

Unaudited Condensed Interim Consolidated Financial Statements of

SPECTRA7 MICROSYSTEMS INC.

For the Three Months Ended March 31, 2023 and 2022

(Expressed in United States Dollars)

The accompanying unaudited condensed interim consolidated financial statements of Spectra7 Microsystems Inc. (the “Company”) have been prepared by and are the responsibility of the Company’s management and approved by the Board of Directors of the Company.

The Company’s independent auditor has not performed a review of these unaudited condensed interim consolidated financial statements in accordance with standards established by the Canadian Institute of Chartered Professional Accountants for a review of interim financial statements by an entity’s auditor.

SPECTRA7 MICROSYSTEMS INC.
(Unaudited)

For the Three Months Ended March 31, 2023 and 2022

Table of Contents

	Page
Condensed Interim Consolidated Statements of Loss and Comprehensive Loss	1
Condensed Interim Consolidated Statements of Changes in Shareholders' Equity (Deficiency)	2 – 3
Condensed Interim Consolidated Statements of Financial Position	4
Condensed Interim Consolidated Statements of Cash Flows	5
Notes to the Condensed Interim Consolidated Financial Statements	6 – 15

SPECTRA7 MICROSYSTEMS INC.

Condensed Interim Consolidated Statements of Loss and Comprehensive Loss (Unaudited)
For the Three Months Ended March 31, 2023 and 2022
(Expressed in United States Dollars)

	2023	2022
	\$	\$
Revenue	3,134,464	2,084,066
Cost of sales	1,171,876	1,191,346
Gross margin	1,962,588	892,720
Expenses (Income):		
Research and development, net of investment tax credits and including amortization of licenses	994,779	1,114,815
Sales and marketing	268,626	165,161
General and administrative	881,038	1,123,868
Depreciation of right-of-use assets	60,036	60,037
Depreciation of property and equipment	7,766	21,283
Share-based compensation (Note 7(b))	540,851	853,156
Interest on lease obligation of right-of-use asset (Note 4)	1,435	6,837
Accretion and interest expense (Note 6)	369,944	355,063
Foreign exchange gain	(71,920)	(45,199)
Total Expenses	3,052,555	3,655,021
Net Loss	(1,089,967)	(2,762,301)
Other comprehensive loss:		
Unrealized foreign currency translation	(289)	19,257
Total comprehensive loss	(1,090,256)	(2,743,044)
Loss per share		
Basic and diluted	(0.03)	(0.08)
Weighted average number of common shares outstanding		
Basic and diluted	34,906,763	33,081,877

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

SPECTRA7 MICROSYSTEMS INC.

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

For the Three Months Ended March 31, 2023 and 2022

(Expressed in United States Dollars)

	Common shares #	Common shares \$	Share-based payment reserve \$	Convertible debentures - share conversion option \$	Warrants \$	Deficit \$	Accumulated other comprehensive loss \$	Total Equity \$
Balance, December 31, 2021	33,074,937	167,674,271	4,493,506	911,274	3,667,941	(172,774,180)	(417,974)	3,554,838
Conversions of convertible debt to shares <i>(Note 6)</i>	4,593	3,975	-	-	-	-	-	3,975
Share-based compensation expense <i>(Note 7(b)(ii))</i>	-	-	853,156	-	-	-	-	853,156
Shares issued upon exercise of stock options	2,500	1,965	-	-	-	-	-	1,965
Total comprehensive loss	-	-	-	-	-	(2,762,301)	19,257	(2,743,044)
Balance, March 31, 2022	33,082,030	167,680,211	5,346,662	911,274	3,667,941	(175,536,481)	(398,717)	1,670,890

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

SPECTRA7 MICROSYSTEMS INC.

Condensed Interim Consolidated Statements of Changes in Shareholders' Equity (Deficiency) (Unaudited)
 For the Three Months Ended March 31, 2023 and 2022
 (Expressed in United States Dollars)

	Common shares #	Common shares \$	Share-based payment reserve \$	Convertible debentures - share conversion option \$	Warrants \$	Deficit \$	Accumulated other comprehensive loss \$	Total Equity \$
Balance, December 31, 2022	33,689,934	168,991,070	5,718,126	1,514,142	3,902,307	(179,815,622)	268,885	578,908
Shares issued under Restricted Share Unit plan	147,370	33,362	(33,362)	-	-	-	-	-
Private Placement March 2023 Equity component of convertible debentures, net of issuance costs	5,990,000	1,884,520	-	-	1,992,688	-	-	3,877,208
Share-based compensation expense (Note 7(b)(iii))	-	-	540,851	-	-	-	-	540,851
Total comprehensive loss	-	-	-	-	-	(1,089,967)	(289)	(1,090,256)
Balance, March 31, 2023	39,827,304	170,908,952	6,225,615	1,514,142	5,894,995	(180,905,589)	268,596	3,906,711

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

SPECTRA7 MICROSYSTEMS INC.

Condensed Interim Consolidated Statements of Financial Position (Unaudited)

March 31, 2023 and December 31, 2022

(Expressed in United States Dollars)

	March 31, 2023	December 31, 2022
	\$	\$
Assets		
Current assets:		
Cash	4,376,831	772,255
Trade and other receivables	2,484,690	2,526,848
Investment tax credits	5,562	5,562
Inventories	3,756,195	3,523,719
Prepaid expenses and other assets	246,616	920,026
	10,869,894	7,748,410
Non-current investment tax credits	7,983	7,983
Property and equipment	312,677	400,796
Right-of-use assets (Note 3)	260,464	80,048
Intangible assets	70,203	69,897
	11,521,221	8,307,134
Liabilities		
Current liabilities:		
Trade and other payables	1,746,653	1,932,000
Deferred revenue	-	68,750
Lease obligation on right-of-use assets (Note 4)	241,643	87,204
	1,988,296	2,087,954
Non-current convertible debentures (Note 6)	5,605,366	5,640,272
Non-current lease obligation on right-of-use assets (Note 4)	20,848	-
	7,614,510	8,666,522
Shareholders' Equity		
Common shares (Note 7(a))	170,908,952	168,991,070
Share-based payment reserve	6,225,615	5,718,126
Convertible debentures - share conversion option (Note 6)	1,514,142	1,514,142
Warrants (Note 7(c))	5,894,995	3,902,307
Deficit	(180,905,589)	(179,815,622)
Accumulated other comprehensive income(loss)	268,596	268,885
	3,906,711	578,908
	11,521,221	8,307,134

Nature of operations, going concern and continuation of the business (Note 1)

Signed on behalf of the Board:

"Ron Pasek"

Director

"Raouf Halim"

Director

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

SPECTRA7 MICROSYSTEMS INC.

Condensed Interim Consolidated Statements of Cash Flows (Unaudited)

Three Months Ended March 31, 2023 and 2022

(Expressed in United States Dollars)

	Three months ended March 31,	
	2023	2022
	\$	\$
Operating activities:		
Net Loss	(1,089,967)	(2,762,301)
Items not involving cash:		
Amortization of license	76,482	161,684
Depreciation of property and equipment	42,742	21,283
Depreciation of right-of-use assets (Note 3)	60,036	60,036
Share-based compensation (Note 7)	540,851	853,156
Accretion and interest expense (Note 6)	369,944	355,063
Loss on disposal of equipment	45,374	
	45,462	(1,311,078)
Net change in non-cash working capital items		
Trade and other receivables	42,158	962,499
Inventories	(232,476)	(704,508)
Prepaid expenses and other assets	673,409	489,869
Trade and other payables	(185,346)	9,006
Deferred Revenue	(68,750)	-
	274,457	(554,212)
Interest paid (Note 6)	(411,311)	-
	(136,854)	(554,212)
Financing activities:		
Proceeds from March 2023 private placement	3,877,207	-
Proceeds from exercise of stock options (Note 7)	-	1,965
Repayment of lease obligation on right-of-use assets (Note 4)	(65,166)	(57,963)
	3,812,041	(55,998)
Investing activities:		
Acquisition of property and equipment	-	(108,437)
Acquisition of licenses	(76,788)	(76,884)
	(76,788)	(185,321)
Effect of foreign exchange rate changes on cash	6,177	19,257
(Decrease)/Increase in cash	3,604,576	(776,274)
Cash, beginning of period	772,255	5,944,155
Cash, end of period	4,376,831	5,167,881

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

SPECTRA7 MICROSYSTEMS INC.

Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
For the Three Months Ended March 31, 2023 and 2022
(Expressed in United States Dollars)

1. Nature of operations, going concern and continuation of the business

Spectra7 Microsystems Inc. (the "Company" or "Spectra7"), is a publicly traded company listed on the TSX Venture Exchange (the "TSXV"). The Company delivers high performance analog semiconductors at unmatched bandwidth, speed and resolution to enable disruptive industrial design for leading electronics manufacturers in data centers, Virtual Reality ("VR"), Augmented Reality ("AR") and other connectivity markets.

The Company is domiciled in Canada and its registered office is located at 181 Bay Street, Suite 1800, Toronto, Canada M5J 2T9.

The Company's condensed interim consolidated financial statements have been prepared on a going concern basis. The going concern basis of presentation assumes that the Company will continue its operations for the foreseeable future and be able to realize the carrying value of its assets and discharge its liabilities in the normal course of operations. The Company incurred a comprehensive loss of \$1,090,522 for the three months ended March 31, 2023 (March 31, 2022 - \$2,743,044) and has an accumulated deficit of \$180,905,855 (March 31, 2022 - \$175,536,481). To date, the Company has funded operations through debt financings and through private and public equity offerings. These factors represent material uncertainties that may cast significant doubt upon the Company's ability to continue as a going concern. The Company's ability to continue as a going concern is dependent upon its ability to obtain additional financing and/or achieve profitable operations in the future. The condensed interim consolidated financial statements do not reflect adjustments that would be necessary if the going concern assumption were not appropriate.

The COVID-19 pandemic has negatively impacted the Company and its impact on the data center programs is uncertain. While demand for the Company's new data center products remains strong, Spectra7 continues to experience significant customer disruptions, logistics and supply chain challenges caused by the associated shutdowns due to COVID-19 that are expected to continue to impact overall revenues in the near term. The Company continues to pursue the best available paths to manage operational risk and preserve capital during this time.

2. Basis of presentation

a) Statement of compliance

These condensed interim consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"), using International Accounting Standard 34, Interim Financial Reporting ("IAS 34").

These condensed interim consolidated financial statements do not include all of the information required for full annual consolidated financial statements and should be read in conjunction with the Company's audited consolidated financial statements for the years ended December 31, 2022 and 2021.

Except as noted below, the Company has followed the same basis of presentation, accounting policies and method of computation for these condensed interim consolidated financial statements as were disclosed in the audited consolidated financial statements for the years ended December 31, 2022 and 2021. These consolidated financial statements have been prepared in accordance with IFRS as issued by the IASB.

These condensed interim consolidated financial statements were approved for issuance by the Board of Directors on May 9, 2023.

b) Basis of measurement

The condensed interim consolidated financial statements have been prepared on the historical cost basis except for certain financial instruments measured at fair value through profit or loss. Historical cost is generally based on the fair value of the consideration given in exchange for assets.

These condensed interim consolidated financial statements are presented in United States dollars. The Company's functional currency is Canadian dollars.

c) Basis of consolidation

The condensed interim consolidated financial statements incorporate the financial statements of the Company and

SPECTRA7 MICROSYSTEMS INC.

Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
For the Three Months Ended March 31, 2023 and 2022
(Expressed in United States Dollars)

its wholly owned subsidiaries and their corresponding functional currencies:

Spectra7 Microsystems Corp., a company incorporated under the laws of Ontario (USD);
Spectra7 Microsystems Ltd., a company incorporated under the laws of Delaware (USD);
Spectra7 Microsystems (Ireland) Limited, a company incorporated under the laws of Ireland (USD); and
Si Bai Ke Te (Dongguan) Electronics Trading Co. Ltd., a China wholly foreign owned enterprise (CNY) .

All intercompany balances and transactions are eliminated in full on consolidation.

d) Critical accounting estimates and judgements

The Company uses the same critical accounting estimates and judgements as those that applied to the annual consolidated financial statements for the year ended December 31, 2022.

3. Right-of-use assets

The following table sets forth the right-of-use assets:

	\$
Balance, January 1, 2022	320,194
Depreciation	(293,539)
Lease Amendment	53,393
Balance, December 31, 2022	80,048
Depreciation	(60,036)
Lease Amendment	240,452
Balance, March 31, 2023	260,464

The Company recorded a right-of-use assets and a corresponding lease obligations of \$240,452 using an incremental borrowing rate of 8.75% in 2023 when the Company entered into an amendment to extend the lease for its headquarters through April 2024.

4. Lease obligations on right-of-use assets

The present value of the remaining minimum lease payments on the obligations for right-of-use assets as at March 31, 2023 are as follows:

	\$
Balance, January 1, 2022	331,758
Repayments	(264,000)
Interest	19,446
Balance, December 31, 2022	87,204
Lease Amendment	240,452
Repayments	(66,600)
Interest	1,435
Balance, March 31, 2023	262,491
Current	241,643
Non-current	20,848

SPECTRA7 MICROSYSTEMS INC.

Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
For the Three Months Ended March 31, 2023 and 2022
(Expressed in United States Dollars)

5. Inventories

	March 31, 2023	December 31, 2022
	\$	\$
Work-in-progress	3,562,809	3,362,138
Finished goods	460,517	428,712
	4,023,326	3,585,312
Less: provision for obsolescence	(267,131)	(267,131)
	3,756,195	3,523,719

Inventories recognized as cost of sales for the three months ended March 31, 2023 amounted to \$1,098,107 (\$1,109,176 for the three months ended March 31, 2022).

6. Convertible debentures

	\$
Balance, January 1, 2022	5,947,307
Repayment of principal	(6,346,555)
Proceeds from issuance of convertible debt	6,730,570
Allocation to equity	(602,868)
Finder warrants, allocated to transaction costs	(234,366)
Transaction costs	(387,761)
Accretion and interest expense	1,474,501
Repayment of interest	(438,290)
Repayment of interest in shares	(3,975)
Foreign exchange translation adjustment	(498,291)
Balance, December 31, 2022	5,640,272
Accretion and interest expense	369,944
Repayment of interest	(411,311)
Foreign exchange translation adjustment	6,461
Balance, March 31, 2023	5,605,366

The Company's convertible debentures are subject to certain covenants including restrictions against incurring certain additional indebtedness. As at March 31, 2023, the Company was in compliance with all covenants. During the year ended December 31, 2022, 4,593 common shares were issued to repay interests due for \$3,975.

On December 9, 2021, the Company entered into a second supplemental convertible debenture indenture (the "Second Supplemental Indenture") to amend the terms and conditions of its 7% unsecured convertible debentures (the "7% Debentures") to reduce the conversion price from CDN \$5.00 per common share to CDN \$2.50 per common share from January 10, 2022 to July 9, 2022. The Company treated the change as a modification of the existing instrument and recorded a gain of \$379,140.

The Second Supplemental Indenture was recorded as a modification of the financial instrument with debt component of \$5,947,307, determined using present value of future cash flows including a principal amount of \$6,354,099 and a discount rate of 18.0%. Debt component is being amortized using an effective interest rate of approximately 23.6% over its remaining term.

SPECTRA7 MICROSYSTEMS INC.

Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)

For the Three Months Ended March 31, 2023 and 2022

(Expressed in United States Dollars)

On July 26, 2022, the Company entered into a third supplemental convertible debenture indenture (the "Third Supplemental Indenture") to amend certain terms and conditions of the 7% Debentures. Pursuant to the Third Supplemental Indenture, the maturity date of the 7% Debentures was extended to September 9, 2022. The Company repaid 20% of the outstanding principal amount together with the 10% bonus principal outstanding on the 7% Debentures on August 2, 2022, including accrued and unpaid interest, totaling CDN \$2,600,704. The principal outstanding after the payment was CDN \$5,422,400. As consideration for the extension, the Company agreed to pay non-convertible extension bonuses at maturity of an aggregate of approximately CDN \$199,978. As at September 2, 2022, the Company repaid the remaining balance of the 7% Debentures in full. The total amount repaid was \$6,346,555 (CDN \$8,067,800) principal amount, \$62,637 (CDN \$80,802) of accrued and unpaid interest thereon, as well as \$157,321 (CDN \$199,978) of the extension bonus and \$1,115 (CDN \$1,438) of associated interest. The 7% Debentures were repaid in full effective September 2, 2022.

On July 26, 2022, the Company announced a non-brokered private placement (the "Offering") of the 14% convertible unsecured debentures (the "14% Debentures") and completed the first tranche of the Offering through the issuance of \$2,940,739 (CDN \$3,809,000) principal amount of 14% Debentures for gross proceeds of \$2,881,924 (CDN \$3,732,820). On August 25, 2022, the Company entered into a first supplemental convertible debenture indenture to increase the size of the Offering and completed the second tranche of the Offering through the issuance of \$3,927,162 (CDN \$5,064,000) principal amount of the 14% Debentures for gross proceeds of \$3,848,619 (CDN \$4,962,720). In aggregate, the Offering consisted of the issuance of \$6,867,901 (CDN \$8,873,000) principal amount of 14% Debentures for gross proceeds of \$6,730,543 (CDN \$8,695,540). Proceeds from the Offering were primarily used to repay the 7% Debentures.

Each CDN \$1,000 principal amount of 14% Debentures was sold at a subscription price of CDN \$980. The 14% Debentures mature on December 31, 2024 and the principal amount is convertible into common shares at the option of the holder at any time prior to the close of business on the last business day immediately preceding maturity, at a conversion price of CDN \$1.02 per common share, subject to adjustment upon certain customary events. Holders converting their 14% Debentures will receive accrued and unpaid interest thereon for the period from and including the date of the latest interest payment date to, and including, the date of conversion. In connection with the Offering, the Company paid \$387,761 (CDN \$500,968) in finder's fees and issued an aggregate of 401,603 finder's warrants, with each such warrant entitling the holder thereof to purchase one common share at a price of \$1.02 for a period of two years from the date of issuance.

The Company determines the carrying amount of the financial liability using the present value of future cash flows with the principal amount of \$6,694,367 and a discount rate of 25.8%. Debt component is being amortized using an effective interest rate of approximately 21% over its remaining term. The liability component is then increased by accretion of the discounted amounts to reach the nominal value of the convertible notes at maturity which is recorded in the statement of loss and comprehensive loss as accretion expense.

The carrying amount of other components (when applicable), such as warrants, is determined using the Black Scholes option pricing model based on the following assumptions: volatility of 172%, expected term of 2 years, risk free rate of 3.12% and zero dividend. The carrying amount of the equity component is calculated by deducting the carrying amount of the financial liability and the carrying amounts of any other components from the amount of the convertible notes, and is presented in Equity as an equity component of convertible notes.

The transaction costs are distributed between liability, equity and other (when applicable) components, on a pro rata basis according to their carrying amounts. Accordingly, the face value of the 14% Debentures, net of issuance costs, were allocated as follows:

	\$
Liability component	335,758
Conversion feature	52,003
Transaction costs	387,761

SPECTRA7 MICROSYSTEMS INC.

Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
For the Three Months Ended March 31, 2023 and 2022
(Expressed in United States Dollars)

7. Shareholders' equity

(a) Common shares

Authorized share capital consists of an unlimited number of common shares.

(i) March 2023 Private Placement

On March 15, 2023, the Company completed a brokered private placement (the "March 2023 Private Placement") of 5,990,000 units (the "March 2023 Units") at a price of CDN \$1.00 per March 2023 Unit for aggregate gross proceeds of \$4,342,750 (CDN \$5,990,000). Each March 2023 Unit consists of one common share and one common share purchase warrant (each, a "March 2023 Warrant") with each March 2023 Warrant being exercisable into one common share at an exercise price of CDN \$1.18 until March 15, 2028, subject to adjustment upon certain customary events. The expiry date of the March 2023 Warrants can be accelerated by the Company to the date that is thirty (30) days following the delivery of an acceleration notice to the holders of the March 2023 Warrants if, at any time following the closing date of the March 2023 Private Placement, the closing price of the common shares is greater than CDN \$4.00 for a period of 10 non-consecutive trading days on the TSXV.

In connection with the March 2023 Private Placement, the Company paid a commission of \$291,183 (CDN \$401,632) and issued 229,504 broker warrants, with each broker warrant being exercisable into one common share at a price of CDN \$1.10 for the period commencing on the date that is six months after the closing date until the fifth anniversary of the closing date. Gross proceeds from the March 2023 Private Placement were allocated to the common shares and warrants based on their relative fair values, net of issuance costs. The fair value of the warrants was determined using the Black Scholes option pricing model based on the following assumptions: volatility of 172%, expected term of 5 years, risk free rate of 3.59% and zero dividend. The equity portion allocated to warrant was \$1,992,688.

(b) Share-based compensation

The Company has established a stock option plan (the "Stock Option Plan") and a restricted share unit plan (the "RSU Plan") with the intention of attracting, retaining and motivating employees, officers and directors.

The Company's Board of Directors determines, among other things, the eligibility of individuals to participate in the RSU Plan and the Stock Option Plan and the term, vesting periods, and the exercise price of options granted under the Stock Option Plan.

At the annual and special meeting of shareholders in June 2022, shareholders approved amendments to both the Stock Option Plan and the RSU Plan to provide that the combined maximum number of common shares reserved for issuance under both the Stock Option Plan and the RSU Plan, inclusive of existing stock options and RSUs, shall not exceed 20% of the then outstanding common shares or 6,710,018 common shares.

(i) Restricted Share Units (RSU)

Vesting is determined by the Company's Board of Directors at the time of grant. Vesting is contingent upon continuous service/employment through the specific vesting date. The fair value as of the grant date is used to determine the value.

The following table summarizes information about the Company's outstanding RSUs as at March 31, 2023 and 2022:

	March 31, 2023	March 31, 2022
	#	#
Balance, opening	4,328,217	2,907,256
Granted	50,000	220,027
Forfeited	(1,000)	(24,461)
Vested and Shares issued	(147,370)	-
Balance, ending	4,229,847	3,102,822

SPECTRA7 MICROSYSTEMS INC.

Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
For the Three Months Ended March 31, 2023 and 2022
(Expressed in United States Dollars)

(ii) Stock options

Vesting is determined by the Company's Board of Directors at the time of grant. Vesting is contingent upon continuous service/employment through the specific vesting date. Options have an exercise price as set forth in the option certificate issued in respect of such options and in any event shall not be less than market price of the common shares as of the award date. The expiry date of an option is fixed by the Board of Directors at the time the particular option is awarded, provided that the expiry date shall be no later than the date that is 10 years following the award date of such option, subject to earlier termination upon the option holder ceasing to be a director, officer, employee or consultant of the Company.

The following table summarizes information about the Company's outstanding stock options as at March 31, 2023 and 2022:

	March 31, 2023		March 31, 2022	
	Number of Options #	Weighted Average Price CDN \$	Number of Options #	Weighted Average Price CDN \$
Options outstanding, opening	259,768	1.38	298,274	2.43
Granted	-	-	-	-
Exercised	-	-	-	-
Expired	-	-	-	-
Forfeited	(2,100)	11.62	(4,494)	9.80
Options outstanding, ending	257,668	1.80	293,780	2.38

The following table is a summary of the Company's stock options outstanding as at March 31, 2023:

Exercise price range CDN \$	Number outstanding #	Options Outstanding		Options Exercisable	
		Weighted average remaining contractual life (years) #	Weighted average exercise price CDN \$	Number exercisable #	Weighted average exercise price CDN \$
1.00 – 1.90	254,000	4.80	1.46	254,000	1.46
9.50 – 26.00	3,668	0.66	25.27	3,268	25.27
Balance, March 31, 2023	257,668	4.74	1.80	257,268	1.80

The following table is a summary of the Company's stock options outstanding as at March 31, 2022:

Exercise price range CDN \$	Number outstanding #	Options Outstanding		Options Exercisable	
		Weighted average remaining contractual life (years) #	Weighted average exercise price CDN \$	Number exercisable #	Weighted average exercise price CDN \$
1.00 – 1.90	280,000	6.42	1.44	240,000	1.37
9.50 – 34.00	13,780	1.52	21.35	13,551	21.69
Balance, March 31, 2022	293,780	6.19	2.38	253,551	2.59

SPECTRA7 MICROSYSTEMS INC.

Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
For the Three Months Ended March 31, 2023 and 2022
(Expressed in United States Dollars)

(iii) Share-based compensation expense

For its RSU Plan and Stock Option Plan, the Company recognized share-based compensation expense of \$540,851 for the three months ended March 31, 2023 (\$853,156 for the three months ended March 31, 2022) with a corresponding amount recognized as share-based payment reserve.

The fair value of the RSUs is determined based upon the Company's stock price on the date of grant. There were no stock options granted during the three months ended March 31, 2023 and 2022.

(c) Warrants

The following table summarizes information about the Company's outstanding warrants as at March 31, 2023 and 2022:

	March 31, 2023		March 31, 2022	
	Number of Warrants #	Weighted Average Price CDN \$	Number of Warrants #	Weighted Average Price CDN \$
Balance, opening	9,756,307	3.09	9,398,804	3.23
Warrants component of March 2023 Private Placement (Note 7 (a))	5,990,000	1.18	-	-
Broker Warrants component of March 2023 Private Placement (Note 7 (a))	229,504	1.10		
Warrants expired	-	-	(44,100)	15.00
Balance, ending	15,975,811	2.35	9,354,704	3.17

The following is a summary of the warrants outstanding by exercise price as at March 31, 2023:

Number of warrants outstanding	Exercise Price	Expiry Date
Warrants ⁽¹⁾		
283,363	CDN \$7.875	July 6, 2023
324,122	CDN \$11.25	October 30, 2023
1,584,316	CDN \$4.00	August 21, 2024
210,469	CDN \$2.50	July 15, 2025
166,779	CDN \$2.50	September 25, 2025
1,140,138	CDN \$2.50	January 15, 2026
478,665	CDN \$2.50	February 12, 2026
4,223,141	CDN \$2.50	May 14, 2026
5,990,000	CDN \$1.18	March 15, 2028
Broker Warrants (Compensation Options)		
242,489 ⁽²⁾	CDN \$1.50	May 14, 2023
9,943	CDN \$7.875	July 6, 2023
411,028	CDN \$1.32	October 26, 2023
28,941	CDN \$11.25	October 30, 2023
118,055	CDN \$1.02	July 26, 2024
251,310	CDN \$2.50	August 21, 2024
283,548	CDN \$1.02	August 25, 2024
229,504	CDN \$1.10	March 15, 2028

SPECTRA7 MICROSYSTEMS INC.

Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)
For the Three Months Ended March 31, 2023 and 2022
(Expressed in United States Dollars)

The following is a summary of the warrants outstanding as at March 31, 2022:

Number of warrants outstanding	Exercise Price	Expiry Date
Warrants ⁽¹⁾		
283,363	CDN \$7.875	July 6, 2023
324,122	CDN \$11.25	October 30, 2023
1,584,316	CDN \$4.00	August 21, 2024
210,469	CDN \$2.50	July 15, 2025
166,779	CDN \$2.50	September 25, 2025
1,140,138	CDN \$2.50	January 15, 2026
478,665	CDN \$2.50	February 12, 2026
4,223,141	CDN \$2.50	May 14, 2026
Broker Warrants (Compensation Options)		
242,489 ⁽²⁾	CDN \$1.50	May 14, 2023
9,943	CDN \$7.875	July 6, 2023
411,028	CDN \$1.32	October 26, 2023
28,941	CDN \$11.25	October 30, 2023
251,310	CDN \$2.50	August 21, 2024

⁽¹⁾ Subject to acceleration in certain circumstances.

⁽²⁾ Convertible into one common share and one warrant exercisable at CDN \$2.50.

8. Related party transactions and balances

The Company transacts with key individuals from management and with its directors who have authority and responsibility to plan, direct and control the activities of the Company. The nature of these dealings was in the form of payments for services rendered in their capacity as employees and as directors of the Company and are recorded at their fair value.

The Company's key management personnel are comprised of the Board of Directors and current and former members of the executive team of the Company.

Key management personnel compensation is comprised of the following:

	Three Months Ended March 31,	
	2023	2022
	\$	\$
Salaries, fees and short-term benefits	269,250	320,500
Share-based compensation	328,176	447,428
	597,426	767,928

As at March 31, 2023, the amount owing to directors and officers was \$140,000 (\$143,000 for the three months ended March 31, 2022).

SPECTRA7 MICROSYSTEMS INC.

Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)

For the Three Months Ended March 31, 2023 and 2022

(Expressed in United States Dollars)

9. Economic dependence

During the three months ended March 31, 2023, the Company derived approximately 99% of its revenue from two customers (March 31, 2022 – 98% from two customers).

10. Financial instruments

The Company's financial instruments consist of cash, trade and other receivables, trade and other payables, lease obligation on right of use assets and convertible debt. These financial instruments are classified as financial assets and liabilities at amortized cost and are reported at amortized cost.

Basis of fair values

Assets and liabilities recorded at fair value on the statement of financial position are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

Level 1 – quoted prices (unadjusted) observed in active markets for identical assets or liabilities.

Level 2 – inputs other than quoted prices included in level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices).

Level 3 – inputs for the asset or liability that are not based on observable market data (unobservable inputs)

If the inputs used to measure the fair value of an asset or liability fall into different levels of the fair value hierarchy, then the fair value measurement is categorized in its entirety in the same level of the fair value hierarchy as the lowest level input that is significant to the entire measurement.

The Company recognizes transfers between levels of the fair value hierarchy at the end of the reporting period during which the change has occurred. There have been no significant transfers between levels during the year.

The carrying value of the Company's financial assets and liabilities approximate their fair values due to their nature and their short-term to maturity.

The Company may be exposed to risks of varying degrees of significance that affect its ability to achieve its strategic objectives. The main objectives of the Company's risk processes are to ensure that the risks are properly identified and that the capital base is adequate in relation to those risks. The principal risks to which the Company is exposed to are as follows:

Foreign currency risk

The Company may undertake sales and purchases transactions in foreign currencies, and therefore is exposed to gains or losses due to fluctuations in foreign currency exchange rates. Management believes the foreign exchange risk derived from currency conversions is currently low and therefore does not actively hedge its foreign currency risk. There has been no change to the Company's policies and processes with respect to the way it manages foreign currency risk.

Interest risk

Interest rate risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate due to changes in market interest rates. Interest rate risk associated with the Company's 14% Debentures arises from fluctuations in interest rates and the degree of volatility of these rates. The 14% Debentures provide for a fixed annual rate of 14% and hence no interest rate risk. The Company does not use derivative financial instruments to reduce its exposure to interest rate risk.

Credit risk

Credit risk is the risk of loss associated with a counterparty's inability to fulfill its payment obligations. The Company's credit risk is primarily attributable to trade and other receivables and money held in the Company's bank accounts. The carrying value of these assets represents the maximum credit exposure. The Company mitigates this risk by monitoring the credit worthiness of its customers and only dealing with creditworthy counterparties. At March 31, 2023, two customers represented 99% of the Company's trade and other receivables.

SPECTRA7 MICROSYSTEMS INC.

Notes to the Condensed Interim Consolidated Financial Statements (Unaudited)

For the Three Months Ended March 31, 2023 and 2022

(Expressed in United States Dollars)

Liquidity risk

The Company's objective is to have sufficient liquidity to meet its liabilities when due. The Company monitors its cash balances and cash flows generated from operations to meet its requirements. There has been no change to the Company's policies and processes with respect to the way it manages liquidity risk.

12. Capital management

The Company's objectives when managing capital are to: (i) ensure the Company continues to operate as a going concern to maximize the return on investment to shareholders; (ii) ensure sufficient liquidity to meet the Company's financial obligations and to execute its operating and strategic plans; and (iii) minimize the after tax cost of capital while taking into consideration current and future industry, market and economic risks and conditions. The Company's capital structure consists of its equity, loan facility and convertible debentures. Other than covenants disclosed in convertible debentures note (Note 6), there are no externally imposed restrictions on capital.

The Company intends to maintain a flexible capital structure in order to finance its ongoing growth and respond to changes in economic conditions.