



CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS OF
Photon Control Inc.

For the three months ended March 31, 2020 and 2019

ACCURATE



RELIABLE



RESPONSIVE

PHOTON CONTROL INC.

Condensed Interim Consolidated Statements of Financial Position (Unaudited)

(In thousands of Canadian dollars)

	Note	March 31, 2020	December 31, 2019
Assets			
Current assets			
Cash and cash equivalents		\$ 41,214	\$ 33,400
Trade and other receivables		8,475	4,051
Income taxes receivable		-	714
Inventories		7,574	6,459
Prepaid expenses and deposits		593	575
Total current assets		57,856	45,199
Property and equipment	4	6,527	6,752
Intangible assets	5	3,214	3,386
Goodwill		849	849
Deferred tax assets		3,660	1,915
Total assets		\$ 72,106	\$ 58,101
Liabilities and Shareholders' Equity			
Current liabilities			
Accounts payable and accrued liabilities		\$ 6,630	\$ 4,318
Income taxes payable	6	5,035	-
Current portion of contingent consideration		1,534	1,419
Current portion of lease liabilities		276	272
Total current liabilities		13,475	6,009
Contingent consideration		1,313	1,473
Lease liabilities		1,170	1,241
Total liabilities		15,958	8,723
Shareholders' equity			
Share capital	7	29,366	29,366
Contributed surplus	7	4,953	4,838
Accumulated other comprehensive loss		(105)	(121)
Retained earnings		21,934	15,295
Total shareholders' equity		56,148	49,378
Total liabilities and shareholders' equity		\$ 72,106	\$ 58,101

Subsequent event (note 14)

See accompanying notes to the unaudited condensed interim consolidated financial statements

Approved on behalf of the Board:

"Nigel Hunton", Director

"Ronan McGrath", Director



PHOTON CONTROL INC.

Condensed Interim Consolidated Statements of Net Income and Comprehensive Income (Unaudited)

(In thousands of Canadian dollars, except number of shares and per share amounts)

	Note	Three months ended	
		March 31, 2020	March 31, 2019
Revenue	10	\$ 17,312	\$ 8,032
Cost of sales		6,724	3,802
Gross profit		10,588	4,230
Operating expenses			
General and administrative		2,155	1,525
Engineering	9	1,255	1,277
Sales and marketing		687	674
Total operating expenses		4,097	3,476
Operating income		6,491	754
Finance income		154	143
Accretion expense on contingent consideration		(122)	(143)
Change in fair value of contingent consideration		(88)	98
Foreign exchange gain (loss)		2,682	(586)
		2,626	(488)
Net income before taxes		9,117	266
Income taxes		2,478	196
Net income		6,639	70
Other comprehensive income: <i>(Item that may be reclassified to income in the future)</i>			
Unrealized gain from foreign exchange translation of subsidiary		16	50
Total comprehensive income		\$ 6,655	\$ 120
Basic and diluted earnings per share			
Weighted average common shares, basic		104,513,571	109,089,381
Weighted average common shares, diluted		104,925,738	109,568,962
Basic earnings per share		\$ 0.06	\$ 0.00
Diluted earnings per share		\$ 0.06	\$ 0.00

See accompanying notes to the unaudited condensed interim consolidated financial statements



PHOTON CONTROL INC.

Condensed Interim Consolidated Statements of Changes in Shareholders' Equity (Unaudited)

(In thousands of Canadian dollars)

	Note	Share capital	Contributed surplus	Accumulated other comprehensive loss	Retained earnings	Total
Balance, December 31, 2018		\$ 30,833	\$ 4,463	\$ (125)	\$ 18,494	\$ 53,665
Exercise of stock options		18	(1)	-	-	17
Repurchase of common shares for cancellation		(548)	-	-	(1,951)	(2,499)
Share-based payments	7 (e)	-	145	-	-	145
Adjustment on initial application of IFRS 16		-	-	-	(72)	(72)
Unrealized gain from foreign exchange translation of subsidiary		-	-	50	-	50
Net income for the period		-	-	-	70	70
Balance, March 31, 2019		30,303	4,607	(75)	16,541	51,376
Exercise of stock options		24	(17)	-	-	7
Settlement of restricted share units		88	(88)	-	-	-
Repurchase of common shares for cancellation		(1,049)	-	-	(3,547)	(4,596)
Share-based payments		-	336	-	-	336
Unrealized loss from foreign exchange translation of subsidiary		-	-	(46)	-	(46)
Net income for the period		-	-	-	2,301	2,301
Balance, December 31, 2019		29,366	4,838	(121)	15,295	49,378
Share-based payments	7 (e)	-	115	-	-	115
Unrealized gain from foreign exchange translation of subsidiary		-	-	16	-	16
Net income for the period		-	-	-	6,639	6,639
Balance, March 31, 2020		\$ 29,366	\$ 4,953	\$ (105)	\$ 21,934	\$ 56,148



PHOTON CONTROL INC.

Condensed Interim Consolidated Statements of Cash Flows (Unaudited)

(In thousands of Canadian dollars)

	Three months ended	
	March 31, 2020	March 31, 2019
Operating activities		
Net income for the period	\$ 6,639	\$ 70
Adjustments for		
Depreciation of property and equipment	365	393
Amortization of intangible assets	196	243
Share-based payments	115	145
Accretion expense on contingent consideration	122	143
Change in fair value of contingent consideration	88	(98)
Finance income	(154)	(143)
Income tax expense	2,478	196
Net change in non-cash working capital items		
Trade and other receivables	(4,424)	(837)
Inventories	(1,115)	639
Prepaid expenses and deposits	(18)	(140)
Accounts payable and accrued liabilities	2,312	320
Income taxes received (paid)	1,526	(3,393)
Interest paid	(28)	(50)
Net cash provided by (used in) operating activities	8,102	(2,512)
Financing activities		
Repurchase of common shares for cancellation	-	(2,499)
Payment of contingent consideration	(255)	(268)
Payment of lease liabilities	(67)	(63)
Proceeds from exercise of stock options	-	17
Net cash used in financing activities	(322)	(2,813)
Investing activities		
Purchase of property and equipment	(140)	(50)
Purchase of intangible assets	(24)	(11)
Interest received	182	193
Net cash provided by investing activities	18	132
Net increase (decrease) in cash and cash equivalents	7,798	(5,193)
Cash and cash equivalents, beginning of period	33,400	42,407
Effects of foreign exchange on cash and cash equivalents	16	50
Cash and cash equivalents, end of period	\$ 41,214	\$ 37,264

See accompanying notes to the unaudited condensed interim consolidated financial statements



1. Nature of business and continuing operations

Photon Control Inc. (“Photon Control” or the “Company”) is listed on the Toronto Stock Exchange (the “TSX”) under the trading symbol PHO, and is incorporated under the laws of British Columbia, Canada. The Company’s head office is located at 130-13500 Verdun Place, Richmond, BC, Canada, V6V 1V2. The address of the Company’s registered and records office is Suite 2600, Three Bentall Centre, 595 Burrard Street, PO Box 49314, Vancouver, British Columbia, Canada, V7X 1L3.

These condensed interim consolidated financial statements of the Company for the three months ended March 31, 2020 and 2019 comprise the statements of the Company and its subsidiaries. The financial statements were authorized for issue by the Board of Directors on May 5, 2020.

Photon Control designs, manufactures and distributes a wide range of optical sensors and systems to measure temperature and position for the semiconductor and other high technology industries.

2. Basis of presentation

Statement of compliance

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

These unaudited condensed interim consolidated financial statements have been prepared in accordance with International Accounting Standard (“IAS”) 34, Interim Financial Reporting, as issued by the International Accounting Standards Board (“IASB”). The condensed interim consolidated financial statements have been prepared on a basis consistent with and should be read in conjunction with the most recent annual consolidated financial statements for the years ended December 31, 2019 and 2018, which have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the IASB. Changes to significant accounting policies are described in note 3.

The results for the three months ended March 31, 2020 and 2019 may not be indicative of the results that may be expected for the full year or any other period.

Use of critical accounting judgments and estimates

The preparation of the condensed interim consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. The judgments, estimates and assumptions applied in the condensed interim consolidated financial statements, including key sources of estimation



uncertainty, were the same as those applied in the last annual consolidated financial statements for the years ended December 31, 2019 and 2018.

Valuation of contingent consideration

The Company recognizes the fair value of contingent consideration relating to acquisitions on the date the transaction closes. Contingent consideration is classified as either a liability or equity. Contingent consideration classified as a liability is carried at fair value with changes in fair value recorded in the condensed interim consolidated statements of net income and comprehensive income. Contingent consideration classified as equity is not remeasured subsequent to initial recognition.

Contingent consideration classified as a liability is measured at fair value based on management's best estimate of future royalties on revenues earned from defined products at the date of acquisition and is subsequently revalued at each financial reporting period. Changes in management's estimate of royalties could have a material impact on the valuation of the contingent consideration classified as a liability. The current portion of contingent consideration is based on the Company's estimate of the value that will be payable within twelve months.

Operating income

The Company defines operating income as earnings before finance income; accretion expense on contingent consideration; change in fair value of contingent consideration; foreign exchange gain (loss); and income taxes.

3. Significant accounting policies

The accounting policies applied in these condensed interim consolidated financial statements were the same as those applied in the most recent annual consolidated financial statements for the years ended December 31, 2019 and 2018.

Uncertain tax position

The Company's uncertain tax position consists of payments received from the Canadian tax authority related to foreign tax credits claimed on historical tax returns from 2013 to 2017. The Company evaluates the tax position for recognition by determining whether it is more likely than not that the position will be sustained on audit, including resolution of related appeals or litigation processes, if any. The amount of the liability to recognize is measured as the maximum amount which is more likely than not to be realized. The tax position is derecognized when it is no longer more likely than not that the position will be sustained on audit and the Company will adjust income tax expense accordingly in the period in which the position changes.

Future accounting pronouncements

The Company reviewed future accounting pronouncements and determined that there are no standards that are not yet effective and that would be expected to have a material impact on the entity in the current or future reporting period and on foreseeable future transactions.

Notes to Condensed Interim Consolidated Financial Statements (Unaudited)

(In thousands of Canadian dollars)

For the three months ended March 31, 2020 and 2019

4. Property and equipment

	Computers, office furniture and equipment	Laboratory equipment	Leasehold improvements	Production equipment	Right-of-use assets	Total
Cost						
Balance, January 1, 2019	\$ 1,387	\$ 1,505	\$ 4,041	\$ 2,552	\$ -	\$ 9,485
Adjustment on initial application of IFRS 16	-	-	-	-	1,683	1,683
Additions for the period	84	233	3	47	15	382
Balance, December 31, 2019	1,471	1,738	4,044	2,599	1,698	11,550
Additions for the period	30	96	14	-	-	140
Balance, March 31, 2020	\$ 1,501	\$ 1,834	\$ 4,058	\$ 2,599	\$ 1,698	\$ 11,690
Accumulated Depreciation						
Balance, January 1, 2019	\$ 535	\$ 605	\$ 828	\$ 1,220	\$ -	\$ 3,188
Depreciation for the period	182	205	535	410	278	1,610
Balance, December 31, 2019	717	810	1,363	1,630	278	4,798
Depreciation for the period	39	48	134	74	70	365
Balance, March 31, 2020	\$ 756	\$ 858	\$ 1,497	\$ 1,704	\$ 348	\$ 5,163
Net Book Value						
At December 31, 2019	\$ 754	\$ 928	\$ 2,681	\$ 969	\$ 1,420	\$ 6,752
At March 31, 2020	745	976	2,561	895	1,350	6,527

For the three months ended March 31, 2020, the Company recorded depreciation expense of \$155 and \$210 (2019 - \$184 and \$209) within cost of sales and operating expenses, respectively.



Notes to Condensed Interim Consolidated Financial Statements (Unaudited)

(In thousands of Canadian dollars)

For the three months ended March 31, 2020 and 2019

5. Intangible assets

	Acquired technologies	Computer software and other	Reacquired rights	Total
Cost				
Balance, January 1, 2019	\$ 4,439	\$ 542	\$ 2,000	\$ 6,981
Additions for the period	92	84	-	176
Balance, December 31, 2019	4,531	626	2,000	7,157
Additions for the period	13	11	-	24
Balance, March 31, 2020	\$ 4,544	\$ 637	\$ 2,000	\$ 7,181
Accumulated Amortization				
Balance, January 1, 2019	\$ 2,032	\$ 407	\$ 327	\$ 2,766
Amortization for the period	734	84	187	1,005
Balance, December 31, 2019	2,766	491	514	3,771
Amortization for the period	131	18	47	196
Balance, March 31, 2020	\$ 2,897	\$ 509	\$ 561	\$ 3,967
Net Book Value				
At December 31, 2019	\$ 1,765	\$ 135	\$ 1,486	\$ 3,386
At March 31, 2020	1,647	128	1,439	3,214

For the three months ended March 31, 2020, the Company recorded amortization expense of \$178 and \$18 (2019 - \$228 and \$15) within cost of sales and operating expenses, respectively.

6. Uncertain tax position

As at March 31, 2020, the Company accrued for an uncertain tax position of \$1,264 (December 31, 2019 - \$nil). Based on management's assessment, the uncertain tax position could decrease tax expense starting in the 2023 fiscal year, as tax years become statute barred for purposes of audit by the Canadian tax authority.

7. Share capital

(a) Authorized

Unlimited number of common shares without par value



Notes to Condensed Interim Consolidated Financial Statements (Unaudited)

(In thousands of Canadian dollars)

For the three months ended March 31, 2020 and 2019

(b) Issued and outstanding

	Number of common shares	Share capital	Contributed surplus
Balance as at December 31, 2018	109,867,913	\$ 30,833	\$ 4,463
Issued upon exercise of stock options	56,060	42	(18)
Issued upon settlement of restricted share units	79,598	88	(88)
Repurchase of common shares for cancellation	(5,490,000)	(1,597)	-
Share-based payments	-	-	481
Balance as at December 31, 2019	104,513,571	29,366	4,838
Share-based payments	-	-	115
Balance as at March 31, 2020	104,513,571	\$ 29,366	\$ 4,953

(c) Stock options

For the three months ended March 31, 2020, the Company granted 127,000 stock options to employees of the Company (2019 – 210,000). The weighted average fair value of stock options granted is \$0.38 (2019 - \$0.57). The options have a five-year term and vest over three years.

A summary of the activity in the Company's stock option plan is presented below:

	Number of options	Weighted average exercise price
Options outstanding, December 31, 2018	3,072,250	\$ 1.43
Granted	1,440,000	1.17
Exercised	(77,500)	0.62
Forfeited	(1,038,500)	1.65
Options outstanding, December 31, 2019	3,396,250	1.27
Granted	127,000	0.85
Forfeited	(71,250)	1.53
Options outstanding, March 31, 2020	3,452,000	\$ 1.25

During the three months ended March 31, 2020, the Company issued nil (2019 – 3,000) common shares for the cashless exercise of nil (2019 – 2,280) stock options.



Notes to Condensed Interim Consolidated Financial Statements (Unaudited)

(In thousands of Canadian dollars)

For the three months ended March 31, 2020 and 2019

As at March 31, 2020, the Company had the following stock options outstanding, entitling the holders to purchase one common share for each stock option held as follows:

	Options outstanding	Weighted average remaining term (years)	Options exercisable	Weighted average remaining term (years)
\$0.00 - 0.99	1,092,750	2.63	638,500	1.41
\$1.00 - 1.49	1,700,500	3.39	730,833	2.79
\$1.50 - 1.99	468,750	2.74	343,750	2.72
\$2.00 - 2.50	190,000	3.16	86,250	3.14
	3,452,000	3.05	1,799,333	2.30

The following weighted average assumptions were used in calculating the fair value of stock options granted during the period using the Black-Scholes model:

	Three months ended	
	March 31, 2020	March 31, 2019
Expected option life	5 years	5 years
Risk-free interest rate	1.25%	1.79%
Dividend yield	0%	0%
Volatility	51%	52%
Forfeiture	30%	30%

(d) Restricted share units ("RSUs")

RSU transactions are summarized as follows:

	Number of RSUs
RSU outstanding, December 31, 2018	129,000
Settled	(86,000)
RSU outstanding, December 31, 2019 and March 31, 2020	43,000

- (e) During the three months ended March 31, 2020, the Company recorded \$115 (2019 - \$145) of share-based payments relating to the fair value of stock options and RSUs vesting during the period with a corresponding increase to contributed surplus.



Notes to Condensed Interim Consolidated Financial Statements (Unaudited)

(In thousands of Canadian dollars)

For the three months ended March 31, 2020 and 2019

8. Related party transactions

The remuneration of key management for the three months ended March 31, 2020 and 2019 is as follows:

	Three months ended	
	March 31, 2020	March 31, 2019
Cash-based payments	\$ 542	\$ 190
Share-based payments	56	37
Total	\$ 598	\$ 227

Cash-based payments include salaries, bonuses, consulting fees, and other benefits.

9. Investment tax credits

For the three months ended March 31, 2020, the Company recognized investment tax credits of \$50 (2019 – \$nil) in the condensed interim consolidated statements of net income and comprehensive income.

10. Segmented information

(a) Revenue

The Company carries on business in the semiconductor industry and all sales and costs are made in this segment. Revenue is disaggregated by primary geographical market as follows:

	Three months ended	
	March 31, 2020	March 31, 2019
Primary geographical markets		
Asia	\$ 9,622	\$ 3,500
United States	7,690	4,532
	\$ 17,312	\$ 8,032

(b) Assets

The Company's property and equipment and intangible assets are located in Canada.

(c) Major customers

Sales to the Company's three largest customers accounted for 84% of the Company's total sales for the three months ended March 31, 2020 (2019 – 86%).



Notes to Condensed Interim Consolidated Financial Statements (Unaudited)

(In thousands of Canadian dollars)

For the three months ended March 31, 2020 and 2019

11. Financial instruments and fair values
Measurement categories, fair values and valuation methods

The Company's financial assets and liabilities, with the exception of contingent consideration liability, are measured using amortized costs which approximates fair value due to the nature of these instruments:

	March 31, 2020		December 31, 2019	
	Carrying value	Fair value	Carrying value	Fair value
Financial assets	\$ 49,689	\$ 49,689	\$ 37,451	\$ 37,451
Financial liabilities	6,630	6,630	4,318	4,318

Fair value hierarchy

The following financial assets and liabilities are measured at fair value on a recurring basis using quoted prices in active markets for identifiable assets (Level 1); significant other observable inputs (Level 2); and significant unobservable inputs (Level 3):

March 31, 2020	Carrying value	Level 1	Fair value	
			Level 2	Level 3
Financial liabilities				
Contingent consideration	\$ 2,847	\$ -	\$ -	\$ 2,847

December 31, 2019	Carrying value	Level 1	Fair value	
			Level 2	Level 3
Financial liabilities				
Contingent consideration	\$ 2,892	\$ -	\$ -	\$ 2,892

The Company used a discounted cash flow valuation technique in calculating the fair value of the contingent consideration. This valuation technique included inputs relating to estimated cash outflows under the arrangement and the use of a discount rate appropriate to the Company (20%). The fair value measurements are sensitive to the discount rate used in calculating the fair values. A 1% increase in the discount rate would reduce the fair value of the contingent consideration by \$19. During the three months ended March 31, 2020, the Company recorded accretion expense of \$122 (2019 - \$143) in relation to contingent consideration, reflecting the change in fair value of liability that is attributable to market risk.

Financial risk factors

The Company is exposed to a number of risks. These risks include credit risk, liquidity risk and market risk. The Company has established policies and procedures to manage these risks, with the objective of minimizing the adverse effects that changes in the variable underlying these risks could have on the Company's condensed interim consolidated financial statements.



Notes to Condensed Interim Consolidated Financial Statements (Unaudited)

(In thousands of Canadian dollars)

For the three months ended March 31, 2020 and 2019

Credit risk

The following table provides information regarding the aging of trade and other receivables as at March 31, 2020 and December 31, 2019:

	Neither past due nor impaired	Aged 1 - 30 days	Aged 31 - 60 days	Aged 61 - 90 days	Aged 90 + days
As at March 31, 2020	86%	13%	1%	0%	0%
As at December 31, 2019	93%	5%	2%	0%	0%

As at March 31, 2020, 14% (December 31, 2019 – 7%) of the Company’s trade and other receivables was past due. The definition of items that are past due was determined by reference to the Company’s standard credit terms, net of any provisions for losses. At March 31, 2020, the provision against trade and other receivables was \$nil (December 31, 2019 - \$nil). At each period end, the Company reviews the collectability of outstanding receivables. Specific accounts are only written off once all collection efforts have been explored or when legal bankruptcy has occurred. During the three months ended March 31, 2020, the Company did not incur any bad debt expense (2019 – \$nil).

The Company reviews financial assets past due on an ongoing basis with the objective of identifying potential matters that could delay the collection of funds at an early stage.

Liquidity risk

At March 31, 2020, the Company had a \$220 credit card facility (December 31, 2019 - \$220) with a Canadian Chartered bank.

Market risk
Foreign exchange risk

At March 31, 2020, the Company held net current monetary assets in USD equal to \$33,114 (December 31, 2019 - \$23,659). The Company estimates the impact of a 10% change in the Canadian dollar exchange rate on its net current monetary assets to be \$3,311 (December 31, 2019 - \$2,366).

Interest rate risk

The Company is exposed to interest rate risk by virtue of holding cash and cash equivalents. The Company’s objective in managing its cash is to provide sufficient funds to meet day-to-day requirements and placing excess cash in short-term deposits.



12. Expense by nature

	Three months ended	
	March 31, 2020	March 31, 2019
Wages and employee benefits	\$ 3,819	\$ 2,650
Depreciation of property and equipment	365	393
Amortization of intangible assets	196	243
Share-based payments	115	145
Cost of sales and other	6,326	3,847
Total	\$ 10,821	\$ 7,278

13. Capital risk management

The Company considers shareholders' equity as capital, the book value of which totaled \$56,148 at March 31, 2020 (December 31, 2019 - \$49,378).

14. Subsequent event

On April 3, 2020, the Company acquired certain assets of Micronor Inc., a supplier of fiber optic kinetic sensors based in Camarillo, California, USA, for cash consideration of \$844. The Company will account for the transaction as a business combination in accordance with IFRS 3. Management is in the process of gathering the relevant information that existed at the acquisition date to determine the fair value of the net identifiable assets acquired.