,902)	-	(1,078,902)
Foreign currency translation adjustment	-	-	-	-	(263,308)	(263,308)
Balance at March 31, 2023	**24,904,677**	**$43,279,520**	**$11,117,393**	**$(34,984,187)**	**$2,749,901**	**$22,162,627**

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

Covalon Technologies Ltd.

CONDENSED CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS (UNAUDITED)

Expressed in Canadian Dollars

	Six months ended March 31,	
	2023	2022
Cash flows from (used in) operating activities		
Net loss for the period from continuing operations	**$(1,078,902)**	$(3,569,517)
Adjustments to reconcile net income to net cash used in operating activities:		
Depreciation of property, plant and equipment (Note 6)	**260,346**	110,740
Amortization of intangible assets (Note 5)	**102,391**	75,689
Depreciation - right of use assets (Note 8)	**120,672**	114,289
Share-based payment expense (Note 11)	**329,457**	39,251
Accrued interest income	**(15,061)**	-
Interest expense and accretion	**42,757**	50,241
Cash used in operating activities before change in non-cash working capital balances	**(238,340)**	(3,179,307)
Net changes in non-cash working capital balances:		
Accounts receivable	**(1,114,566)**	2,984,798
Prepaid expenses	**982,451**	(379,847)
Inventories	**(1,976,565)**	(147,497)
Accounts payable and accrued liabilities	**(109,661)**	(1,554,477)
Deferred revenue	**(18,124)**	(61,162)
Total net changes in non-cash working capital balances	**(2,236,465)**	841,815
Total cash flows from (used in) operating activities	**(2,474,805)**	(2,337,492)
Cash flows from (used in) investing activities		
Purchase of property, plant and equipment (Note 6)	**(315,077)**	(264,084)
Purchase of intangible assets (Note 5)	**(286,129)**	(101,296)
Disposal of property, plant and equipment	**-**	101,668
Restricted cash	**(135,329)**	(2,570)
Total cash flows used in investing activities	**(736,535)**	(266,282)
Cash flows from (used in) financing activities		
Buyback of common shares (Note 10)	**(1,053,381)**	-
Exercise of options	**-**	66,000
Exercise of warrants	**-**	60,000
Payment of lease liabilities (Note 9)	**(340,026)**	(321,039)
Total cash flows used in financing activities	**(1,393,407)**	(195,039)
Foreign exchange rate changes on cash	**(60,629)**	(87,224)
Total cash flows during the period of continuing operations	**(4,665,376)**	(2,886,037)
Total cash flows during the period of discontinued operations	**1,370,700**	(482,422)
Total cash flows during the period	**(3,294,676)**	(3,368,459)
Cash and cash equivalents, beginning of the period	**$14,061,631**	$22,946,923
Cash and cash equivalents, end of the period	**$10,766,955**	$19,578,464

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

1. CORPORATE INFORMATION

Covalon Technologies Ltd. ("the Company") is incorporated under the laws of Ontario and is engaged in the business of researching, developing, manufacturing, and marketing of patent-protected medical products that improve patient outcomes and save lives in the areas of infection management, advanced wound care, and surgical procedures. The unaudited condensed consolidated interim financial statements of Covalon Technologies Ltd. for the three and six months ended March 31, 2023 comprise the results of the Company and its wholly owned subsidiaries. The Company leverages its patented medical technology platforms and expertise in two ways: (i) by developing products that are sold under the Company's name; and (ii) by developing and commercializing medical products for other medical companies under development and license contracts. The Company has received regulatory approval on numerous products and leverages contract manufacturers to make its products and distribution contracts to sell its commercialized products to medical customers. The Company generates its revenues through development contracts, licensing agreements, distribution contracts, and sales of products.

The Company is listed on the TSX Venture Exchange, having the symbol COV. The Company also trades on the OTCQX Best Market, having the symbol of CVALF.

The address of the Company's corporate office and principal place of business is 1660 Tech Avenue, Unit 5, Mississauga, Ontario, Canada.

2. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES AND BASIS OF PRESENTATION

The Company's unaudited condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board ("IFRS") applicable to the preparation of interim financial statements, including IAS 34, Interim Financial Reporting. These condensed consolidated interim financial statements are presented in Canadian dollars and should be read in conjunction with the Company's annual financial statements for the year ended September 30, 2022, which were prepared in accordance with IFRS.

Other than as noted herein, the accounting policies adopted are consistent with those of the previous financial year end. Certain comparative amounts within operating expenses have been reclassified to conform to current period classification.

The unaudited condensed consolidated interim financial statements were authorized for issue by the Board of Directors on May 24, 2023.

Share-based payments

The Company operates a long-term incentive plan under which the Company issues equity instruments of the Company as consideration in exchange for employee or director services (the "Plan"). The Plan is open to certain directors and employees of the Company. The Plan regulates the issuance of the following equity instruments: stock options, deferred share units ("DSUs") and restricted shares ("RSUs").

The maximum number of common shares which may be issued under the Plan cannot exceed 10% of the common shares issued and outstanding at any given time, calculated on a non-diluted basis. Grants held by non-employee directors of the Company are at all times limited to no more than 1% of the common shares issued and outstanding, calculated on a non-diluted basis, and the total annual grant to any one non-employee director under the Plan cannot exceed a grant value of $150,000 in total equity.

Stock options

The Company may decide to issue stock options as consideration in exchange for employee or director services. Stock options typically vest over three to four years and expire after five years. The fair value of the grant of the stock options is recognized in the consolidated statement of income and comprehensive income as an expense. The total amount to be expensed is determined by reference to the fair value of the options granted.

The total expense is recognized over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. At the end of each reporting date, the Company revises its estimates of the number of options that are expected to vest based on the non-market vesting conditions.

The fair value of stock options is estimated using the Black-Scholes option pricing model. This model requires the input of a number of assumptions, including expected dividend yield, expected share price volatility, expected time until exercise and risk-free interest rates. Although the assumptions used reflect historical performance and management's best estimates, they involve inherent uncertainties based on conditions outside the Company's control. Changes in these assumptions could significantly impact the valuation of the share-based payment expense.

The contributed surplus within shareholders' equity is reduced as the stock options are exercised. If the stock options are exercised, the amount initially recorded for the stock options in contributed surplus is credited to common shares, along with the proceeds received on the exercise. If the stock options expire unexercised, the amount initially recorded for the stock options remains in contributed surplus.

RSUs

The Company may decide to issue RSUs as consideration in exchange for employee or director services. RSUs typically vest over three years. The fair value of the grant of the RSUs is recognized as a share-based compensation expense. The total amount to be expensed is determined by reference to the fair value of the RSUs granted.

The total expense is recognized over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. At the end of each reporting date, the Company revises its estimates of the number of RSUs that are expected to vest based on the non-market vesting conditions. The fair value of RSUs is estimated using the Company's quoted market price on the grant date.

DSUs

The Company may issue DSUs as consideration in exchange for director or officer services. DSUs typically vest over three years. The fair value of the grant of the DSUs is recognized as a share-based compensation expense. The total amount to be expensed is determined by reference to the fair value of the DSUs granted.

The total expense is recognized over the vesting period, which is the period over which all of the specified vesting conditions are to be satisfied. At the end of each reporting date, the Company revises its estimates of the number of DSUs that are expected to vest based on the non-market vesting conditions. The fair value of DSUs is estimated using the Company's quoted market price on the grant date.

Accounting standards issued but not yet adopted

IAS 1 – Presentation of Financial Statements

On January 23, 2020, the IASB issued an amendment to IAS 1 to clarify that liabilities are classified as either current or non-current, depending on the rights that exist at the end of the reporting period. The standard is effective for periods beginning on or after January 1, 2023, and the Company has assessed that there will be no impact of applying the new standard on the consolidated financial statements.

Expressed in Canadian Dollars

Definition of Accounting Estimates (Amendments to IAS 8)

On February 12, 2021, the IASB issued Definition of Accounting Estimates (Amendments to IAS 8). The amendments will require the disclosure of material accounting policy information rather than disclosing significant accounting policies and clarifies how to distinguish changes in accounting policies from changes in accounting estimates. The amendments are effective for annual periods beginning on or after January 1, 2023. The Company intends to adopt this amendment in its Consolidated Financial Statements for the annual period beginning October 1, 2023. The adoption of this amendment is not expected to have a material impact on the consolidated financial statements.

3. AQUAGUARD SALE

On July 29, 2021, the Company sold the AquaGuard product line to TIDI Products, LLC ("TIDI"), an arm's length party, for $37,837,852 including post-closing adjustments related to actual amounts of inventory and indebtedness. The purchase price of $37,837,852 included $2,513,200 placed in escrow for indemnity claims (which escrow amounts would be released 50% in 12 months following closing and the remaining 50% on September 30, 2022, assuming there were no claims). On August 2, 2022, 50% of the funds were received from escrow, and on October 3, 2022, the final 50% was received from escrow. The financial information related to the AquaGuard product line is reported in the current and comparative periods as discontinued operations.

The financial performance information presented for the three and six months ended March 31, 2023, and March 31, 2022, is summarized below and is included in the condensed consolidated interim statements of operations and comprehensive loss as net loss from discontinued operations:

	Three months ended March 31,		**Six months ended March 31,**	
	2023	2022	**2023**	2022
Revenue	-	-	-	$483,010
Cost of sales and operating expenses	-	-	-	874,306
Finance expenses	-	-	-	17,999
Net income (loss) from discontinued operations	-	-	-	(409,295)

Disclosures with respect to the consolidated statements of cash flows for the six months ended March 31, 2023 are as follows:

	March 31, 2023	March 31, 2022
Cash flows from operating activities	**-**	(384,740)
Cash flows from investing activities	**1,370,700**	(12,623)
Cash flows from financing activities	**-**	(85,059)
Total cash flow	**1,370,700**	(482,422)

Expressed in Canadian Dollars

4. INVENTORIES

Inventories consist of the following:

	March 31, 2023	September 30, 2022
Raw materials	**$2,352,058**	$1,524,083
Finished goods	**7,326,382**	6,337,693
Inventory provision	**(2,751,214)**	(2,896,108)
	$6,927,226	$4,965,668

Cost of product sales for the three and six months ended March 31, 2023, included $3,019,516 (2022 - $1,510,242) and $5,454,056 (2022 - $4,099,916), respectively, in inventoried materials.

5. INTANGIBLE ASSETS

Intangible assets are comprised of the following amounts:

	Deferred Development Costs ($)	**Patents ($)**	**Trademarks ($)**	**Computer Software ($)**	**Total ($)**
Cost					
Balance at September 30, 2022	2,286,362	1,080,912	82,362	372,252	3,821,888
Transfer to property, plant and equipment	-	-	-	(65,389)	(65,389)
Additions	39,328	-	-	246,801	286,129
Foreign exchange	(29,024)	(13,721)	(1,046)	(3,895)	(47,686)
Balance at March 31, 2023	**2,296,666**	**1,067,191**	**81,316**	**549,769**	**3,994,942**
Accumulated amortization					
Balance at September 30, 2022	1,996,030	548,531	-	-	2,544,561
Amortization	56,508	26,121	-	19,762	102,391
Foreign exchange	(25,412)	(6,998)	-	(27)	(32,437)
Balance at March 31, 2023	**2,027,126**	**567,654**	**-**	**19,735**	**2,614,515**
Carrying amounts					
At September 30, 2022	290,332	532,381	82,362	372,252	1,277,327
At March 31, 2023	**269,540**	**499,537**	**81,316**	**530,034**	**1,380,427**

As at September 30, 2022, included in computer software is an amount of $372,252 which primarily related to new information systems where amortization had not yet commenced as they had not yet been placed into service, and during the three months ended December 31, 2022, these assets were placed into service and amortization commenced.

Expressed in Canadian Dollars

6. PROPERTY, PLANT AND EQUIPMENT

	Computer Hardware, Furniture and Fixtures ($)	Production and Lab Equipment ($)	Leasehold Improvements ($)	Total ($)
Cost				
Balance at September 30, 2022	689,748	1,988,726	377,492	3,055,966
Transfer from intangible assets	-	65,389	-	65,389
Additions	19,362	295,715	-	315,077
Foreign exchange	(8,377)	(26,084)	(4,792)	(39,253)
Balance at March 31, 2023	**700,733**	**2,323,746**	**372,700**	**3,397,179**
Accumulated depreciation				
Balance at September 30, 2022	350,312	1,170,877	318,807	1,839,996
Depreciation	70,271	167,579	22,496	260,346
Foreign exchange	(4,849)	(15,087)	(3,399)	(23,335)
Balance at March 31, 2023	**415,734**	**1,323,369**	**337,904**	**2,077,007**
Carrying amounts				
At September 30, 2022	339,436	817,849	58,685	1,215,970
At March 31, 2023	**284,999**	**1,000,377**	**34,796**	**1,320,172**

7. DEFERRED REVENUE

	March 31, 2023	September 30, 2022
Balance, beginning of year	**$260,471**	$577,097
Add:		
Deferred licensing and services revenue	**-**	444,214
Deferred product	**$374,358**	709,654
Less:		
Recognition of deferred product	**(307,528)**	(746,938)
Recognition of deferred licensing and services revenue	**(80,824)**	(791,970)
Foreign exchange	**(2,065)**	68,414
Balance, end of year	**244,412**	260,471
Current portion	**(244,412)**	(209,070)
Non-current portion	**-**	$51,401

Expressed in Canadian Dollars

8. RIGHT-OF-USE ASSETS

	Right-of-use assets ($)
Balance at October 1, 2022	656,727
Depreciation	(120,672)
Foreign exchange	(7,905)
Balance at March 31, 2023	**528,150**

The Company leases office space in Mississauga, Canada and Seattle, USA. Following the sale of AquaGuard (Note 3) the leased facility in Seattle was impaired during the year ended September 30, 2021, as it is not currently expected to generate any future cash in flows. The Company intends to pursue sublease arrangements and will assess for reversal of impairment should the facts change.

9. LEASE LIABILITIES

Lease liabilities are comprised of the following amounts:

	Lease liabilities ($)
Balance at October 1, 2022	2,168,641
Interest	42,757
Payments	(340,026)
Foreign exchange	(2,391)
Balance at March 31, 2023	**1,868,981**
Less: Current portion	629,368
Long-term portion	1,239,613

Following the impairment of the right of use asset related to the Company's Seattle lease agreement at September 30, 2021 (Note 8), an onerous contract liability was recognized in accounts payable and accrued liabilities related to future variable lease payments that are not included in the lease liability. At March 31, 2023 the amount of this liability was $352,585 (September 30, 2022 - $396,713).

10. SHAREHOLDERS' EQUITY

Common Shares

The Company is authorized to issue an unlimited number of common shares with no par value. All shares are fully paid.

On May 25, 2022, the Company announced that it had filed its intention to make a normal course issuer bid ("NCIB") for its common shares with the TSX Venture Exchange for up to 1,296,433 shares, representing 5% of the issued and outstanding common shares. Repurchases under the NCIB program were approved by the TSX Venture Exchange, commenced on June 2, 2022, and are authorized to continue until the earlier of: (a) May 31, 2023; and (b) the date in which the maximum number of common shares purchasable under the NCIB have been acquired by the Company. All common shares that are repurchased by the Company under the NCIB program will be cancelled, with any excess or deficiency as compared to the weighted average cost of common shares being charged to contributed surplus.

Under the NCIB, the Company is limited in making daily purchases of up to 8,000 common shares.

Expressed in Canadian Dollars

On June 29, 2022, in connection with the NCIB, the Company entered into an automatic share purchase plan ("ASPP") with a designated broker. The ASPP is intended to allow for the purchase of the Company's common shares under the NCIB at times when the Company would ordinarily not be permitted to purchase its common shares due to regulatory restrictions and customary self-imposed blackout periods. Pursuant to the ASPP, prior to entering into a blackout period, the Company may instruct the designated broker to make purchases under the NCIB in accordance with the terms of the ASPP. Such purchases will be made by the designated broker in its sole discretion based on parameters established by the Company prior to the blackout period in accordance with the rules of the TSX Venture Exchange, applicable securities laws and the terms of the ASPP. In accordance with the terms of the ASPP, the Company is able to terminate any instructions given to the designated broker with minimal notice. The Company has continued with the ASPP since June 29, 2022 without notice to terminate.

As at September 30, 2022, the Company had purchased 640,900 of its common shares under the NCIB. For the three and six months ended March 31, 2023, the Company purchased an additional 220,900 and 383,100 of its common shares under the NCIB, respectively. Subsequent to March 31, 2023, the Company has purchased an additional 167,400 of its common shares under the NCIB. The Company has purchased a total of 1,191,400 of its common shares since repurchases commenced under the NCIB.

Warrants

The following is a summary of all warrants:

	Number of Warrants	Weighted average exercise Price	Weighted Average Expiry (years)
Balance at September 30, 2022	**2,920,000**	**$2.14**	**2.10**
Exercised during the period	-	-	-
Balance at March 31, 2023	**2,920,000**	**$2.14**	**1.60**

11. SHARE-BASED PAYMENTS

Omnibus Long-Term Incentive Plan

On March 8, 2023, the shareholders approved the Plan. The Plan supersedes and replaces the stock option plan which was in place previously.

Issuance of RSUs and DSUs

RSUs and DSUs vest over a period of three years on each anniversary of the grant date unless a different vesting schedule is approved by the Board. DSUs are only eligible to be converted into common shares of the Company when the holder ceases its relationship to the Company. The Company has not yet issued any RSUs and DSUs under the Plan.

Stock Options

Stock options outstanding are non-transferable options to purchase common shares of the Company which may be granted to Directors, officers, employees, or service providers of the Company. The terms of the stock options provide that the Directors have the right to grant options to acquire common shares of the Company at not less than the closing market price of the shares on the day preceding the grant at terms of up to ten years. No amounts are paid or payable by the recipient on receipt of the stock option, and the stock options granted to date are not dependent on any performance-based criteria, however, future stock options may be granted so as to be dependent on performance-based criteria. All stock options issued to date will vest as follows: 34% of the options vest in one year, with a further 33% vesting in each of the subsequent two years on the anniversary of the initial grant date. Future grants of stock options may vest over alternative periods as authorized by the Directors.

Expressed in Canadian Dollars

The following is a summary of changes in stock options from October 1, 2022 to March 31, 2023:

Grant Date	Expiry Date	Exercise Price	Opening Balance	Granted	Forfeited/ Expired	Closing Balance	Vested	Unvested	Weighted Average Expiry (years)
25-Oct-17	25-Oct-22	$3.80	60,000	-	(60,000)	-	-	-	-
21-Dec-17	21-Dec-22	$4.65	55,000	-	(55,000)	-	-	-	-
24-Jan-18	24-Jan-23	$6.02	60,000	-	(60,000)	-	-	-	-
27-Sep-18	27-Sep-23	$8.50	67,500	-		67,500	67,500	-	0.49
22-Dec-18	22-Dec-23	$4.28	47,500	-	(12,500)	35,000	35,000	-	0.73
15-Mar-19	15-Mar-24	$5.03	40,000	-		40,000	40,000	-	0.96
28-Mar-22	28-Mar-27	$2.19	465,000	-	(17,500)	447,500	152,150	295,350	3.99
06-Sep-22	06-Sep-27	$2.50	437,500	-	(5,000)	432,500	-	432,500	4.43
			1,232,500	**-**	**(210,000)**	**1,022,500**	**294,650**	**727,850**	**3.72**
Weighted Average Exercise Price			**$3.19**	**$0.00**	**$4.52**	**$2.92**	**$4.27**	**$2.37**	

Share Based Payment Expense

Total share-based payment expense recognized during the three and six months ended March 31, 2023 for continuing operations, as part of employee benefits were $173,150 (2022 - $18,217) and $329,457 (2022 - $39,251), respectively.

Total share-based payment expense recognized during the three and six months ended March 31, 2023 for discontinued operations, as part of employee benefits was $nil (2022 - $nil) and $nil (2022 - $6,556), respectively.

12. FINANCIAL RISK MANAGEMENT

The following is a discussion of market, credit, and liquidity risks and related mitigation strategies that have been identified.

Credit Risk

The Company is exposed to credit risk associated with its cash and cash equivalents and accounts receivable. The risk is reduced by having accounts receivables insured or obtaining letters of credit when the Company determines that it is warranted. The Company applies the simplified approach to providing for expected credit losses, which allows the use of a lifetime expected loss for all receivables. Receivables have been grouped based on shared credit risk characteristics and the days outstanding to measure the expected credit loss. On this basis the loss allowance at March 31, 2023 and September 30, 2022 is not significant.

Accounts receivable are written off when there is no reasonable expectation of recovery which may be supported by failure to make contractual payments for more than 180 days as well as other factors.

Accounts receivable are subject to normal industry risks in each geographic region in which the Company operates. The Company attempts to manage these risks by dealing with creditworthy customers; however, due to the limited number of potential customers in each market this is not always possible. As at March 31, 2023, three customers accounted for 57% (September 30, 2022 – three customers for 71%) of the accounts receivable balance. These customers, who are distributors and strategic partners of the Company, represent a large portion of the Company's sales. Credit risk exposure is mitigated by strong credit granting policies, the use of Letters of Credit, and due diligence procedures for new customers.

The aging of accounts receivable is as follows:

	March 31, 2023	September 30, 2022
Current	**$4,647,598**	$4,449,960
30-60 days past due	**996,360**	203,988
Over 60 days past due	**158,692**	78,482
	5,802,650	4,732,430

Interest Rate Risk

The Company is subject to interest rate risk on its cash and cash equivalents. The Company believes that interest rate risk is low due to market based variable interest rates.

Currency Risk

The Company's exposure to foreign currency risk at the end of the reporting period, expressed in Canadian dollars, was as follows:

	March 31, 2023				**September 30, 2022**			
	Canadian	USD	GBP	**Total**	CAD	USD	GBP	**Total**
Cash and cash equivalents	$249,850	$10,459,219	$57,886	**$10,766,955**	$307,483	$13,599,225	$154,923	**$14,061,631**
Accounts receivable	$288,798	$5,513,852	-	**$5,802,650**	$1,340	$4,731,090	-	**$4,732,430**
Restricted cash and cash in escrow	-	$135,329	-	**$135,329**	-	$1,370,700	-	**$1,370,700**
Accounts payable and accrued liabilities	$257,861	$3,364,722	$23,036	**$3,645,619**	$961,691	$2,711,995	$46,522	**$3,720,208**
Lease liabilities	$678,600	$1,190,381	-	**$1,868,981**	$805,625	$1,363,016	-	**$2,168,641**

If exchange rates were to change by 5% at March 31, 2023 total comprehensive loss would change by $579,407 (September 30, 2022 - $786,720).

Expressed in Canadian Dollars

Fair Value

The fair values of cash and cash equivalents, cash in escrow, accounts receivable, accounts payable and accrued liabilities and lease liabilities approximate their carrying values, due to their relatively short periods to maturity.

Liquidity risk

The Company continually monitors working capital to ensure sufficient cash is available to meet operational and capital expenditure requirements. The Company has contractual obligations related to lease liabilities and accounts payable and accrued liabilities that are due as reflected in the following table:

	Carrying amount ($)	Future cash flows ($)	Less than 1 year ($)	Between 1 and 5 years ($)	Greater than 5 years ($)
Accounts payable and accrued liabilities	3,645,619	3,645,619	3,645,619	-	-
Lease liabilities	1,868,981	1,962,497	690,657	1,271,840	-
Total	**5,514,600**	**5,608,116**	**4,336,276**	**1,271,840**	-

13. CAPITAL MANAGEMENT

The Company defines capital that it manages as its shareholders' equity comprising share capital, contributed surplus, and foreign exchange translation reserve accumulated deficit. Its objectives when managing capital are to ensure that the Company will continue as a going concern, so that it can provide services to its customers and returns to its shareholders. The capital at March 31, 2023 is $22,162,627 (September 30, 2022 – $24,228,761).

The Company manages its capital structure and adjusts it in light of economic conditions. The Company, upon approval from its Board of Directors, will make changes to its capital structure as deemed appropriate under the specific circumstances.

14. RELATED PARTY TRANSACTIONS

Key management personnel include the Company's directors and senior management team. These individuals are responsible for planning, directing, and controlling the activities of an entity. Key management personnel compensation comprised:

	Three months ended March 31		Six months ended March 31,	
	2023	2022	**2023**	2022
Compensation and short-term employee benefits	**$300,956**	$286,046	**$589,412**	$518,894
Share based payment expense	**26,024**	6,357	**46,776**	12,481
	326,980	292,403	**636,188**	531,375

During the year end September 30, 2013, a non-interest bearing loan of $50,000 was made to a key employee. As of March 31, 2023, $10,000 of this loan remained outstanding.

Expressed in Canadian Dollars

15. EXPENSES BY NATURE

The consolidated statements of operations and comprehensive loss include the following expenses by nature:

	Three months ended March 31,		**Six months ended March 31,**	
	2023	2022	**2023**	2022
Inventoried materials	**$3,019,516**	$1,510,243	**$5,454,056**	$4,099,916
Wages, benefits, consulting fees, director compensation	**3,232,472**	3,146,577	**5,865,849**	5,492,436
Share based payments	**173,150**	18,217	**329,457**	39,251
Depreciation and amortization	**233,324**	92,360	**483,409**	202,324
Facility	**(5,404)**	93,101	**57,279**	317,588
Professional fees	**256,620**	182,301	**497,736**	627,797
Other expenses	**1,056,705**	675,032	**1,819,855**	970,143
Total	**$7,966,383**	$5,717,831	**$14,507,641**	$11,749,455

Depreciation and amortization	**Three months ended March 31,**		**Six months ended March 31,**	
	2023	2022	**2023**	2022
Cost of product sales	**$53,050**	$41,530	**$109,083**	$95,825
Operations	**22,985**	540	**45,240**	1,300
Research and development activities	**34,340**	9,023	**71,759**	15,249
General and administrative	**122,949**	41,267	**257,327**	89,950
Total depreciation and amortization	**$233,324**	$92,360	**$483,409**	$202,324

16. LOSS PER SHARE

The weighted average number of shares outstanding during the three and six months ended March 31, 2023 was 24,972,631 and 25,076,062, respectively (March 31, 2022 – 25,928,018 and 25,898,018).

For both the three and six months ended March 31, 2023, and March 31, 2022, the computation of diluted loss per share from both continuing and discontinued operations is equal to the basic loss per share due to the Company incurring losses.

For the period ended March 31, 2023, of the 1,022,500 (2022 – 1,404,999) stock options and 2,920,000 (2022 – 2,920,000) warrants not included in the calculation of diluted loss per share 3,214,650 (2022 – 3,650,558) were exercisable.

Expressed in Canadian Dollars

17. SEGMENT REPORTING

During the three months ended March 31, 2023, the Company generated continuing operations revenue of $5,397,205 (2022 – $2,461,582) in the US, $1,668,412 (2022 – $329,581) in the Middle East, $3,850 (2022 – $24,931) in Canada, and $175,127 (2022 – $477,740) in the rest of the world.

During the six months ended March 31, 2023, the Company generated continuing operations revenue of $9,288,863 (2022 – $6,053,448) in the US, $3,032,469 (2022 – $1,068,581) in the Middle East, $41,284 (2022 – $31,931) in Canada, and $1,067,383 (2022 – $1,076,219) in the rest of the world.

As of March 31, 2023, the Company had $3,177,330 (September 30, 2022 - $3,098,014) of its property, plant, and equipment, right-of-use assets and intangible assets located in Canada and $51,419 (September 30, 2022 - $52,010) in the USA.

18. CONTINGENCIES AND COMMITMENTS

The following are commitments of the Company beyond March 31, 2023:

	September 30,		
	2023	**2024**	**2025**
Purchase obligations	$133,874	-	-
Telecommunications and office equipment leases	36,244	46,598	9,338
	$170,118	$46,598	$9,338

From time to time, the Company is party to legal proceedings arising out of the normal course of business. The results of these litigations cannot be predicted with certainty, and management is of the opinion that the outcome of these types of proceedings is generally not determinable. Any loss resulting from these proceedings will be charged to operations in the period that a loss becomes probable.