

Covalon Announces Fiscal 2021 Q2 Results

MISSISSAUGA, ON, May 31, 2021 /CNW/ - Covalon Technologies Ltd. (the "Company" or "Covalon") (TSXV: COV) (OTCQX: CVALF), an advanced medical technologies company, today announced its fiscal 2021 second quarter results for the period ended March 31, 2021.

Brian Pedlar, Covalon's President and CEO said, "I am pleased to report that this past quarter represents the fourth consecutive quarter of improvement in both our operations and our financial performance despite having to deal with the challenges of COVID-19. We were profitable this past quarter with net income of \$421,724 or \$0.02 per share for the three months ended March 31, 2021. Our continued cost-cutting initiatives resulted in a 52% reduction in operating expenses compared to the same period in the prior year. I'm pleased that our efforts have led to a \$4.3 million year-over-year improvement in our net income and a \$1.4 million year-over-year improvement in Adjusted EBITDA⁽¹⁾ in Q2. We achieved these results while continuing to manage COVID-19 related impacts such as temporary delays in shipments of our collagen products in the United States and lower consumption of our products by hospitals due to delays in elective procedures.

"Our collagen business in the United States is stronger than it has ever been with significant increases in orders placed by our distribution customers and visibility into forecasted orders over the next twelve months. We are beginning to see signs of revenue recovery with our United States hospital customers and international distribution channels. At the same time, the Covalon team worked very hard to control operating expenses while working closely with our customers on new products we launched in 2020. This quarter, we engaged in approximately 10 medical coating customer development projects of various sizes with 3 medical product companies and we have a pipeline of new customer development projects. We are extremely excited about the future revenue potential of these new projects as well as the various projects currently underway with the previously announced major contract with one of the world's largest medical device companies.

"With cash-on-hand and amounts available under our HSBC operating bank line, we have sufficient future cash flow to support our operating needs.

"We are working hard to increase our profitability in our next fiscal quarter ending June 30, 2021, and for the remainder of fiscal 2021. Covalon is stronger both financially and operationally today and I am optimistic that our positive growth and improved financial performance will continue."

Outlook for 2021

We are seeing signs of improvement in product usage by our customer base in the United States and internationally even though the COVID-19 restrictions have not completely eased in many of the geographies in which we operate.

Gross margins are currently expected to remain similar to the first half of fiscal 2021 through the remainder of the fiscal year. Reduced operating expenses in the second half of fiscal 2021 are currently anticipated to be consistent with the past six months before including reductions from government subsidies related to COVID-19 relief programs. During the quarter, Covalon applied and was approved for \$1.1 million USD of funding under the United States Payroll Protection Plan and \$338,862 of funding under the Canadian Emergency Wage Subsidy Program. We anticipate a smaller positive impact from additional government subsidies in the fiscal third quarter.

The positive changes made to our operations have placed the Company in a position to continue to be profitable in fiscal 2021.

Strategic Review Process

As previously announced, in response to expressions of interest made by medical industry and private equity organizations, Covalon's Board of Directors formed a Special Committee and hired advisors to assist in undertaking a Strategic Review process, to ensure that available strategic alternatives to enhance value for our shareholders are being evaluated.

Mr. Amir Bloor, Chair of Covalon's Board of Directors and Chair of the Special Committee, said, "I am extremely pleased with the progress made by the Special Committee to date. Over the past several months, we have been carefully evaluating a number of expressions of interest and assessing the impact of these potential strategic alternatives on the overall value, future profitability and the growth prospects of Covalon. Each strategic alternative is being evaluated and assessed as to its impact following any strategic transactions involving one or more of our patented intellectual properties, technology platforms, commercialized medical product portfolio and global sales channels. This process has clearly validated that Covalon owns a number of valuable medical technologies that are of interest to the medical industry."

Mr. Bloor continued, "We are carefully deliberating on which course is in the best interests of the Company's shareholders. The entire Board of Directors, including the Company's major shareholders believe that Covalon is

significantly undervalued given its compelling combination of patented intellectual properties, technology platforms, commercialized medical product portfolio and global sales channels."

Fiscal 2021 Q2 and Year-to-Date Financial Results

Revenue for the three months ended March 31, 2021 increased 28% to \$6.7 million, compared to \$5.3 million in the prior year, due to increased collagen sales and increased in shipments to the Middle East. Revenue in the United States was \$5.3 million in Q2 fiscal 2021 compared to \$4.7 million in Q2 fiscal 2020. Revenue in the United States was up \$0.6 million predominantly as a result of increased collagen sales. We continued to experience temporary shipment delays from one of our contract manufacturers which impacted our collagen sales in Q2. The slowdown in the consumption of our products in hospitals resulting from COVID-19 related issues is anticipated to continue until hospitals and healthcare facilities resume the normal level of elective procedures.

Product revenue increased 38% to \$6.4 million, compared to \$4.6 million for the same period in the prior year. Product revenue increased in the United States by 23% or \$919,808 due to increased collagen sales, and in the Middle East by 522% to \$947,209. Development and consulting services revenue for the three-month period ended March 31, 2021 decreased by 47% to \$0.3 million, compared to \$0.6 million for the same period of the prior year, due to the timing of projects undertaken during the quarter.

Gross margin for the three months ended March 31, 2021 increased to 54% compared to 53% in the prior year. Gross margin is significantly influenced by source of revenue and the relative mix of collagen-based dressings, silicone-based dressings, medical coated devices, passive dressings, moisture barriers, repurposing existing inventory to meet customer orders and related service revenues in any given financial period.

Adjusted gross margin⁽¹⁾, which excludes inventory provisions and depreciation, was 55% for Q2 fiscal 2021, compared to 59% for the prior year. The slight decline is attributed to product mix.

Operational expenses decreased to \$3.1 million compared to \$6.5 million for the prior year's comparative period due to a reduction in headcount and discretionary spending across all departments. Main drivers of the decrease were reductions in compensation expenses across all departments, travel, and administrative expenses. The Company also recorded \$1 million of government subsidies netted out against the related expenses.

Net income was \$421,724 or \$0.02 per share, compared to a net loss of \$3.9 million or \$0.15 per share in Q2 fiscal 2020. Adjusted EBITDA⁽¹⁾ for Q2 fiscal 2021 was a loss of \$141,023 compared to a loss of \$1.5 million in the prior year's comparative period.

Revenue for the six months ended March 31, 2021 decreased 4% to \$12.7 million, compared to \$13.2 million the prior year. Gross margin for the period decreased to 57% compared to 58% for the same period the prior year. Net income was \$49,381 or \$nil per share, compared to a net loss of \$5.1 million or \$0.20 per share in fiscal 2020.

As consistent with prior quarters, the Company obtained a waiver from HSBC Bank Canada ("HSBC") related to the covenants that were not met as of the quarter end. Management is in continued discussions with HSBC regarding the Company's acquisition and operating banking credit facility and anticipates making changes to the banking agreement with HSBC in due course. A further update will be provided at the appropriate time.

(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.

Conference Call Scheduled

A conference call to discuss Covalon's Fiscal 2021 Q2 Financial Results will be held Monday, May 31st, 2021 at 9:00am EST. To participate in the call, please dial:

North American Toll-Free: 1.888.664.6392
Local (Toronto): 416.764.8659
Confirmation Number: 88451716

A recording of the call will be available by calling 1.888.390.0541 or 416.764.8677 and entering the encore replay enter code 451716# from May 31st, 2021, at 12:00pm EST to June 14th, 2021 at 11:59pm EST.

Statement of Operations

The following unaudited table presents Covalon's consolidated statements of operations for the three-month periods ended March 31, 2021 and 2020, and for the six months ended March 31, 2021 and 2020.

<i>(unaudited)</i>	Three months ended, March 31,		Six months ended March 31,	
	2021	2020	2021	2020

Revenue	\$6,376,359	\$4,626,805	\$11,762,431	\$11,801,448
Product				
Development and consulting services	315,145	599,893	856,895	1,333,021
Licensing and royalty fees	49,756	31,874	110,346	72,662
Total revenue	6,741,260	5,258,572	12,729,672	13,207,131
Cost of product sales	3,098,870	2,466,453	5,501,754	5,579,228
Gross profit before operating expenses	3,642,390	2,792,119	7,227,918	7,627,903
Operating expenses				
Operations	259,511	530,146	517,994	991,080
Research and development activities	327,948	223,346	545,176	448,651
Sales, marketing and agency fees	1,046,937	2,323,469	2,663,805	5,235,961
General and administrative	1,468,944	3,398,075	3,215,216	5,584,121
	3,103,340	6,475,036	6,942,191	12,259,813
Financing expenses	117,326	225,705	236,346	451,445
Net income (loss)	\$421,724	\$(3,908,622)	\$49,381	\$(5,083,355)
Other comprehensive income (loss)				
Foreign currency translation adjustment	(215,101)	1,770,263	(1,065,238)	1,359,110
Other comprehensive income (loss)	\$206,623	\$(2,128,359)	\$(1,015,857)	\$(3,724,245)
Basic earnings (loss) per share	\$0.02	\$(0.15)	\$0.00	\$(0.20)
Diluted earnings (loss) per share	\$0.02	\$(0.15)	\$0.00	\$(0.20)

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 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 months, and six months ended March 31, 2021 and 2020. 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 2021 months ended March 31st, 2021	Three 2020 months ended March 31st, 2020	Six 2021 months ended March 31st, 2021	Six 2020 months ended March 31st, 2020
Gross profit before operating expenses	3,642,390	2,792,119	7,227,918	7,627,903
Add: Depreciation and amortization	79,821	86,547	160,330	167,985
Add: Inventory provisions	187	214,809	6,340	500,534
Adjusted Gross Margin	3,722,398	3,093,475	7,394,588	8,296,422
Adjusted Gross Margin (%)	55%	59%	58%	63%

The table below provides a reconciliation of net loss under IFRS in the consolidated financial statements to Adjusted EBITDA for the three months, and six months ended March 31, 2021 and 2020. 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 fund 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 st , 2021		Six months ended March 31 st , 2021	
	2021	2020	2021	2020
Net income (loss)	421,724	(3,908,622)	49,381	(5,038,355)
Add: Interest expense	117,326	225,705	236,346	451,445
Add: Depreciation and amortization	282,803	282,276	573,503	575,654
Add: Stock based compensation	80,484	221,387	204,562	618,876
Less: Government subsidies	(1,043,547)	-	(1,346,001)	-
Add: Inventory provisions	187	214,809	6,340	500,534
Add: Accounts receivable write-off	-	1,420,002	-	1,420,002
Adjusted EBITDA	(141,023)	(1,544,443)	(275,869)	(1,516,844)

About Covalon

Covalon Technologies Ltd. is a researcher, developer, manufacturer, and marketer of patent-protected medical products that improve patient outcomes and save lives in the areas of advanced wound care, infection management and surgical procedures. 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 OTQX Market under the symbol CVALF. To learn more about Covalon, visit our website at www.covalon.com

Neither 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 contains 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" and statements that an event or result "may", "will", "should", "could" or "might" occur or be achieved and other similar expressions. These forward-looking statements involve risk and uncertainties, including the difficulty in predicting product approvals, acceptance of and demands for new products, the impact of the products and pricing strategies of competitors, delays in developing and launching new products, the regulatory environment, fluctuations in operating results, the impact and timing of COVID-19 on operating activities and market conditions, and other risks, any of which could cause results, performance, or achievements to differ materially from the results discussed or implied in the forward-looking statements. Many risks are inherent in the industry; others are more specific to the Company. Investors should consult the Company's ongoing quarterly filings for additional information on risks and uncertainties relating to these forward-looking statements. Investors should not place undue reliance on any forward-looking statements. The Company assumes no obligation to update or alter any forward-looking statements whether as a result of new information, further events or otherwise.

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For further information: To learn more about Covalon, please contact: Brian Pedlar, CEO, Covalon Technologies Ltd., Email: bpedlar@covalon.com, Phone: 905.568.8400 x 233, Toll free: 1.877.711.6055, Web site: www.covalon.com, Twitter: @covalon

<https://ir.covalon.com/2021-05-31-Covalon-Announces-Fiscal-2021-Q2-Results>