Photon Control Inc.

Management's Discussion and Analysis

For the three and six months ended June 30, 2018

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

DATED August 2, 2018

MANAGEMENT'S DISCUSSION AND ANALYSIS

For the three and six months ended June 30, 2018

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MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis ("MD&A") provides information for the three and six months ended June 30, 2018, and up to and including August 2, 2018. This MD&A is prepared in accordance with National Instrument 51-102, and should be read in conjunction with Photon Control Inc.'s (the "Company") condensed interim consolidated financial statements and accompanying notes for the three and six months ended June 30, 2018, and the consolidated financial statements and accompanying notes for the year ended December 31, 2017.

The financial data contained in this report and in the condensed interim consolidated financial statements and accompanying notes for the three and six months ended June 30, 2018 have been prepared in accordance with International Financial Reporting Standards ("IFRS") and are stated in Canadian dollars, unless otherwise noted.

In addition to the results reported in accordance with IFRS, the Company uses various non-GAAP financial measures, which are not recognized under IFRS, as supplemental indicators of the Company's operating performance and financial position. These non-GAAP financial measures are provided to enhance the user's understanding of the Company's historical and current financial performance and its prospects for the future. Management believes that these measures provide useful information in that they exclude amounts that are not indicative of the Company's core operating results and ongoing operations and provide a more consistent basis for comparison between quarters and years. Details of such non-GAAP financial measures and how they are derived are provided in conjunction with the discussion of the financial information reported.

The Company has reclassified certain balances to conform to the presentation adopted in the current year. In addition, there may be minor differences due to rounding of numbers.

Certain statements in this MD&A constitute forward-looking statements or forward-looking information within the meaning of applicable securities laws. You should carefully read "Cautionary Note Regarding Forward Looking Statements" in this MD&A and should not place undue reliance on any such forward-looking statements.

In this MD&A, unless the context otherwise requires, references to "the Company", "Photon Control", "we", "us" and "our" refer to Photon Control Inc. and its subsidiaries.

Additional information about the Company, including the Annual Information Form ("AIF)", is available at www.photon-control.com and www.sedar.com.

OVERVIEW

Photon Control designs, manufactures, and distributes a wide range of optical sensors and systems to measure temperature and position. These products are used by the world's largest Wafer Fabrication Equipment ("WFE") manufacturers and end users in the semiconductor and solid-state industries. Photon Control's high quality products provide industry leading accuracy, speed and quality in the most extreme conditions and are backed by a team of experts providing a variety of on-site and remote services including custom design, installation, training and support. Headquartered in an ISO 9001:2015 manufacturing facility in Vancouver, British Columbia, Canada, Photon Control is listed on the Toronto Stock Exchange (the "TSX"), trading under the symbol "PHO".

COMPANY HIGHLIGHTS

The following significant corporate and financial event have taken place during the three months ended June 30, 2018:

- On May 24, 2018, the Company's normal course issuer bid ("2018 NCIB") previously announced by the Company on January 2, 2018 was accepted by the TSX and would continue through the facilities of the TSX and other Canadian marketplaces; and,
- On May 25, 2018, the Company's common shares were listed and posted for trading on the Toronto Stock Exchange. The common shares were concurrently delisted from the TSX Venture Exchange.

PRODUCTS, DISTRIBUTION AND INDUSTRIES

Semiconductor Industry: Temperature and Position Sensors

The semiconductor capital equipment industry offers several significant and growing applications for our technology and is the primary source of revenue and growth for our business. The Company designs and produces precision temperature and position sensors used by semiconductor WFE manufacturers. The manufacturing of silicon wafers for semiconductors involves a multitude of complex processes; monitoring and maintaining correct position and temperature is critical to this process in optimizing product yield. Fiber optic sensors are both electromagnetic and radio frequency signal immune allowing them to provide highly accurate results in harsh environments encountered in semiconductor manufacturing processes, such as etch and deposition. Photon Control's fiber optic temperature and position sensors are manufactured according to "Copy Exact" standards in its ISO-certified facility.

The need for increasing geometric granularity in the semiconductor manufacturing process has increased the number of measurement points required as well as the need for highly accurate measurements provided by fiber optic sensors. In addition, as semiconductor capital equipment has gone from 28 nm to 10 nm linewidth and narrower for leading edge applications over the last 10 years, the number of required measurement points has increased more than four-fold. Similarly, the proliferation of 3D and advanced logic chip designs are becoming more common; and thus, increasing significantly as a percentage of total chips manufactured. These factors have driven and are expected to continue to drive demand for our products.

SALES, MARKETING AND DISTRIBUTION

Photon Control sells its products globally with sales to original equipment manufacturers ("OEMs") primarily in the United States who in turn sell their products to end users in the United States, Asia and Europe. We also sell through a network of distributors in Asia who sells our products to OEMs in their home markets.

MARKET LANDSCAPE

Semiconductors have revolutionized all aspects of our economy and lives. As a building block of technology, semiconductors will continue to enable innovation and transform industries. With the accelerating pace of new chip capabilities and more applications, chip makers are expected to continue to increase production to meet this growing market. Simultaneously, semiconductor companies are regularly transitioning to new design and production technologies. Many of these technologies increase the number of process steps requiring more overall WFE production capacity and greater precision in measurement. The combination of overall semiconductor growth and increased demand for equipment is expected to in turn drive growth for the Company. Photon Control's primary vertical in this market is in etch, one of many manufacturing steps in the process of creating semiconductors. The Company works in and is developing business plans to meet demand in several other process steps including expanding its revenues from the deposition step as well as extending its product reach into other processes, including processes involved in the manufacturing of Organic Light-Emitting Diode ("OLED") panels and other sophisticated display panel technologies, the fabrication of which is similar to the process for semiconductors.

SELECTED FINANCIAL INFORMATION

The following table highlights key financial information for the three and six months ended June 30, 2018 as compared to the prior comparable periods:

	Three months ended				Six months ended			
	June 30,		Variance		June 30,		Variance	
	2018	2017	($)	(%)	2018	2017	($)	(%)
Revenue	$ 14,565	$ 8,877	$ 5,688	64%	$ 28,419	$ 20,756	$ 7,663	37%
Cost of sales	6,277	4,208	2,069	49%	12,252	8,971	3,281	37%
Gross profit	8,288	4,669	3,619	78%	16,167	11,785	4,382	37%
Gross profit %	*56.9%*	*52.6%*			*56.9%*	*56.8%*		
Operating expenses								
General and administrative	2,199	3,217	(1,018)	-32%	3,955	6,839	(2,884)	-42%
Engineering	886	823	63	8%	1,742	1,628	114	7%
Sales and marketing	681	282	399	141%	1,251	499	752	151%
Total operating expenses	3,766	4,322	(556)	-13%	6,948	8,966	(2,018)	-23%
Operating income	4,522	347	4,175	1203%	9,219	2,819	6,400	227%
Finance income	60	101	(41)	-41%	144	131	13	10%
Accretion expense on contingent consideration	(197)	(63)	(134)	213%	(383)	(63)	(320)	508%
Change in fair value of contingent consideration	(91)	-	(91)	-100%	(902)	-	(902)	-100%
Gain on sale of assets	-	-	-	0%	166	-	166	100%
Foreign exchange gain (loss)	659	(778)	1,437	-185%	1,718	(918)	2,636	-287%
	431	(740)	1,171	-158%	743	(850)	1,593	-187%
Net income (loss) before tax	4,953	(393)	5,346	-1360%	9,962	1,969	7,993	406%
Income tax (recovery)	1,100	(62)	1,162	-1874%	3,227	602	2,625	436%
Net income (loss)	3,853	(331)	4,184	-1264%	6,735	1,367	5,368	393%
Other comprehensive loss on foreign exchange translation of subsidiary	(23)	-	(23)	-100%	(33)	-	(33)	-100%
Total comprehensive income (loss)	$ 3,830	$ (331)	$ 4,161	-1257%	$ 6,702	$ 1,367	$ 5,335	390%
Basic earnings (loss) per share	$ 0.03	$ -	$ 0.03	100%	$ 0.06	$ 0.01	$ 0.05	500%
Diluted earnings (loss) per share	$ 0.03	$ -	$ 0.03	100%	$ 0.06	$ 0.01	$ 0.05	500%

Operating income is a non-GAAP measure and is therefore not universally defined. The Company defines operating income as earnings before finance income, accretion expense on contingent consideration, change in fair value of contingent consideration, gain on sale of assets, foreign exchange gain (loss) and income tax (recovery).

(In Canadian dollars, amounts in thousands except number of shares and per share amounts) 4

The following table highlights key financial information as at June 30, 2018 and December 31, 2017:

Financial Position	June 30, 2018	December 31, 2017	Variance ($)	Variance (%)
Cash	$ 40,794	$ 34,345	$ 6,449	19%
Total assets	66,394	55,549	10,845	20%
Total liabilities	12,174	8,889	3,285	37%
Total shareholders' equity	54,220	46,660	7,560	16%

The following table provides the details of our EBITDA for the three and six months ended June 30, 2018 and 2017:

	Three months ended June 30,		Six months ended June 30,	
	2018	2017	2018	2017
Net income (loss) for the period	$ 3,853	$ (331)	$ 6,735	$ 1,367
Add (deduct)				
Finance income	(60)	(101)	(144)	(131)
Accretion expense on contingent consideration	197	63	383	63
Income tax (recovery)	1,100	(62)	3,227	602
Depreciation of property and equipment	365	161	706	227
Amortization of intangible assets	328	9	651	16
Foreign exchange (gain) loss	(659)	778	(1,718)	918
Corporate Changes	-	945	-	2,953
Photon R&D settlement	-	594	-	951
Relocation costs	-	411	-	411
EBITDA[1] for the period	**$ 5,124**	**$ 2,467**	**$ 9,840**	**$ 7,377**

(1) EBITDA is a non-GAAP measure and is therefore not universally defined. The Company defines EBITDA as earnings (loss) before finance income, accretion expense, income tax (recovery), depreciation, amortization and foreign exchange (gain) loss. For the comparative period, EBITDA was further refined to remove the effect of non-recurring items.

The Company considers the following items as non-recurring:

- Corporate Changes – the Company made significant changes to its Board of Directors, management team and business structure in 2017. Additionally, the Company restructured its Oil and Gas business model from direct sales to a distributor model in 2017 before its eventual sale in 2018. One-time expenditures resulting from these changes include legal, consulting and recruiting fees, as well as severance and related payments.
- Photon R&D settlement – the Company took actions following the unauthorized transfer of $4,500 to Photon Control R&D Ltd. on June 3, 2016 (the "Unauthorized Transfer"), resulting in a settlement agreement on April 14, 2017 ("Settlement Agreement"). One-time expenditures related to this matter include settlement costs, legal, consulting and advisory fees.
- Relocation costs – the Company completed the fit-out of and relocation to a new manufacturing facility in 2017. One-time expenditures include third party services, labour costs and the cost of dismantling and restoring the vacated premises.

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OVERALL PERFORMANCE AND DISCUSSION OF OPERATIONS

Revenue

The following table provides a summary of our revenues by segment:

	Three months ended June 30, 2018	Three months ended June 30, 2017	Variance ($)	Variance (%)	Six months ended June 30, 2018	Six months ended June 30, 2017	Variance ($)	Variance (%)
Semiconductor	$ 14,525	$ 8,741	$ 5,784	66%	$ 28,344	$ 20,562	$ 7,782	38%
Other	40	136	(96)	-71%	75	194	(119)	-61%
Total	**$ 14,565**	**$ 8,877**	**$ 5,688**	**64%**	**$ 28,419**	**$ 20,756**	**$ 7,663**	**37%**

Semiconductor revenues for the three and six months ended June 30, 2018 grew 66% and 38% over the prior comparable periods, respectively. The increase is attributable to the Company capturing an increased share of its customers' spend and continued robust market conditions persisting in the semiconductor industry. Other revenues decreased due to the sale of the Company's Oil and Gas product line earlier in 2018 and an increased focus on semiconductor revenues.

The following table provides a summary of our revenues by territory:

	Three months ended June 30, 2018	Three months ended June 30, 2017	Variance ($)	Variance (%)	Six months ended June 30, 2018	Six months ended June 30, 2017	Variance ($)	Variance (%)
United States	$ 8,370	$ 5,437	$ 2,933	54%	$ 17,344	$ 12,683	$ 4,661	37%
Asia	6,183	3,374	2,809	83%	11,036	7,973	3,063	38%
Rest of world	12	66	(54)	-82%	39	100	(61)	-61%
Total	**$ 14,565**	**$ 8,877**	**$ 5,688**	**64%**	**$ 28,419**	**$ 20,756**	**$ 7,663**	**37%**

For the three and six months ended June 30, 2018, the Company's revenues generated from customers located in the United States and Asia increased over the prior comparable periods due to the overall growth in the semiconductor segment. There were nominal fluctuations in revenues earned from rest of world compared to the same year-ago periods.

Gross Profit

Gross profit for the three and six months ended June 30, 2018 increased over the prior comparable periods as a result of higher overall revenues and increased gross margins.

Gross margin increased to 56.9% for the three and six months ended June 30, 2018 compared to 52.6% and 56.8% in the prior comparable periods, respectively, due to favourable product and customer mix. The Company also benefitted from greater economies of scale by leveraging its previous investment in its manufacturing facility to support higher unit volumes.

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Operating Expenses

	Three months ended June 30, 2018	Three months ended June 30, 2017	Variance ($)	Variance (%)	Six months ended June 30, 2018	Six months ended June 30, 2017	Variance ($)	Variance (%)
Operating expenses, as reported	$ 3,766	$ 4,322	$ (556)	-13%	$ 6,948	$ 8,966	$ (2,018)	-23%
Deduct								
Depreciation of property and equipment	(174)	(59)	(115)	195%	(341)	(74)	(267)	361%
Amortization of intangible assets	(24)	(9)	(15)	167%	(42)	(16)	(26)	163%
Share-based payments	(209)	(366)	157	-43%	(524)	(585)	61	-10%
Corporate Changes	-	(826)	826	-100%	-	(2,834)	2,834	-100%
Photon R&D settlement	-	(594)	594	-100%	-	(951)	951	-100%
Relocation costs	-	(411)	411	-100%	-	(411)	411	-100%
Operating expenses, adjusted	**$ 3,359**	**$ 2,057**	**$ 1,302**	**63%**	**$ 6,041**	**$ 4,095**	**$ 1,946**	**48%**

Total operating expenses for the three and six months ended June 30, 2018 were $3,766 and $6,948 compared to $4,322 and $8,966 in the prior comparable periods, respectively. When adjusted for non-cash charges and non-recurring items such as Corporate Changes, Photon R&D settlement and Relocation costs incurred in 2017, operating expenses increased to $3,359 and $6,041 compared to $2,057 and $4,095 in the prior comparable periods, respectively; the increase is attributable to an increased labour workforce to support the increased revenue levels, development costs for new products, and one-time costs associated with the graduation to the Toronto Stock Exchange.

General and Administrative

	Three months ended June 30, 2018	Three months ended June 30, 2017	Variance ($)	Variance (%)	Six months ended June 30, 2018	Six months ended June 30, 2017	Variance ($)	Variance (%)
General and administrative expenses, as reported	$ 2,199	$ 3,217	$ (1,018)	-32%	$ 3,955	$ 6,839	$ (2,884)	-42%
Deduct								
Depreciation of property and equipment	(174)	(59)	(115)	195%	(341)	(74)	(267)	361%
Amortization of intangible assets	(19)	(7)	(12)	171%	(37)	(12)	(25)	208%
Share-based payments	(192)	(325)	133	-41%	(437)	(535)	98	-18%
Corporate Changes	-	(730)	730	-100%	-	(2,738)	2,738	-100%
Photon R&D settlement	-	(594)	594	-100%	-	(951)	951	-100%
Relocation costs	-	(411)	411	-100%	-	(411)	411	-100%
General and administrative, adjusted	**$ 1,814**	**$ 1,091**	**$ 723**	**66%**	**$ 3,140**	**$ 2,118**	**$ 1,022**	**48%**

General and administrative expenses totalled $2,199 and $3,955 for the quarter and year-to-date compared to $3,217 and $6,839 in the prior comparable periods, respectively. When adjusted for non-cash charges and non-recurring items as described elsewhere, adjusted cash expenses totalled $1,814 and $3,140 for the three and six months ended June 30, 2018 compared to $1,091 and $2,118 in the prior comparable periods, respectively. The increase in adjusted cash expenses for the quarter and year-to-date were due to the effect of increased workforce and related costs throughout the preceding 12 months, and professional and listing fees incurred for the Company's graduation to the Toronto Stock Exchange.

Engineering

Engineering totalled $886 and $1,742 for the quarter and year-to-date compared to $823 and $1,628 in the prior comparable periods, respectively. Prior to the Settlement Agreement, the Company outsourced its engineering activities to Photon R&D. On April 14, 2017, following the acquisition of Photon R&D, the Company onboarded an engineering team and the variance relates to the change in approach and investments made to new product development to support future growth.

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Sales and Marketing

Sales and marketing expenses were $681 and $1,251 for the quarter and year-to-date compared to $282 and $499 in the prior comparable periods, respectively. The increase in sales and marketing resulted from the increased staff levels to support current and future growth of our revenues.

Accretion Expense on Contingent Consideration

Contingent consideration relates to the acquisition of certain assets of Photon Control R&D Ltd. in 2017. It is determined using a discount model applied to royalties on revenues earned from defined products from January 1, 2017 to December 31, 2021. Accretion expense represents the increase of contingent consideration through the discount model resulting from the passage of time.

Change in Fair Value of Contingent Consideration

Change in fair value of contingent consideration totalled $91 and $902 for the quarter and year-to-date. The increases resulted from an upward revision in management's estimate of the potential total amount of contingent consideration compared to the estimate made at the end of the preceding period.

Gain on Sale of Assets

On February 15, 2018, the Company sold all of the assets and rights associated with its Optical Flow Meter product to King's Energy Inc. ("King's") for minimum gross proceeds of $350. The gross proceeds include immediate cash consideration of $200 and contingent consideration of at least $150, and is based on a percentage of revenues earned by King's for a five year period commencing from the Transaction Date.

The carrying value of the disposed assets was $184, resulting in a gain on sale of assets totaling $166 for the quarter.

Foreign Exchange Gain/Loss

The Company is subject to foreign exchange risk as its products are priced in United States dollars ("USD"), while the majority of its expenses and assets are denominated in Canadian dollars. The Company does have a partial "natural hedge" against foreign exchange risk, as some of its component parts and accounts payable are priced and or valued in US dollars. The foreign exchange gain for the three and six months ended June 30, 2018 were due to the strengthening of the US dollar relative to the Canadian dollar throughout the period.

Net Income (Loss) Before Tax

Net income (loss) before tax for the quarter and year-to-date increased to $4,953 and $9,962 compared to ($393) and $1,969 in the comparable periods in 2017 due to strong market conditions in the semiconductor industry and the completion of non-recurring activities in 2017, as described elsewhere.

Income Tax (Recovery)

Income tax for the three and six months ended June 30, 2018 were $1,100 and $3,227 compared to ($62) and $602 in the comparable period in 2017.

EBITDA

EBITDA is defined as earnings before finance income, accretion expense, income tax (recovery), depreciation, amortization and foreign exchange (gain) loss. For the comparative period, EBITDA was further refined to remove the effect of non-recurring items, including Corporate Changes, Photon R&D settlement, and Relocation costs as described elsewhere.

EBITDA for the three and six months ended June 30, 2018 improved to $5,124 and $9,840 compared to $2,467 and $7,377 in the comparable period in 2017 due to continued growth in the semiconductor segment.

Order Backlog

Order backlog was $19,500 on June 30, 2018, an increase from $18,300 at December 31, 2017 and $11,900 at June 30, 2017. Order backlog represents the unfulfilled value of sales orders received and scheduled for fulfillment in the remaining rolling 6-month period. The increase in the order backlog reflects the continued demand growth occurring in the semiconductor industry and early results from investments made in sales, marketing and engineering.

SUMMARY OF QUARTERLY RESULTS

The global semiconductor industry is fast paced, competitive and constantly innovating to increase processing speed and power. The ability to anticipate these technological changes and innovate to meet them without compromising quality, is a key competitive advantage in this market. As a supplier of componentry to semiconductor WFE manufacturers, Photon Control’s key strengths include our rapid prototyping capabilities, our ISO certified production facility and CE methods, and our ability to manufacture to our customer’s exacting standards with our highly trained workforce. In addition to our high quality manufacturing strengths, our products include unique proprietary characteristics which both differentiate our products and allow us to outperform competitive offerings.

The following table provides a summary of the Company’s financial results for the eight most recently completed quarters.

	Q3 2016	Q4 2016	Q1 2017	Q2 2017	Q3 2017	Q4 2017	Q1 2018	Q2 2018
Revenue	$ 8,733	$ 9,011	$ 11,879	$ 8,877	$ 12,024	$ 11,033	$ 13,854	$ 14,565
Gross profit	$ 4,569	$ 4,285	$ 7,116	$ 4,669	$ 6,551	$ 4,955	$ 7,879	$ 8,288
Gross margin %	52%	48%	60%	53%	54%	45%	57%	57%
Net income (loss)	$ 2,181	$ 1,351	$ 1,698	$ (331)	$ 1,672	$ 2,653	$ 2,882	$ 3,853
Basic EPS (loss)	$ 0.02	$ 0.01	$ 0.02	$ (0.00)	$ 0.02	$ 0.02	$ 0.03	$ 0.03
Diluted EPS (loss)	$ 0.02	$ 0.01	$ 0.02	$ (0.00)	$ 0.01	$ 0.02	$ 0.03	$ 0.03
Cash	$ 31,139	$ 32,508	$ 32,112	$ 25,053	$ 26,966	$ 34,345	$ 33,367	$ 40,794

The Company has achieved generally consistent growth in its revenue over the past eight quarters as its primary segment, the semiconductor industry, has grown, and the Company has solidified its position as a supplier of choice for its customers. The Company’s net income for quarters in 2016 and 2017 were negatively affected by the non-recurring items as described elsewhere.

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LIQUIDITY AND CAPITAL RESOURCES

The following table provides a summary of the Company's working capital as at June 30, 2018 and December 31, 2017:

	June 30, 2018	December 31, 2017	Variance
Cash	$ 40,794	$ 34,345	$ 6,449
Trade and other receivables	7,050	3,393	3,657
Inventories	5,568	4,052	1,516
Prepaid expenses and deposits	457	279	178
Assets held for sale	-	184	(184)
Total current assets	**53,869**	**42,253**	**11,616**
Accounts payable and accrued liabilities	5,371	4,003	1,368
Income taxes payable	1,987	579	1,408
Current portion of contingent consideration	1,613	1,321	292
Total current liabilities	**8,971**	**5,903**	**3,068**
Working capital	**$ 44,898**	**$ 36,350**	**$ 8,548**

Management believes the Company will be able to continue to meet its liabilities and commitments as they become due and will generate sufficient amounts of cash from the continued manufacturing and distribution of existing products and the commercialization of new products. This cash will be used to maintain capacity, meet planned growth and development activities. The Company continues to monitor all expenditures and implement cash management strategies to ensure that it has adequate cash reserves to fund identified expenditure requirements.

Capital Management

The Company considers shareholders' equity as capital, the book value of which totaled $54,220 at June 30, 2018 (December 31, 2017 - $46,660).

The Company manages its capital structure to safeguard its ability to operate as a going concern, to provide sufficient resources to meet day-to-day operating requirements, to allow it to enhance existing product offerings as well as develop new ones, and to have the financial ability to expand the size of its operations by taking on new customers. In managing its capital structure, the Company takes into consideration various factors, including the growth of its business and related infrastructure and the upfront cost of taking on new clients.

The Company's officers and senior management are responsible for managing the Company's capital and do so through regular meetings and regular review of financial information. The Company's Board of Directors is responsible for overseeing this process.

Working Capital

The increase of working capital over December 31, 2017 was the result of its profitable operating performance, and significant capital expenditures in 2017 which did not reoccur during the six months ended June 30, 2018.

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Cash

At June 30, 2018, the Company held cash of $40,794 compared to $34,345 as at December 31, 2017, with the increase attributable to its strong operating performance.

Trade and Other Receivables

Trade and other receivables of $7,050 increased from $3,393 as at December 31, 2017 due to the effect of an early payment arrangement with a customer ending on December 31, 2017.

Inventories

Inventories as at June 30, 2018 totaled $5,568 compared to $4,052 as at December 31, 2017 with the increase occurring in anticipation of future demand from our major customers

The Company follows a "Copy Exact" standard in providing its products to its customers, and is required to maintain adequate inventory on hand to fill purchase orders from its customers. As a result, and due to the fact that the timing and quantum of such purchases orders cannot be forecasted with complete accuracy, the Company must also have available an adequate quantity of inventories on hand. In addition, it may have to add contract staff to its production team to meet large orders. These variances in demand and revenue can have a short-term effect on the Company's liquidity from time to time.

Accounts Payable and Accrued Liabilities

As at June 30, 2018, the Company's accounts payable and accrued liabilities, which fall due for payment within 12 months of the balance sheet date, were $5,371, compared to $4,003 as at December 31, 2017; the increase is the result of trade payables for inventory purchases to support current and future revenue opportunities.

OFF BALANCE SHEET ARRANGEMENTS

The Company had no off-balance sheet arrangements for the three and six months ended June 30, 2018 and 2017.

COMMITMENTS

Under operating lease agreements for office premises, the Company is required to make future annual minimum lease payments as follows:

2018	$	167
2019		334
2020		297
2021		285
2022 and onwards		854
Total	**$**	**1,937**

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RELATED PARTY TRANSACTIONS

The remuneration of key management for the three and six months ended June 30, 2018 and 2017 is as follows:

	Three months ended		Six months ended	
	June 30, 2018	June 30, 2017	June 30, 2018	June 30, 2017
Cash-based payments	**$ 452**	$ 613	**$ 865**	$ 1,104
Share-based payments	**201**	310	**396**	504
Total	**$ 653**	$ 923	**$ 1,261**	$ 1,608

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

FINANCIAL INSTRUMENTS AND FAIR VALUES

The Company's financial assets and liabilities are measured using amortized costs which approximates fair value due to the nature of these instruments.

	June 30, 2018		December 31, 2017	
	Carrying Value	Fair Value	Carrying Value	Fair Value
Financial assets	**$ 47,844**	**$ 47,844**	$ 37,791	$ 37,791
Financial liabilities	**5,371**	**5,371**	4,003	4,003

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):

			Fair Value	
June 30, 2018	**Carrying Value**	**Level 1**	**Level 2**	**Level 3**
Financial liabilities				
Contingent consideration	$ 4,514	$ -	$ -	$ 4,514

			Fair Value	
December 31, 2017	**Carrying Value**	**Level 1**	**Level 2**	**Level 3**
Financial liabilities				
Contingent consideration	$ 4,005	$ -	$ -	$ 4,005

The Company has 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 $55. During the three and six months ended June 30, 2018, the Company recorded accretion expense of $197 and $383 (2017 - $63) in relation to contingent consideration, respectively, reflecting the change in fair value of liability that is attributable to credit 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 consolidated financial statements.

(In Canadian dollars, amounts in thousands except number of shares and per share amounts) 12

Credit risk

The following table provides information regarding the aging of trade and other receivables as at June 30, 2018 and December 31, 2017:

	Neither past due nor impaired	Aged 1 - 30 days	Aged 31 - 60 days	Aged 61 - 90 days	Aged 90 + days
As at June 30, 2018	**93%**	**4%**	**2%**	**0%**	**1%**
As At December 31, 2017	91%	10%	0%	-1%	0%

As at June 30, 2018, 7% (December 31, 2017 – 9%) 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 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 and six months ended June 30, 2018, the Company incurred $84 and $98 of bad debts expense (2017 - $21 and $24), respectively.

Liquidity risk

As at June 30, 2018 and December 31, 2017, the Company had a $80 credit card facility with a Canadian Chartered bank.

Market risk

Foreign exchange risk

At June 30, 2018, the Company held net current monetary assets in USD equal to $26,223 (December 31, 2017 - $34,966). The Company estimates the impact of a 10% change in the Canadian dollar exchange rate on its net current monetary assets to be $2,622 (December 31, 2017 - $3,497).

Interest rate risk

The Company is exposed to interest rate risk by virtue of holding cash.

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. Information about critical judgments in applying accounting policies that have the most significant effect on the amounts recognized in the condensed interim consolidated financial statements is as follows:

(a) Valuation of contingent consideration

The Company recognizes the fair value of contingent consideration relating to acquisitions on the date the transaction closes. Contingent consideration classified as a liability is carried at fair value with changes in fair value flowing through 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 the probability of the attainment of specified revenue targets at the date of acquisition and is subsequently revalued at each financial reporting period. Management's estimate of the probability of the attainment of specified revenue targets takes into account management's evaluation of the revenue forecast for the respective acquired businesses and the risks thereon. Changes in management's estimate of the probability of achieving the specified target 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.

(In Canadian dollars, amounts in thousands except number of shares and per share amounts) 13

OUTSTANDING SHARE DATA

As at June 30, 2018, the Company had 111,314,968 common shares issued and outstanding. As at August 1, 2018, the Company had 111,389,467 common shares were issued and outstanding.

As at June 30, 2018, the Company had 3,450,750 stock options outstanding entitling the holders to purchase one common share for each option held. As at August 1, 2018, the Company had 3,364,750 stock options outstanding.

As at June 30, 2018, the Company had restricted share units outstanding for 262,000 common shares. As at August 1, 2018, the Company had restricted share units outstanding for 219,000 common shares.

RISKS AND UNCERTAINTIES

Our business is subject to significant risks and uncertainties and past performance is no guarantee of future performance. The risks and uncertainties in the Company's most recently filed AIF, which is available on the Canadian System for Electronic Document Analysis and Retrieval website ("SEDAR" (www.sedar.com) are those that we currently believe to be material, and do not represent all of the risks that we face. Additional risks and uncertainties, not presently known to us, may become material in the future or those risks that we currently believe to be immaterial may become material in the future. If any of the following risks actually occur, alone or in combination, our business, financial condition and results of operations, as well as the market price of our common shares, could be materially adversely affected.

CAUTIONARY NOTE REGARDING FORWARD LOOKING STATEMENTS

This MD&A contains certain statements and information that are not based on historical facts and constitute forward-looking statements or forward-looking information within the meaning of Canadian securities laws (collectively, "forward-looking statements"), including our business outlook for the short and longer term and statements regarding our strategy, plans and future operating performance. Forward-looking statements are provided to help you understand our views of our short and longer-term plans, expectations and prospects. We caution you that forward-looking statements may not be appropriate for other purposes.

Any statements that express or involve discussions with respect to predictions, expectations, beliefs, plans, projections, objectives, assumptions or future events or performance (often, but not always, identified by words or phrases such as "expects", "is expected", "anticipates", "believes", "plans", "projects", "estimates", "assumes", "intends", "strategy", "goals", "objectives", "potential", "possible" or variations thereof or stating that certain actions, events, conditions or results "may", "could", "would", "should", "might" or "will" be taken, occur or be achieved, or the negative of any of these terms and similar expressions) are not statements of historical fact and may be forward-looking statements. Forward-looking statements are not promises or guarantees of future performance; they represent our current views and may change significantly. Forward-looking statements are based on a number of material assumptions, including, but not limited to, those listed below, which could prove to be significantly incorrect:

- our ability to develop, manufacture and sell new products that meet the needs of our customers and gain commercial acceptance;
- our ability to continue to sell our products in line with quantity, price and delivery expectations;
- our ability to attract new business;
- our production being adversely affected by development, operating and regulatory risks;
- our ability to successfully complete new purchase orders along the timelines expected;
- continued and future demand for the Company's products;
- continued sales to the Company's major customers;
- continued financial health of the semiconductor industry;
- our ability to continue and further enhance revenue diversification and open new market opportunities; and
- our expectations regarding market risk, including interest rate changes, tax changes and foreign currency fluctuations.

Forward-looking statements involve known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company to be materially different from any results, performance or achievements expressed or implied by the forward-looking statements. Such uncertainties and factors include, among others:

- risks associated with compliance with regulatory bodies' quality system regulations;
- risks associated with the Company's ability to retain major customers;
- risks associated with shifts in demand for the Company's products and the Company's ability to expand its manufacturing capacity;
- risks associated with continuous technological change, evolving industry standards, shifting customer needs and new product introductions and enhancements;
- uncertainty relating to the timing of product development and commercial launch;
- risks associated with competition;
- uncertainty relating to operating results;
- risks associated with product liability claims;
- risks related to product pricing;
- risks associated with the Company's intellectual property;
- uncertainty related to potential legal proceedings involving the Company;
- operational risks associated with manufacturing;
- uncertainty relating to general economic conditions and the cyclical nature of the semiconductor industry;

- uncertainty relating to fluctuations in currency exchange rates, particularly between the Canadian and U.S. dollars;
- uncertainty related to international operations, including additional development projects and other business opportunities;
- risks related to the volatility of the trading price and volume of the Company's common shares;
- risks associated with attracting and retaining qualified personnel;
- risks associated with operating in jurisdictions with complex and changing tax laws;
- risks related to managing and storing proprietary information and sensitive or confidential data relating to the Company's operations electronically; and
- risks associated with compliance with various federal, provincial, local and international laws governing the environment.

This list is not exhaustive of the factors that may affect any of our forward-looking statements. Forward looking statements are statements about the future and are inherently uncertain, and our actual achievements or other future events or conditions may differ materially from those reflected in the forward-looking statements due to a variety of risks, uncertainties and other factors, including, without limitation, those referred to in this report under the heading "Risks and Uncertainties".

The Company's forward-looking statements are based on beliefs, expectations and opinions of management on the date the statements are made. For the reasons set forth above, readers should not place undue reliance on forward-looking statements. The Company undertakes no obligation to update or revise any forward-looking statements included herein if these beliefs, estimates and opinions or other circumstances should change, except as otherwise required by applicable law.