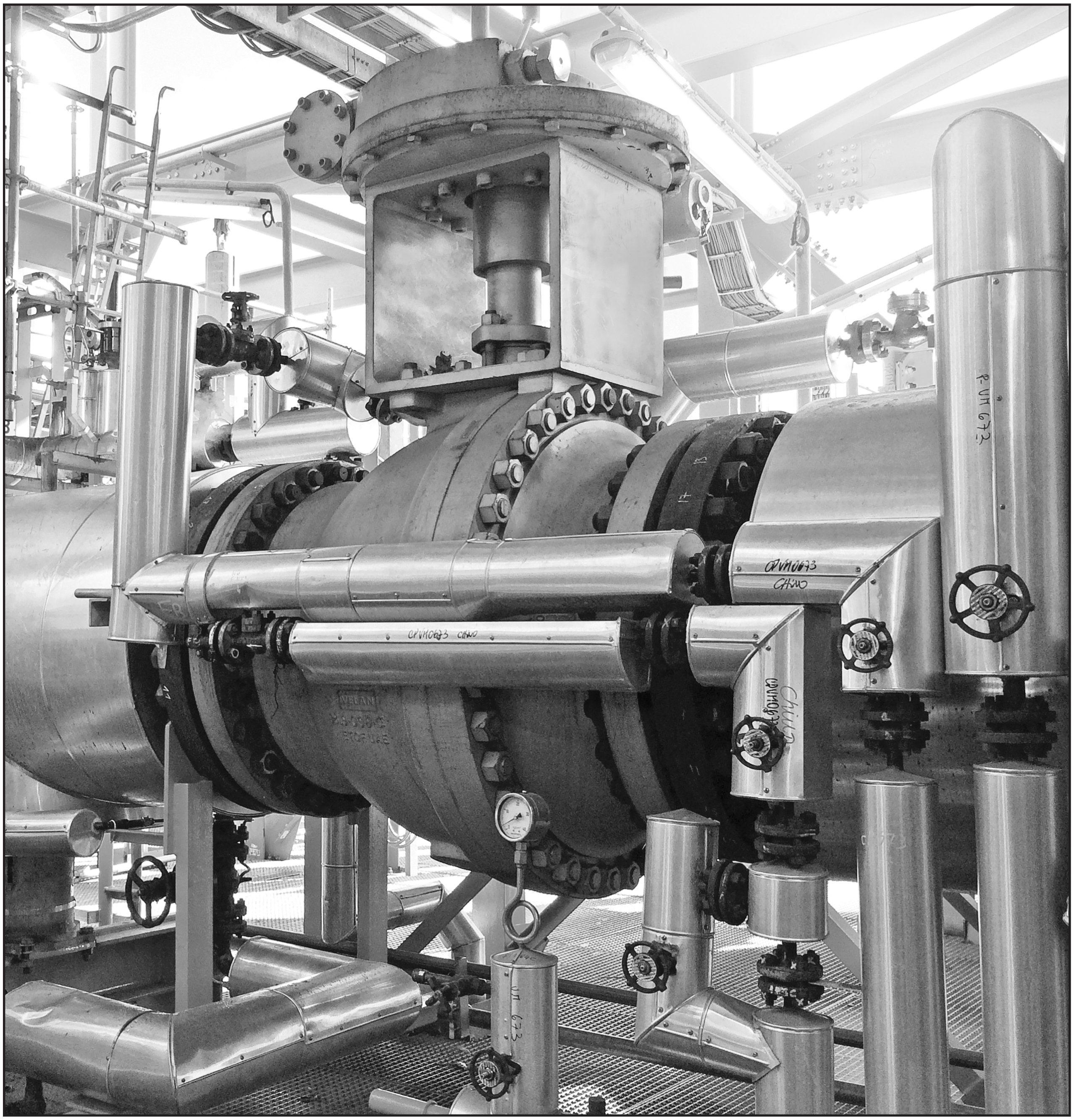
Report to shareholders
Third quarter

Nine month period ended November 30, 2019



Velan. Quality that lasts.

VELAN

Management's Discussion and Analysis

3rd QUARTER ENDED NOVEMBER 30, 2019

January 9, 2020

The following discussion provides an analysis of the consolidated operating results and financial position of Velan Inc. ("the Company") for the quarter ended November 30, 2019. This Management's Discussion and Analysis ("MD&A") should be read in conjunction with the Company's audited consolidated financial statements for the years ended February 28, 2019 and 2018. The Company's consolidated financial statements have been prepared in accordance with International Financial Reporting Standards as issued by the International Accounting Standards Board ("IFRS"). The significant accounting policies upon which these consolidated financial statements have been prepared are detailed in Note 2 and 3 of the Company's audited consolidated financial statements. The Company's reporting currency is the US dollar. Additional information relating to the Company, including the Annual Information Form and Proxy Information Circular, can be found on SEDAR at **www.sedar.com**.

NON-IFRS MEASURES

In this MD&A, the Company has presented measures of performance or financial condition which are not defined under IFRS ("non-IFRS measures") and are, therefore, unlikely to be comparable to similar measures presented by other companies. These measures are used by management in assessing the operating results and financial condition of the Company and are reconciled with the performance measures defined under IFRS. Reconciliations of these amounts can be found at the end of this report.

FORWARD-LOOKING INFORMATION

This MD&A may include forward-looking statements, which generally contain words like "should", "believe", "anticipate", "plan", "may", "will", "expect", "intend", "continue" or "estimate" or the negatives of these terms or variations of them or similar expressions, all of which are subject to risks and uncertainties. These risks and uncertainties are disclosed in the Company's filings with the appropriate securities commissions. While these statements are based on management's assumptions regarding historical trends, current conditions and expected future developments, as well as other factors that it believes are reasonable and appropriate in the circumstances, no forward-looking statement can be guaranteed and actual future results may differ materially from those expressed herein. The Company disclaims any intention or obligation to update or revise any forward-looking statements contained herein whether as a result of new information, future events or otherwise, except as required by the applicable securities laws. The forward-looking statements contained in this report are expressly qualified by this cautionary statement.

OVERVIEW

The Company designs, manufactures and markets on a worldwide basis a broad range of industrial valves for use in most industry applications including power generation, oil and gas, refining and petrochemicals, chemicals, LNG and cryogenics, pulp and paper, geothermal processes and shipbuilding. The Company is a world leader in steel industrial valves operating 13 manufacturing plants worldwide with 1,827 employees. The Company's head office is located in Montreal, Canada. The Company's business strategy is to design, manufacture, and market new and innovative valves with emphasis on quality, safety, ease of operation, and long service life. The Company's strategic goals include, but are not limited to, customer-driven operational excellence and margin improvements, accelerated growth through increased focus on key target markets where the Company has distinct competitive advantages and continuously improving and modernizing its systems and processes.

The consolidated financial statements of the Company include the North American operations comprising three manufacturing plants in Canada, as well as one manufacturing plant and one distribution facility in the U.S. Significant overseas operations include manufacturing plants in France, Italy, Portugal, Korea, Taiwan, India, and China. The Company's operations also include a distribution facility in Germany and a 50%-owned Korean foundry.

Management's Discussion and Analysis

CONSOLIDATED HIGHLIGHTS[1]

(millions, excluding per share amounts)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Increase (decrease)	% Increase (decrease)
Consolidated statements of earnings				
Sales	$88.7	$92.3	$(3.6)	(3.9)%
Gross profit	22.2	22.6	(0.4)	(1.8)%
Gross profit %	25.0%	24.5%		
Operating profit before restructuring and transformation costs[3]	1.0	0.2	0.8	400.0%
Net loss[2]	(0.8)	(0.2)	(0.6)	(300.0)%
Net loss[2] %	(0.9)%	(0.2)%		
Net loss[2] per share – basic and diluted	(0.04)	(0.01)	(0.03)	(300.0)%
Adjusted EBITDA[3]	4.3	3.4	0.9	26.5%
Adjusted EBITDA[3] %	4.8%	3.7%		
Adjusted EBITDA[3] per share – basic and diluted	0.20	0.16	0.04	25.0%
Weighted average shares outstanding	21.6	21.6		
Consolidated statements of cash flows				
Cash provided (used) by operating activities	10.4	(2.2)	12.6	572.7%
Cash used by investing activities	(3.7)	(1.1)	(2.6)	(236.4)%
Cash provided (used) by financing activities	(1.8)	2.6	(4.4)	(169.2)%
Demand data				
Net new orders received	97.2	100.8	(3.6)	(3.6)%
Period end backlog of orders	432.1	471.5	(39.4)	(8.4)%

[1] *All dollar amounts in this schedule are denominated in U.S. dollars.*
[2] *Net earnings or loss refers to net income or loss attributable to Subordinate and Multiple Voting Shares.*
[3] *Non-IFRS measures – see reconciliations at the end of this report.*

Management's Discussion and Analysis

(millions, excluding per share amounts)	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018	Increase (decrease)	% Increase (decrease)
Consolidated statements of earnings				
Sales	$258.0	$261.5	$(3.5)	(1.3)%
Gross profit	60.2	59.7	0.5	0.8%
Gross profit %	23.3%	22.8%		
Operating loss before restructuring and transformation costs[2]	(3.3)	(6.3)	3.0	47.6%
Net loss[1]	(5.3)	(6.4)	1.1	17.2%
Net loss[1] %	(2.1)%	(2.4)%		
Net loss[1] per share – basic and diluted	(0.24)	(0.30)	0.06	20.0%
Adjusted EBITDA[2]	6.2	3.3	2.9	87.9%
Adjusted EBITDA[2] %	2.4%	1.3%		
Adjusted EBITDA[2] per share – basic and diluted	0.29	0.15	0.14	93.3%
Weighted average shares outstanding	21.6	21.6		
Consolidated statements of cash flows				
Cash provided (used) by operating activities	13.4	(5.4)	18.8	348.1%
Cash used by investing activities	(8.5)	(5.3)	(3.2)	(60.4)%
Cash used by financing activities	(4.6)	(0.8)	(3.8)	(475.0)%
Demand data				
Net new orders received	252.1	290.4	(38.3)	(13.2)%
Period end backlog of orders	432.1	471.5	(39.4)	(8.4)%

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[2] *Non-IFRS measures – see reconciliations at the end of this report.*

Management's Discussion and Analysis

Highlights *(unless otherwise noted, all amounts are in U.S. dollars and all comparisons are to the same period in the prior fiscal year)*

Results for the quarter ended November 30, 2019

- Sales amounted to $88.7 million, a decrease of $3.6 million or 3.9% from the prior year. The decrease for the quarter was primarily attributable to the shipment by the North American operations of a large complex Chinese order in the third quarter of the prior fiscal year, partially offset by an increase in shipments of large project orders in the Company's Italian operations due to a record backlog at the beginning of the year.
- Gross profit percentage increased by 50 basis points from 24.5% to 25.0%. The increase in the gross profit percentage is mainly attributable to a stronger proportion of higher margin product sales and an increased sales volume in the Company's Italian operations, which allowed the subsidiary to cover its fixed costs more efficiently. This increase was partially offset by temporary factors such as a less efficient product mix in the Company's North American operations, including a lower volume of higher margin spare parts sales. The Company has realized an improvement in the gross profit percentage of its North American operations in comparison to the first and second quarters of the current fiscal year, thanks to improved margins in its project manufacturing business.
- Net loss[1] amounted to $0.8 million or $0.04 per share compared to $0.2 million or $0.01 per share last year. Net loss[1] for the current quarter was significantly impacted by the $1.4 million spent on the Company's restructuring and transformative initiative, V20, which aims to improve its operational efficiency and optimize its manufacturing footprint in North America. The Company's current production is being reorganized from four North American plants to three more specialized plants that will be structured to better support the new business units' market strategies. The production of certain non-project valves produced in North America, as well as the less complex project valves are also being transferred to India. Restructuring and transformation costs include temporary project resources and their travel and lodging costs as well as the moving costs related to dismantling and transportation of machinery and equipment to reflect the optimized manufacturing footprint plan. Excluding this $1.4 million amount, as well as the after-tax impact of these restructuring and transformation costs incurred during the quarter, the Company would have presented net earnings[1] of $0.2 million compared to a net loss[1] of $0.2 million last year, representing an improvement of $0.4 million in net loss[1] which is primarily attributable to lower administration costs partially offset by higher finance costs.
- Operating profit before restructuring and administration costs[2] amounted to $1.0 million compared to $0.2 million last year. Operating profit presents the profitability of a business before taking into account interest and taxes. Adjusted EBITDA[2] amounted to $4.3 million or $0.20 per share compared to $3.4 million or $0.16 per share last year. The increase in operating profit before restructuring and administration costs[2] and adjusted EBITDA[2] is mainly attributable to lower administration costs and an improved gross profit percentage, partially offset by a lower sales volume.
- Net new orders received ("bookings") amounted to $97.2 million, a decrease of $3.6 million or 3.6% compared to last year. This decrease is primarily attributable to lower order bookings by the Company's Italian operations, which booked a record of large project orders in the prior year. This decrease was partially offset by higher order bookings in the Company's Indian operations.
- The Company ended the period with net cash of $39.0 million, an increase of $4.1 million or 11.7% since the beginning of the quarter. This increase is primarily attributable to cash provided by operating activities partially offset by investments in property, plant and equipment. Net cash was also negatively impacted by V20 related disbursements as well as the weakening of the euro spot rate against the U.S. dollar over the course of the current quarter.

Results for the nine-month period ended November 30, 2019

- Sales amounted to $258.0 million, a decrease of $3.5 million or 1.3% from the prior year. Sales were negatively impacted by decreased shipments of certain large project orders in the Company's North American and French operations due to various customer-related issues and the timing of the delivery schedule for such orders, partially offset by increased shipments from the Company's Italian operations which continued to deliver the record backlog

[1] *Net earnings or loss refers to net income or loss attributable to Subordinate and Multiple Voting Shares.*
[2] *Non-IFRS measures – see reconciliations at the end of this report.*

at the beginning of the year. The decrease of sales in the Company's French operations is due to the timing of the deliveries of certain of its large project orders which have been delivered in part in this quarter and are expected to ship in the last quarter of this fiscal year.

- Gross profit percentage increased by 50 basis points from 22.8% to 23.3%. This improvement is due to a higher sales volume and a stronger proportion of higher margin product sales in the Company's Italian operations, partially offset by a lower sales volume and a less efficient product mix in the Company's North American operations. Overall, the Company is still delivering its backlog built during the last fiscal year which means that the margins do not yet reflect the impact of the margin improvement measures launched in the last quarters under the Company's V20 transformation plan. The combined effect of these measures is expected to gradually take effect in the last quarter of this fiscal year and next year but the greater impact of the Company's restructuring and transformative V20 initiatives is only expected late in fiscal year 2021, when the task of reorganizing and reducing the Company's North American footprint is planned to be completed.
- Net loss[1] amounted to $5.3 million or $0.24 per share compared to $6.4 million or $0.30 per share last year. Net loss[1] for the current nine-month period was significantly impacted by the $2.5 million spent on the Company's restructuring and transformative initiative, V20. Restructuring and transformation costs include temporary project resources and their travel and lodging costs as well as the moving costs related to dismantling and transportation of machinery and equipment to reflect the optimized manufacturing footprint plan. Excluding this $2.5 million amount, as well as the after-tax impact of these restructuring and transformation costs incurred during the nine-month period, the Company's net loss[1] would have been $3.5 million compared to $6.4 million last year, representing an improvement of $2.9 million in net loss[1] which is primarily attributable to lower administration costs and an improved gross margin despite the lower sales volume.
- Operating loss before restructuring and transformation costs[2] amounted to $3.3 million compared to $6.3 million last year. Adjusted EBITDA[2] amounted to $6.2 million or $0.29 per share compared to $3.3 million or $0.15 per share last year. The improvement in operating loss before restructuring and transformation costs[2] and adjusted EBITDA[2] is primarily attributable to lowered administration and an increase in gross profit percentage.
- Bookings amounted to $252.1 million, a decrease of $38.3 million or 13.2% compared to last year. This decrease is due primarily to lower order bookings by the Company's North American operations which had seen an unusually high surge of non-project valve re-stocking orders from its distributors in the first quarter of the prior fiscal year. MRO distributor orders this fiscal year are expected to reflect a more normalized stock replenishment cycle. The decrease is also due to lower large project orders booked by the Company's Italian operations which booked a record of large project orders in the prior year. The Company's project quotation activity has notably increased this year in sectors where margins are healthy, and concurrently decreased in other sectors where the Company experiences the most aggressive competition and where margins are much tighter. The shift is the result of deliberate screening that is expected to take effect gradually as the Company replaces its existing backlog with higher margin orders. The net decrease in bookings experienced in the last nine months, which the Company's plan aims to reverse, must be understood in this context.
- The Company ended the period with a backlog of $432.1 million, a decrease of $17.6 million or 3.9% since the beginning of the current fiscal year. The decrease in backlog is primarily attributable to a lower book-to-bill ratio of 0.98 and the weakening of the euro spot rate against the U.S. dollar over the course of the current fiscal year.
- Administration costs amounted to $63.7 million, a decrease of $2.5 million or 3.8% compared to last year. The decrease in administration costs was achieved despite the recording of a $0.9 million provision regarding the settlement of a product claim that was filed against the Company in a prior fiscal year as well as an increase in the costs recognized in connection with the Company's ongoing asbestos litigation (see *Contingencies* section). The fluctuation in asbestos costs for the period is due more to the timing of settlements in these two periods rather than to changes in long-term trends. The reduction in administration costs is mainly attributable to lower sales commissions as well as the higher freight charges that were incurred in the prior fiscal year in order to air freight a large delayed order.
- The Company ended the period with net cash of $39.0 million, a decrease of $1.9 million or 4.6% since the beginning of the year. This decrease, which occurred mainly in the first half of the fiscal year, is primarily attributable to investments in property, plant and equipment, land restoration costs related to a property, long-term

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[2] *Non-IFRS measures – see reconciliations at the end of this report.*

debt and lease liabilities repayments, as well as distributions to shareholders via dividends, partially offset by cash provided by operating activities and an increase in long-term debt. Net cash was also negatively impacted by V20 related disbursements as well as the weakening of the euro spot rate against the U.S. dollar over the course of the current year.

- Foreign currency impacts:
  - Based on average exchange rates, the euro weakened 5.1% against the U.S. dollar when compared to the same period last year. This resulted in the Company's net profits and bookings from its European subsidiaries being reported as lower U.S. dollar amounts in the current period.
  - Based on average exchange rates, the Canadian dollar weakened 2.1% against the U.S. dollar when compared to the same period last year. This resulted in the Company's Canadian dollar expenses being reported as lower U.S. dollar amounts in the current period.
  - The net impact of the above currency swings was generally unfavourable on the Company's results.

SUMMARY OF QUARTERLY RESULTS

Summary financial data derived from the Company's unaudited financial statements from each of the eight most recently completed quarters are as follows:

For the quarters in months ending May, August, November and February
(in thousands of U.S. dollars, excluding per share amounts)

	QUARTERS ENDED							
	November 2019	**August 2019**	**May 2019**	**February 2019**	**November 2018**	**August 2018**	**May 2018**	**February 2018**
Sales	$88,701	$85,467	$83,816	$105,345	$92,271	$91,375	$77,874	$102,607
Net earnings (loss)[1]	(819)	1,369	(5,824)	1,519	(236)	(2,438)	(3,727)	(8,221)
Net earnings (loss)[1] per share								
- Basic	(0.04)	0.06	(0.27)	0.07	(0.01)	(0.11)	(0.17)	(0.38)
- Diluted	(0.04)	0.06	(0.27)	0.07	(0.01)	(0.11)	(0.17)	(0.38)

Sales can vary from one quarter to the next due to the timing of the shipment of large project orders. Sales were higher in the quarters ended in February 2018 and August 2018 due to increased shipments of such orders, while the lower sales amounts for the quarters ended in May 2018, May 2019, August 2019 and November 2019 were due to delays on the shipments of such orders. Sales were higher in the quarters ended in February 2019 and November 2018 due to increased shipments of a large project order in China, but, more significantly, as a result of a large surge in the MRO business. Net earnings[1] for the quarter ended in February 2019 was higher due to an improved sales volume and a more profitable product mix. The net loss[1] for the quarter ended in May 2019 was due to a less profitable product mix partly caused by the shipment of technically complex orders with lower margins. Net earnings[1] for the quarter ended August 2019 was due to a more profitable product mix. The net loss[1] for the quarters ended in August 2018 and November 2018 were largely due to the fact that the North American operations were still below break even and additional costs were incurred in the quarter to meet delivery commitments. The net loss[1] for the quarters ended in February 2018 and May 2018 were due to a less profitable product mix and shipping delays caused by internal operational issues. The quarter ended in February 2018 also had a $4.3 million one-time income tax charge resulting from the U.S. tax reform legislation passed in December 2017. The net loss[1] for the quarter ended in November 2019 is mainly due to additional costs incurred by the Company to execute its restructuring and transformative initiative, V20.

[1] *Net earnings or loss refers to net income or loss attributable to Subordinate and Multiple Voting Shares.*

RESULTS OF OPERATIONS – comparison of three and nine-month periods ended November 30, 2019 and 2018 *(unless otherwise noted, all amounts are in U.S. dollars and all comparisons are to same period in the prior fiscal year)*

Sales

(millions)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Sales	$88.7	$92.3	$258.0	$261.5

Sales decreased by $3.6 million or 3.9% for the quarter and by $3.5 million or 1.3% for the nine-month period. The decrease for the quarter was primarily attributable to the shipment by the North American operations of a large complex Chinese order in the third quarter of the prior fiscal year, which was partially offset this year by an increase in shipments of large project orders in the Company's Italian operations due to a record backlog at the beginning of the year. Sales for the nine-month period were relatively flat as fluctuations in shipments both in France and North America were offset by increased shipments from the Company's Italian operations which continued to deliver the record backlog at the beginning of the year.

Net bookings and backlog

(millions)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Net bookings	$97.2	$100.8	$252.1	$290.4

Bookings decreased by $3.6 million or 3.6% for the quarter and $38.3 million or 13.2% for the nine-month period. The decrease for both periods is due to lower project orders booked by the Company's Italian operations which booked a record of large project orders in the prior year. For the quarter, the decrease is partially offset by higher order bookings in the Company's Indian operations. For the nine-month period, the decrease is also due to lower order bookings by the Company's North American operations which had seen an unusually high surge of non-project valve re-stocking orders from its distributors in the first quarter of the prior fiscal year. MRO distributor orders this fiscal year are expected to reflect a more normalized stock replenishment cycle. As competition remains fierce, the Company is continuing to shift its focus and target discrete market segments where its products enjoy a competitive advantage based upon its good reputation for quality. These conditions provide better pricing power for the Company which should ultimately lead to improved margins.

(millions)	**November 2019**	**February 2019**	**November 2018**
Backlog	$432.1	$449.7	$471.5
For delivery within the next twelve months	$287.0	$299.6	$298.7
For delivery beyond the next twelve months	$145.1	$150.1	$172.9
Percentage – beyond the next twelve months	33.6%	33.4%	36.7%

As a result of sales outpacing bookings in the nine-month period, the Company's book-to-bill ratio was 0.98 for the period. Furthermore, the total backlog decreased by $17.6 million or 3.9% since the beginning of the fiscal year, settling at $432.1 million. The backlog was negatively impacted by the lower book-to-bill ratio and the weakening of the euro spot rate against the U.S. dollar over the course of the nine-month period. The Company's quotation activity has notably increased this year in sectors where margins are healthy, and concurrently decreased in other sectors where the Company experiences the most aggressive competition and where margins are much tighter. The shift is the result of deliberate screening that is expected to take effect gradually as the Company replaces its existing backlog with higher margin orders. The net decrease in bookings experienced in the last nine months, which the Company's plan aims to reverse, must be understood in this context.

Gross profit

(millions)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Gross profit	$22.2	$22.6	$60.2	$59.7
Gross profit percentage	25.0%	24.5%	23.3%	22.8%

Gross profit decreased by $0.4 million for the quarter and increased by $0.5 million for the nine-month period. The gross profit percentage increased by 50 basis points for the quarter and for the nine-month period. The increase in the gross profit percentage in both periods is mainly attributable to a stronger proportion of higher margin product sales and an increased sales volume in the Company's Italian operations, which allowed the subsidiary to cover its fixed costs more efficiently. This increase was partially offset by temporary factors such as a less efficient product mix in the Company's North American operations, including a lower volume of higher margin spare parts sales. Overall, the Company is still delivering a backlog that dates back to the prior fiscal year, which means that the margins do not yet reflect the impact of the margin improvement measures launched in the last quarter under the Company's V20 transformation plan. The combined effect of these measures is expected to gradually take effect in the course of this fiscal year and next year but the greater impact of the Company's restructuring and transformative V20 initiatives is only expected late in fiscal year 2021, when the task of reorganizing and reducing the Company's North American footprint is planned to be completed.

Administration Costs

(millions)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Administration costs*	$21.3	$22.5	$63.7	$66.2
As a percentage of sales	24.0%	24.4%	24.7%	25.3%
*Includes asbestos-related costs of:	$3.6	$2.3	$6.9	$6.0

Administration costs decreased by $1.2 million or 5.3% for the quarter and $2.5 million or 3.8% for the nine-month period. The decrease in administration costs was achieved despite the recording of a $0.9 million provision regarding the settlement of a product claim that was filed against the Company in a prior fiscal year as well as an increase in the costs recognized in connection with the Company's ongoing asbestos litigation (see *Contingencies* section). The fluctuation in asbestos costs for the period is due more to the timing of settlements in these two periods rather than to changes in long-term trends. The reduction in administration costs for both periods is mainly attributable to lower sales commissions as well as the higher freight charges that were incurred in the prior fiscal year in order to air freight a large delayed order.

Like many other U.S. valve manufacturers, two of the Company's U.S. subsidiaries have been named as defendants in a number of pending lawsuits brought on behalf of individuals seeking to recover damages for their alleged asbestos exposure. These lawsuits are related to products manufactured and sold in the past. Management believes that any asbestos was incorporated entirely within the product in such a way that it would not allow for any ambient asbestos during normal operation, inspection or repairs. Management strongly believes its products, which were supplied in accordance with valve industry practice and customer mandated specifications, did not contribute to any asbestos-related illness. The Company will continue to vigorously defend against these claims but given the ongoing course of asbestos litigation in the U.S. and the unpredictability of jury trials, it is not possible to make an estimate of any settlement costs and legal fees.

Net finance costs

(millions)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Net finance costs	$0.7	$0.1	$0.8	$0.7

Net finance costs increased by $0.6 million for the quarter and $0.1 million the nine-month period. While long-term debt is lower compared to the beginning of the year, the Company's overall debt load increased, particularly the bank indebtedness in its North American operations, resulting in an increase in its net finance costs (see *Liquidity and Capital Resources* section). The Company's adoption of IFRS 16 caused a $0.3 million increase for the nine-month period since the Company elected the modified retrospective transition method whereby comparative balances have not been restated.

Income taxes

(in thousands, excluding percentages)	Three-month period ended November 30, 2019		Three-month period ended November 30, 2018	
	$	%	$	%
Income tax at statutory rate of 26.7%	(296)	26.7	41	26.7
Tax effects of:				
Difference in statutory tax rates in foreign jurisdictions	444	(40.1)	509	328.1
Non-deductible (taxable) foreign exchange loss (gain)	(75)	6.8	97	62.6
Losses not tax effected (Losses utilized not previously tax effected)	(154)	13.9	681	439.4
Benefit attributable to a financing structure	(217)	19.6	(222)	(143.2)
Other permanent differences	(102)	9.2	(609)	(392.9)
Provision for (Recovery of) income taxes	(400)	36.1	497	320.7

(in thousands, excluding percentages)	Nine-month period ended November 30, 2019		Nine-month period ended November 30, 2018	
	$	%	$	%
Income tax at statutory rate of 26.7%	(1,755)	26.7	(1,869)	26.7
Tax effects of:				
Difference in statutory tax rates in foreign jurisdictions	811	(12.3)	1,157	(16.5)
Non-deductible foreign exchange loss	347	(5.3)	338	(4.8)
Losses not tax effected (Losses utilized not previously tax effected)	(202)	3.1	1,140	(16.3)
Benefit attributable to a financing structure	(661)	10.1	(673)	9.6
Other permanent differences	92	(1.4)	(529)	7.5
Recovery of income taxes	(1,368)	20.8	(436)	6.2

A separate estimated average annual tax rate is determined for each taxing jurisdiction and applied to their respective interim pre-tax income.

Net loss[1], Operating profit (loss) before restructuring and transformation costs[2] and Adjusted EBITDA[2]

(millions)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Net loss[1]	$(0.8)	$(0.2)	$(5.3)	$(6.4)
As a percentage of sales	(0.9)%	(0.2)%	(2.1)%	(2.4)%
Operating profit (loss) before restructuring and transformation costs[2]	$1.0	$0.2	$(3.3)	$(6.3)
Adjusted EBITDA[2]	$4.3	$3.4	$6.2	$3.3
As a percentage of sales	4.8%	3.7%	2.4%	1.3%

Net loss[1] for the nine-month period amounted to $5.3 million or $0.24 per share compared to $6.4 million or $0.30 per share last year. Net loss[1] for the current nine-month period was significantly impacted by the $2.5 million amount spent on the Company's restructuring and transformative initiative, V20, which aims to improve its operational efficiency and optimize its manufacturing footprint in North America. The Company's current production is being reorganized from four North American plants to three more specialized plants that will be structured to better support the new business units' market strategies. The production of certain non-project valves produced in North America, as well as the less complex project valves are also being transferred to India. Excluding this $2.5 million amount, as well as the after-tax impact of these restructuring and transformation costs incurred during the nine-month period, the Company's net loss[1] would have been $3.5 million compared to $6.4 million last year, representing an improvement of $2.9 million in net loss[1] which is primarily attributable to lower administration costs and an increased gross margin despite the lower sales volume. The Company is estimating $4.0 to $7.0 million of severance costs before taxes for this fiscal 2020 but did not record a provision at the end of the nine-month period ending November 30, 2019 since the plan was not yet finalized at this date. Net loss[1] for the quarter amounted to $0.8 million or $0.04 per share compared to $0.2 million or $0.01 per share last year. Net loss[1] for the current quarter was significantly impacted by the $1.4 million amount spent on the Company's restructuring and transformative initiative, V20. Excluding this $1.4 million amount, as well as the after-tax impact of these restructuring and transformation costs incurred during the quarter, the Company's would have presented net earnings[1] of $0.2 million compared to a net loss[1] of $0.2 million last year, representing an improvement of $0.4 million in net loss[1] which is primarily attributable to lower administration costs partially offset by higher finance costs. Operating loss before restructuring and transformation costs[2] for the nine-month period amounted to $3.3 million compared to $6.3 million last year. Operating profit presents the profitability of a business before taking into account interest and taxes. Adjusted EBITDA[2] for the nine-month period amounted to $6.2 million or $0.29 per share compared to $3.3 million or $0.15 per share last year. Operating profit before restructuring and transformation costs[2] for the quarter amounted to $1.0 million compared to $0.2 million last year. Adjusted EBITDA[2] for the quarter amounted to $4.3 million or $0.20 per share compared to $3.4 million or $0.16 per share last year. The improvement in operating profit or loss before restructuring and transformation costs[2] and adjusted EBITDA[2] for the quarter and the nine-month period is primarily attributable to lowered administration costs and an increase in gross profit percentage, while the operating profit before restructuring and transformation costs[2] and the adjusted EBITDA[2] for the quarter were also negatively impacted by the lower sales volume.

[1] *Net earnings or loss refers to net income or loss attributable to Subordinate and Multiple Voting Shares.*

[2] *Non-IFRS measures – see reconciliations at the end of this report*

LIQUIDITY AND CAPITAL RESOURCES – a discussion of liquidity risk, credit facilities, cash flows and proposed transactions *(unless otherwise noted, all dollar amounts are denominated in U.S. dollars)*

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they come due. The Company manages its liquidity risk by continually monitoring its future cash requirements. Cash flow forecasting is performed in the operating entities and aggregated by the Company's corporate finance team. The Company's policy is to maintain sufficient cash and cash equivalents and available credit facilities in order to meet its present and future operational needs.

The following table presents the Company's financial obligations identified by type and future contractual dates of payment:

(In thousands)					November 30, 2019
	Total $	**Less than 1 year** $	**1 to 3 Years** $	**4 to 5 Years** $	**After 5 years** $
Long-term debt	19,889	7,967	5,459	3,366	3,097
Long-term lease Liabilities	16,020	1,640	2,600	917	10,863
Accounts payable and accrued liabilities	76,449	76,449	-	-	-
Customer deposits	52,634	52,634	-	-	-
Bank indebtedness and short-term bank loans	39,649	39,649	-	-	-
Derivative liabilities	30	30	-	-	-

On November 30, 2019, the Company's order backlog was $432.1 million and its net cash plus unused credit facilities amounted to $99.7 million, which it believes, along with future cash flows generated from operations, is sufficient to meet its financial obligations, increase its capacity, satisfy its working capital requirements, and execute on its business strategy. However, there can be no assurance that the risk of another sharp downturn in the economy will not materially adversely affect the Company's results of operations or financial condition. The Company continues to closely monitor the continued weakness of the price of oil and the euro currency, as well as recent trade protectionist measures and economic sanctions.

As part of managing its liquidity risk, the Company also monitors the financial health of its key customers and suppliers.

Proposed transactions

The Company has not committed to any material asset or business acquisitions or dispositions, other than those already discussed in this MD&A.

Cash flows - comparison of three and nine-month periods ended November 30, 2019 and 2018

(unless otherwise noted, all amounts are in U.S. dollars and all comparisons are to same period in the prior fiscal year)

Net cash

(millions)	November 30, 2019	August 31, 2019	May 31, 2019	February 28, 2019	November 30, 2018	August 31, 2018	May 31, 2018
Net cash	$39.0	$34.9	$39.4	$40.9	$50.0	$51.3	$51.6

The Company's net cash increased by $4.1 million or 11.7% since the beginning of the current quarter and decreased by $1.9 million or 4.6% since the beginning of the current fiscal year. The decrease, which occurred mainly in the first half of the fiscal year, is primarily attributable to investments in property, plant and equipment, land restoration costs related to a property, long-term debt and lease liabilities repayments, as well as distributions to shareholders via dividends, partially offset by cash provided by operating activities and an increase in long-term debt. The increase for the quarter is primarily attributable to cash provided by operating activities, partially offset by investments in property, plant and equipment. Net cash was also negatively impacted by the weakening of the euro spot rate against the U.S. dollar over the course of the quarter and the nine-month period.

Cash provided (used) by operating activities

(millions)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Net cash provided (used) by operating activities	$10.4	$(2,2)	$13.4	$(5.4)

Cash provided by operating activities amounted to $10.4 million for the current quarter compared to cash used by operating activities of $2.2 million in the prior year. The current quarter's source of funds consisted of positive cash net earnings[1] of $2.9 million and positive non-cash working capital movements of $7.5 million. Cash provided by operating activities amounted to $13.4 million for the current nine-month period compared to cash used by operating activities of $5.4 million in the prior year. The current nine-month period's source of funds consisted of positive cash net earnings[1] of $5.3 million and positive non-cash working capital movements of $8.1 million. The non-cash working capital increase for the quarter resulted from the increase in accounts payable and customer deposits partially offset by the increase in accounts receivable, inventories and income taxes recoverable. The non-cash working capital increase for the nine-month period resulted from the decrease in accounts receivable and increase in customer deposits partially offset by the increase in inventories.

Accounts receivable

(millions)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Accounts receivable decrease (increase)	$(4.7)	$4.0	$12.6	$11.0

Accounts receivable balances are a function of the timing of sales and cash collections. The accounts receivable balance decreased since the beginning of the fiscal year due to a combination of lower sales output in both the quarter and nine-month period, coupled with increased collections of prior year accounts in the first quarter of the current fiscal year.

[1] *Net earnings or loss refers to net income or loss attributable to Subordinate and Multiple Voting Shares.*

Inventories

(millions)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Inventory decrease (increase)	$(4.3)	$(2.6)	$(15.3)	$0.5
Customer deposits increase (decrease)	$9.6	$(5.8)	$12.4	$(11.5)

The inventory increase in the quarter is due to the replenishment of stock following large shipments that occurred in prior quarters as well as the build up of inventory in reaction to the booking of certain large project orders. In order to help finance its investment in inventories, the Company, where possible, obtains customer deposits for large orders. Customer deposits increased for the current quarter and nine-month period due to the timing of the booking of certain large project orders, particularly in the Company's French and Italian operations.

Accounts payable and accrued liabilities

(millions)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Accounts payable and accrued liabilities increase	$10.5	$7.5	$1.5	$6.0

The increase in accounts payable and accrued liabilities in the current quarter and nine-month period was primarily related to the timing of payments.

Additions to property, plant and equipment

(millions)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Additions to property, plant and equipment	$5.7	$1.1	$7.4	$6.4

The additions to property, plant and equipment in the quarter include a 2.8M investment, required by the local authorities to re-zone the land of the Company's Korean foundry.

The Company has adopted IFRS 16 at the beginning of the current fiscal year using the modified retrospective transition method whereby the comparative period was not restated. The adoption of the new standard resulted in a $1.5 million increase in additions to property plant and equipment since the beginning of the fiscal year.

Dividends paid and repurchase of shares

(millions)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Dividends paid	$0.5	$0.5	$1.5	$2.6
Repurchase of shares	$0.1	$-	$0.1	$-

The Company changed its dividend policy two fiscal years ago, reducing the dividend from CA$0.10 per share per quarter to CA$0.03 per share per quarter. The new policy took effect starting with the dividend payment of June 29, 2018. The dividend paid in the first quarter of the prior fiscal year was under the prior dividend policy.

The Board of the Company has authorized on October 10, 2019 a normal course issuer bid to purchase for cancellation up to 151,384 Subordinate Voting Shares representing approximately 2.5 % of the outstanding Subordinate Voting Shares of the Company. Following the approval of the Normal Course Issuer Bid by the TSX, the Company repurchased for cancellation a total of 16,900 Subordinate Voting Shares for a cash consideration of $0.1 million over the course of the nine-month period.

Long-term debt

(millions)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Additions to long-term debt	$-	$3.5	$1.1	$4.1
Repayment of long-term debt	$0.6	$0.9	$2.4	$2.7

During the nine-month period, while the Company continued to pay down its outstanding long-term debt, one of its French subsidiaries undertook a new debt issuance to finance its operating activities. Specifically, the Company borrowed $1.1 million (€1.0 million) in form of an unsecured bank loan, bearing interest at 0.30% and repayable in 60 monthly installments, expiring in 2024.

Long-term lease liabilities

(millions)	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Repayment of long-term lease liabilities	$0.5	$-	$1.1	$-

The Company has adopted IFRS 16 at the beginning of the current fiscal year using the modified retrospective transition method whereby the comparative period was not restated. As per the new standard, repayments of the capital portion of lease liabilities are considered financing activities in the statement of cash flow.

FINANCIAL INSTRUMENTS AND FINANCIAL RISK MANAGEMENT

The Company’s activities expose it to a variety of financial risks: market risk (including currency risk, cash flow interest rate risk and fair value interest rate risk), credit risk and liquidity risk. The Company’s overall financial risk management program focuses on mitigating unpredictable financial market risks and their potential adverse effects on the Company’s financial performance.

The Company’s financial risk management is generally carried out by the corporate finance team, based on policies approved by the Board of Directors. The identification, evaluation and hedging of the financial risks are the responsibility of the corporate finance team in conjunction with the finance teams of the Company’s subsidiaries. The Company uses derivative financial instruments to hedge certain risk exposures. Use of derivative financial instruments is subject to a policy which requires that no derivative transaction be entered into for the purpose of establishing a speculative or leveraged position (the corollary being that all derivative transactions are to be entered into for risk management purposes only).

Risk overview

The Company’s financial instruments and the nature of risks which they may be subject to are set out in the following table:

	Risks			
	Market			
Financial instrument	**Currency**	**Interest rate**	**Credit**	**Liquidity**
Cash and cash equivalents	x	x	x	
Short-term investments	x	x	x	
Accounts receivable	x		x	
Derivative assets	x		x	
Bank indebtedness	x	x		x
Short-term bank loans	x	x		x
Accounts payable and accrued liabilities	x			x
Customer deposits	x			x
Dividend payable	x			x
Derivative liabilities	x			x
Long-term debt	x	x		x
Long-term lease liabilities	x	x		x

Market risk

Currency risk

Currency risk on financial instruments is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Company operates internationally and is exposed to foreign exchange risk arising from various currency exposures. Currency risk arises when future commercial transactions and recognized assets and liabilities are denominated in a currency other than a company’s functional currency. The Company has operations with different functional currencies, each of which will be exposed to currency risk based on its specific functional currency.

When possible, the Company matches cash receipts in a foreign currency with cash disbursements in that same currency. The remaining anticipated net exposure to foreign currencies is hedged. To hedge this exposure, the Company uses foreign currency derivatives, primarily foreign exchange forward contracts. These derivatives are not designated as hedges for accounting purposes.

The amounts outstanding as at November 30, 2019 and February 28, 2019 are as follows:

	Range of exchange rates		Gain (loss) (In thousands of U.S. dollars)		Notional amount (In thousands of indicated currency)	
	November 30, 2019	February 28, 2019	November 30, 2019 $	February 28, 2019 $	November 30, 2019	February 28, 2018
Foreign exchange forward contracts						
Sell US$ for CA$ – 0 to 12 months	1.35-1.36	1.36	-	(61)	US$20,250	US$26,000
Buy US$ for CA$ – 0 to 12 months	1.28-1.30	1.30	-	183	US$20,250	US$26,000
Sell US$ for € – 0 to 12 months	-	1.15-1.18	-	(15)	-	US$2,010
Sell € for US$ – 0 to 12 months	1.11-1.15	1.14	(2)	(2)	€4,700	€907
Buy € for US$ – 0 to 12 months	1.09-1.10	-	-	-	€4,700	-
Sell US$ for KW – 0 to 12 months	1,139-1,176	-	(28)	-	US$2,904	-

Foreign exchange forward contracts are contracts whereby the Company has the obligation to sell or buy the currencies at the strike price. The fair value of the foreign currency instruments is recorded in the consolidated statement of income and reflects the estimated amounts the Company would have paid or received to settle these contracts as at the financial position date. Unrealized gains are recorded as derivative assets and unrealized losses as derivative liabilities on the consolidated statement of financial position.

Cash flow and fair value interest rate risk

The Company's exposure to interest rate risk is related primarily to its credit facilities, long-term debt and cash and cash equivalents. Items at variable rates expose the Company to cash flow interest rate risk, and items at fixed rates expose the Company to fair value interest rate risk. The Company's long-term debt and credit facilities predominantly bear interest, and its cash and cash equivalents earn interest at variable rates. An assumed 0.5% change in interest rates would have no significant impact on the Company's net income or cash flows.

Credit risk

Credit risk is the risk of an unexpected loss if a customer or counterparty to a financial instrument fails to meet its contractual obligations. Credit risk arises primarily from the Company's trade accounts receivable.

The Company's credit risk related to its trade accounts receivable is concentrated. As at November 30, 2019, three (February 28, 2019 – four) customers accounted for more than 5% each of its trade accounts receivable, of which one customer accounted for 13.4% (February 28, 2019 – 10.5%), and the Company's ten largest customers accounted for 55.4% (February 28, 2019 – 58.9%) of trade receivables. In addition, there was one (February 28, 2019 – one) customer who accounted for more than 10% of the Company's sales.

In order to mitigate its credit risk, the Company performs a continual evaluation of its customers' credit and performs specific evaluation procedures on all its new customers. In performing its evaluation, the Company analyzes the ageing of accounts receivable, historical payment patterns, customer creditworthiness and current economic trends. A specific credit limit is established for each customer and reviewed periodically. An allowance for doubtful accounts is recorded when, based on management's evaluation, the collection of an account receivable is not reasonably certain.

The Company applies the IFRS 9 simplified approach to measure expected credit losses using a lifetime expected credit loss allowance for trade receivables. The expected credit loss rates are based on the Company's historical credit losses experienced over the last fiscal year prior to period end. The historical rates are then adjusted for current and forward-looking information on macro-economic factors affecting the Company's customers.

For some trade accounts receivable, the Company may obtain security in the form of credit insurance which can be called upon if the counterparty is in default under the terms of the agreement.

The Company is also exposed to credit risk relating to derivative financial instruments, cash and cash equivalents and short-term investments, which it manages by dealing with highly rated financial institutions.

The Company's primary credit risk is limited to the carrying value of the trade accounts receivable and gains on derivative assets.

The table below summarizes the ageing of the trade accounts receivable as at:

(In thousands of U.S. dollars)	**November 30, 2019 $**	**February 28, 2019 $**
Current	65,370	75,888
Past due 0 to 30 days	13,145	13,329
Past due 31 to 90 days	14,907	15,860
Past due more than 90 days	22,381	26,845
	115,803	131,922
Less: Allowance for doubtful accounts	1,263	1,662
Trade accounts receivable	114,540	130,260
Other receivables	10,466	7,260
Total accounts receivable	125,006	137,520

The table below summarizes the movement in the allowance for doubtful accounts:

(In thousands of U.S. dollars)	**November 30, 2019 $**	**November 30, 2018 $**
Balance – Beginning of the year	1,662	1,088
Bad debt expenses	292	391
Recoveries of trade accounts receivable	(447)	(40)
Write-off of trade accounts receivable	(233)	(193)
Foreign exchange	(11)	(52)
Balance – End of the period	1,263	1,194

Liquidity risk – see discussion in *liquidity and capital resources* section

CONTINGENCIES (in thousands of U.S. dollars, excluding number of cases)

Two of the Company's U.S. subsidiaries have been named as one of the defendants in a number of pending lawsuits that seek to recover damages for personal injury allegedly caused by exposure to asbestos-containing products manufactured and sold in the past. Management believes it has a strong defence related to certain products that may have contained an internal asbestos containing component. 1,514 claims were outstanding at the end of the reporting period (February 28, 2019 – 1,349). These claims were filed in the states of Arizona, California, Connecticut, District of Columbia, Delaware, Florida, Georgia, Hawaii, Illinois, Louisiana, Maine, Maryland, Massachusetts, Michigan, Missouri, Montana, New Jersey, New York, North Carolina, Pennsylvania, Rhode Island, South Carolina, Texas, Virginia, Washington and West Virginia. During the reporting period, the Company resolved 324 claims (November 30, 2018 – 313) and was the subject of 489 new claims (November 30, 2018 – 434). Because of the many uncertainties inherent in predicting the outcome of these proceedings, as well as the course of asbestos litigation in the United States, management believes that it is not possible to make an estimate of the Company's asbestos liability. Accordingly, no provision has been set up in the accounts. Settlement costs and legal fees related to these asbestos claims amounted to $3,601 for the quarter (November 30, 2018 - $2,311) and $6,944 (November 30, 2018 - $6,027) for the nine-month period.

On December 3, 2014, San Diego Gas & Electric Company ("SDG") filed a claim against Velan Valve Corp., a wholly-owned subsidiary of the Company, in the Superior Court of the State of California, concerning high pressure valves supplied to SDG and installed at its Palomar Energy Center ("Facility"). This lawsuit alleged damages to the Facility in excess of $9,000 related to allegedly defective valves supplied by Velan Valve Corp. The claim was for alleged strict product liability and alleged negligence. The Company vigorously defended its position and undertook all actions necessary to protect its reputation. During the nine-month period ended November 30, 2019, the Company made a final settlement of this case and recorded a net settlement of $850.

OFF-BALANCE SHEET ARRANGEMENTS

There have been no material changes from those identified in the annual MD&A.

RELATED PARTY TRANSACTIONS (in thousands of U.S. dollars)

The Company has entered into the following transactions with related parties, which are measured at their exchange value.

a) PDK Machine Shop Ltd. ("PDK") is a company owned by certain relatives of the controlling shareholder. PDK is a supplier of machined material components for use in the Company's plants.

	Three-month period ended November 30		Nine-month period ended November 30	
	2019	2018	2019	2018
Purchases of material components	$384	$163	$575	$757

The Company entered into an agreement with PDK pursuant to which it has the right to purchase the shares of PDK for a consideration equal to the book value thereof in the event that they propose to sell their shares to a third party. In the event that PDK proposes to sell all or substantially all of its assets to a third party, the Company has the right to purchase inventory at cost and other assets at book value. In the event of a proposed liquidation or sale of sufficient assets such that PDK cannot fulfill its obligations to the Company under any outstanding purchase orders, the Company also has the right and the obligation to purchase PDK's inventory at an amount equal to the cost thereof. The maximum obligation of the Company pursuant to such put right is $200.

INTERNAL CONTROLS AND PROCEDURES

The Company's Chief Executive Officer and Chief Financial Officer have designed disclosure controls and procedures in order to provide reasonable assurance that the information presented in the Company's interim and annual report is accumulated and communicated to management on a timely basis so that appropriate decisions can be made in terms of disclosures.

Internal controls over financial reporting (ICFR) has also been designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with IFRS.

The Company did not make any changes to the design of internal controls over financial reporting during the nine-month period ended November 30, 2019 that have materially affected, or are reasonably likely to materially affect, the Company's internal controls over financial reporting.

CRITICAL ACCOUNTING ESTIMATES & JUDGEMENTS

The Company's financial statements are prepared in accordance with IFRS as issued by the IASB. The Company's significant accounting policies as described in note 2 and 3 of the Company's audited consolidated financial statements are essential to understanding the Company's financial positions, results of operations and cash flows. Certain of these accounting policies require critical accounting estimates that involve complex and subjective judgments and the use of assumptions, some of which may be for matters that are inherently uncertain and susceptible to change. The assumptions and estimates used are based on parameters which are derived from the knowledge at the time of preparing the financial statements and believed to be reasonable under the circumstances. In particular, the circumstances prevailing at this time and assumptions as to the expected future development of the global and industry-specific environment were used to estimate the Company's future business performance. Where these conditions develop differently than assumed and beyond the control of the Company, the actual results may differ from those anticipated (see *Forward-looking information* section above). These estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is changed. There were no significant changes made to critical accounting estimates during the past two fiscal years.

There have been no material changes from those identified in the annual MD&A.

ACCOUNTING STANDARDS AND AMENDMENTS ADOPTED IN THE PERIOD

(i) In January 2016, the IASB issued IFRS 16, *Leases*, which sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract. It eliminates the classification of leases as either operating leases or finance leases and introduces a single lessee accounting model for lessees. It substantially carries forward the lessor accounting requirements. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. IFRS 16 replaces IAS 17, *Leases*, IFRIC 4, *Determining whether an Arrangement contains a Lease*, SIC-15, *Operating Leases – Incentives*, and SIC-27, *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*.

The new standard was adopted effective March 1, 2019 and the Company elected the modified retrospective transition method on the effective date, without restatement of the comparative figures. As such, comparative information continues to be reported under previous accounting standards.

At inception of a contract, the Company assesses whether a contract is, or contains, a lease based on whether the contract includes the right to control the use of an identified asset for a period of time in exchange for consideration.

In situations where the Company is a lessee, the result is the recording, at the lease commencement date, of a right-of-use asset and a lease liability for the present value of the future lease payments on the statement of financial position for most of its contracts that were considered operating leases under IAS 17. In order to determine the present value of the future lease payments, the Company uses the interest rate implicit in the lease or, if that rate cannot be readily determined, the Company uses the incremental borrowing rate of each of its subsidiaries. The Company depreciates its right-of-use asset on the lesser of the lease term or the useful life of the asset using the straight-line method since it closely reflects the expected pattern of consumption of the future economic benefits.

The right-of-use asset may be periodically reduced by impairment losses, if any, and adjusted for certain remeasurement of the lease liability. The lease liability is measured at amortized cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index, rate or estimate. The lease liability is remeasured with a corresponding adjustment to the carrying value of the right-of use asset. If the carrying value of the right-of-use asset has been reduced to zero, the remaining adjustment is recorded in the statement of income (loss).

Cash payments for the principal portion of the lease liability are presented within the financial activities and the interest portion of the lease liability is presented within the operating activities of the statement of cash flows. Payments associated with short-term leases and leases of low-value assets are not included in the measurement of the lease liability and are presented in operating activities in the statement of cash flows.

At the date of initial application, the Company elected to measure the right-of-use asset in an amount equal to the lease liability. The Company also applied the following practical expedients when applying IFRS 16 to leases previously classified as operating leases under IAS 17:

a) The Company elected to apply the standard to contracts that were previously identified as leases under IAS 17 and IFRIC 4 and elected to not apply the standard to contracts that were not previously identified as leases under IAS 17 and IFRIC 4.
b) The Company has elected to exclude intangible assets from the scope of this standard.
c) The Company used the exemptions proposed by the standard on lease contracts for which the lease terms end within 12 months as the date of initial application, and lease contracts for which the underlying asset is of low value.
d) The Company used hindsight to determine the lease terms if the contract contained options to extend or terminate the lease term.

The following table reconciles the Company's operating lease obligations at February 28, 2019 to the lease liabilities recognized on initial application of IFRS 16 at March 1, 2019.

Operating Lease Commitments disclosed as at February 28, 2019	**15,763**
Discounted using the lessee's weighted average incremental borrowing rate of 2.49% at the date of initial application	(4,249)
Less: Short-term leases and low-value leases recognized on a straight-line basis as an expense	(331)
Add: Adjustments as a result of a different treatment of extension and termination options	3,980
Lease liability recognized as at March 1, 2019	**15,163**
Of which are:	
Current portion of long-term lease liabilities	1,290
Long-term lease liabilities	13,873

The recognized right-of-use assets relate to the following types of assets:

	As at November 30, 2019 $	As at March 1, 2019 $
Land	6,678	6,528
Buildings	7,168	7,150
Furniture & Fixtures	217	48
Data Processing Equipment	164	241
Rolling Stock	1,617	1,196
Total Right of use asset	15,844	15,163

The following table summarizes the impact of adopting IFRS 16 on the Company's consolidated statement of financial position as at March 1, 2019. Prior amounts have not been restated. The Company's transition to IFRS 16 did not impact the Company's retained earnings.

	February 28, 2019 $	Adjustment due to IFRS 16 $	March 1, 2019 $
Non-current assets			
Property, Plant and Equipment	83,537	15,163	98,700
Current liabilities			
Current portion of long-term lease liabilities	-	1,290	1,290
Non-current liabilities			
Long-term lease liabilities	-	13,873	13,873

(ii) In June 2017, IFRIC issued IFRIC 23, *Uncertainty over Income Tax Treatments*. This interpretation clarifies how the recognition and measurement requirements of IAS 12, *Income Taxes*, are applied where there is uncertainty over income tax treatments that have yet to be accepted by tax authorities.

The Company has adopted the interpretation of IFRIC 23 on March 1, 2019 and concluded that it has no impact on previously reported results.

CERTAIN RISKS THAT COULD AFFECT OUR BUSINESS

There have been no material changes from those identified in the annual MD&A.

SUMMARY OF RESULTS

Summary financial data derived from the Company’s financial statements prepared in accordance with IFRS for the three most recently completed reporting periods are as follows:

For the reporting periods ended on the following dates
(in thousands of U.S. dollars, excluding number of shares and per share amounts)

	Fiscal year ended February 28, 2019	Fiscal year ended February 28, 2018	Fiscal year ended February 28, 2017
Operating Data			
Sales	$366,865	$337,963	$331,777
Net Earnings (loss)[1]	(4,882)	(17,811)	7,737
Earnings (loss) per Share			
- Basic	(0.23)	(0.82)	0.36
- Diluted	(0.23)	(0.82)	0.36
Balance Sheet Data			
Total Assets	524,357	540,193	519,297
Total Long-Term Financial Liabilities	21,723	22,200	22,532
Shareholder Data			
Cash dividends per share			
- Multiple Voting Shares[2]	0.09	0.31	0.31
- Subordinate Voting Shares	0.09	0.31	0.31
Outstanding Shares at report date			
- Multiple Voting Shares[2]	15,566,567		
- Subordinate Voting Shares	6,055,368		

Sales for fiscal year 2019 increased by 8.6% compared to fiscal year 2018. This increase was primarily attributable to an increase in shipments from the Company’s North American, Korean and Indian subsidiaries, which were partially offset by decreased shipments from the Company’s German operations. The Company was able to notably improve its MRO business as well as increasing its shipments related to large project orders. Sales for fiscal year 2018 increased by 1.9% compared to fiscal year 2017. This increase was primarily attributable to an increase in shipments from the Company’s Italian subsidiary, which were offset by decreased shipments from the Company’s North American operations. Delays in shipments of certain large project orders caused by various customer-related, supply chain and internal operational issues, and lower shipments of non-project valves negatively impacted the Company’s North American operations in fiscal year 2018.

Gross profit for fiscal year 2019 amounted to $85.6 million, an increase of $14.7 million from fiscal year 2018, while the gross profit percentage increased from the 21.0% reported in fiscal year 2018 to 23.3% in fiscal year 2019. This increase was due primarily to the higher sales volume achieved by the Company’s North American, Korea and Indian operations combined with the shipment of a more efficient product mix by the Company’s French operations, which was partially offset by the lower sales volume shipped by the Company’s German operations. Gross profit for fiscal year 2018 amounted to $70.9 million, a decrease of $17.6 million from fiscal year 2017, while the gross profit percentage decreased from the 26.7% reported in fiscal year 2017 to 21.0% in fiscal year 2018. This decrease was due primarily to the Company’s North American operations, which shipped a product mix with a greater proportion of projects with lower margins, coupled with pricing pressures brought on by fierce competition and continued weakness in certain markets, which was only partially offset by material cost savings.

Administration costs for fiscal year 2019 increased by $5.6 million when compared to fiscal year 2018. This fluctuation was attributable to an increase in bad debt expense, selling expenses, retirement expenses and freight charges for certain overseas project customers resulting from the higher sales volume as well as the need to incur air freight costs on a large delayed order. The Company had also invested $1.0 million in anticipation of its current transformation initiative, Velocity 2020. The Company also experienced an increase in costs recognized in connection with the Company’s ongoing asbestos litigation (see *Contingencies* section). Administration costs for fiscal year 2018 increased by $11.8 million when compared to fiscal year 2017. This increase was primarily attributable to an increase in sales commissions and freight charges due to the increased sales volume, an increase in technology license fees paid on the sale of certain highly-engineered cryogenic valves, and an increase in costs recognized in connection with the Company’s ongoing asbestos litigation (see *Contingencies* section).

The fiscal year 2018 net loss[1] was also negatively impacted by a $4.3 million one-time income tax charge due to the U.S. tax reform legislation passed in December 2017.

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[1] *Net earnings or loss refers to net income or loss attributable to Subordinate and Multiple Voting Shares.*

[2] *Multiple Voting Shares (five votes per share) are convertible into Subordinate Voting Shares on a 1 to 1 basis.*

RECONCILIATIONS OF NON-IFRS MEASURES

In this MD&A, the Company presented measures of performance or financial condition which are not defined under IFRS ("non-IFRS measures") and are therefore unlikely to be comparable to similar measures presented by other companies. These measures are used by management in assessing the operating results and financial condition of the Company and are reconciled with the performance measures defined under IFRS. Reconciliations of these amounts can be found below.

Operating profit (loss) before restructuring and transformation costs and Adjusted net earnings (loss) before interest, taxes, depreciation and amortization ("EBITDA")

	Three-month period ended November 30, 2019	Three-month period ended November 30, 2018	Nine-month period ended November 30, 2019	Nine-month period ended November 30, 2018
Operating profit (loss)	(0.4)	0.2	(5.7)	(6.3)
Adjustment for:				
Restructuring and transformation costs	1.4	-	2.5	-
Operating profit (loss) before restructuring and transformation costs	**1.0**	**0.2**	**(3.2)**	**(6.3)**
Net loss[1]	(0.8)	(0.2)	(5.3)	(6.4)
Adjustments for:				
Depreciation of property, plant and equipment	2.9	2.6	8.1	8.1
Amortization of intangible assets	0.5	0.4	1.5	1.3
Finance costs – net	0.7	0.1	0.8	0.7
Income taxes	(0.4)	0.5	(1.4)	(0.4)
EBITDA	**2.9**	**3.4**	**3.7**	**3.3**
Adjustment for:				
Restructuring and transformation costs	1.4	-	2.5	-
Adjusted EBITDA	**4.3**	**3.4**	**6.2**	**3.3**

The term "operating profit or loss before restructuring and transformation costs" is defined as operating profit or loss plus restructuring and transformation costs. The Company opted to not adjust the prior year figures due to the different nature of the expenses, which were more related to the assessment of the required restructuring and transformation plan rather than the execution of the plan itself. The forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement.

The term "adjusted EBITDA" is defined as net income or loss attributable to Subordinate and Multiple Voting Shares plus restructuring and transformation costs, depreciation of property, plant & equipment, plus amortization of intangible assets, plus net finance costs plus income tax provision. The Company opted to not adjust the prior year figures due to the different nature of the expenses, which were more related to the assessment of the required restructuring and transformation plan rather than the execution of the plan itself. The forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement.

[1] *Net earnings or loss refers to net income or loss attributable to Subordinate and Multiple Voting Shares.*

Velan Inc.

Unaudited Condensed Interim Consolidated Financial Statements
For the three-month and nine-month periods ended November 30, 2019

Notice of no auditor review of Interim Consolidated Financial Statements
In accordance with National Instrument 51-102 released by the Canadian Securities Administrators, the Company discloses that its auditor PricewaterhouseCoopers LLP have not reviewed the unaudited condensed interim consolidated financial statements for the three-month and nine-month periods ended November 30, 2019

Velan Inc.

Condensed Interim Consolidated Statements of Financial Position

(Unaudited)
(in thousands of U.S. dollars)

As At	November 30, 2019 $	February 28, 2019 $
Assets		
Current assets		
Cash and cash equivalents	77,143	70,673
Short-term investments	89	658
Accounts receivable	125,006	137,520
Income taxes recoverable	17,606	16,863
Inventories (note 7)	180,923	165,583
Deposits and prepaid expenses	4,422	4,612
Derivative assets	-	189
	405,189	396,098
Non-current assets		
Property, plant and equipment (note 3)	98,843	83,537
Intangible assets and goodwill	16,357	18,146
Deferred income taxes	24,667	25,947
Other assets	528	629
	140,395	128,259
Total assets	545,584	524,357
Liabilities		
Current liabilities		
Bank indebtedness	38,115	29,807
Short-term bank loans	1,534	2,172
Accounts payable and accrued liabilities	76,450	74,910
Income taxes payable	828	495
Dividend payable	501	497
Customer deposits	52,634	40,240
Provisions	7,215	8,494
Accrual for performance guarantees	21,510	23,014
Derivative liabilities	30	83
Current portion of long-term debt	7,967	8,609
Current portion of long-term lease liabilities (note 3)	1,640	-
	208,424	188,321
Non-current liabilities		
Long-term debt	11,922	13,242
Long-term lease liabilities (note 3)	14,380	-
Income taxes payable	1,576	1,742
Deferred income taxes	3,310	3,738
Other liabilities	8,592	8,481
	39,780	27,203
Total liabilities	248,204	215,524
Equity		
Equity attributable to the Subordinate and Multiple Voting shareholders		
Share capital (note 8)	72,906	73,090
Contributed surplus	6,170	6,074
Retained earnings	247,871	254,606
Accumulated other comprehensive loss	(33,571)	(28,990)
	293,376	304,780
Non-controlling interest	4,004	4,053
Total equity	297,380	308,833
Total liabilities and equity	545,584	524,357

Commitments and contingencies (note 9)

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

Velan Inc.

Condensed Interim Consolidated Statements of Loss

(Unaudited)

(in thousands of U.S. dollars, excluding number of shares and per share amounts)

	Three-month periods ended November 30		Nine-month periods ended November 30	
	2019	**2018**	**2019**	**2018**
	$	**$**	**$**	**$**
Sales	88,701	92,271	257,984	261,520
Cost of sales (note 7)	66,548	69,622	197,755	201,791
Gross profit	22,153	22,649	60,229	59,729
Administration costs	21,275	22,467	63,659	66,151
Restructuring and transformation costs (note 14)	1,406	-	2,480	-
Other income	(118)	(63)	(171)	(87)
Operating profit (loss)	(410)	245	(5,739)	(6,335)
Finance income	135	131	870	493
Finance costs	833	221	1,709	1,165
Finance costs – net	(698)	(90)	(839)	(672)
Income (Loss) before income taxes	(1,108)	155	(6,578)	(7,007)
Provision for (Recovery of) income taxes	(400)	497	(1,368)	(436)
Net loss for the period	(708)	(342)	(5,210)	(6,571)
Net income (loss) attributable to:				
Subordinate Voting Shares and Multiple Voting Shares	**(819)**	**(236)**	**(5,274)**	**(6,401)**
Non-controlling interest	111	(106)	64	(170)
	(708)	(342)	(5,210)	(6,571)
Net loss per Subordinate and Multiple Voting Share				
Basic	(0.04)	(0.01)	(0.24)	(0.30)
Diluted	(0.04)	(0.01)	(0.24)	(0.30)
Dividends declared per Subordinate and Multiple Voting Share	0.02 (CA$0.03)	0.02 (CA$0.03)	0.07 (CA$0.09)	0.07 (CA$0.09)
Total weighted average number of Subordinate and Multiple Voting Shares				
Basic	21,617,207	21,621,935	21,616,543	21,621,935
Diluted	21,617,207	21,621,935	21,616,543	21,621,935

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

Velan Inc.

Condensed Interim Consolidated Statements of Comprehensive Loss

(Unaudited)
(in thousands of U.S. dollars)

	Three-month periods ended November 30		Nine-month periods ended November 30	
	2019 **$**	**2018** **$**	**2019** **$**	**2018** **$**
Comprehensive loss				
Net loss for the period	(708)	(342)	(5,210)	(6,571)
Other comprehensive loss				
Foreign currency translation adjustment on foreign operations whose functional currency is other than the reporting currency (U.S. dollar)	(124)	(2,454)	(4,694)	(9,276)
Comprehensive loss	(832)	(2,796)	(9,904)	(15,847)
Comprehensive income (loss) attributable to:				
Subordinate Voting Shares and Multiple Voting Shares	(1,002)	(2,682)	(9,855)	(15,582)
Non-controlling interest	170	(114)	(49)	(265)
	(832)	(2,796)	(9,904)	(15,847)

Other comprehensive income (loss) is composed solely of items that may be reclassified subsequently to the consolidated statement of income (loss).

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

Velan Inc.

Condensed Interim Consolidated Statements of Changes in Equity

(Unaudited)

(in thousands of U.S. dollars, excluding number of shares)

	Equity attributable to the Subordinate and Multiple Voting shareholders							
	Number of shares	Share capital	Contributed surplus	Accumulated other comprehensive loss	Retained earnings	Total	Non-controlling interest	Total equity
Balance - February 28, 2019	21,621,935	73,090	6,074	(28,990)	254,606	304,780	4,053	308,833
Net income (loss) for the period	-	-	-	-	(5,274)	(5,274)	64	(5,210)
Other comprehensive loss	-	-	-	(4,581)	-	(4,581)	(113)	(4,694)
	21,621,935	73,090	6,074	(33,571)	249,332	294,925	4,004	298,929
Effect of share-based compensation (note 8 (d))	-	-	2	-	-	2	-	2
Share repurchase (note 8 (c))	(16,900)	(184)	94	-	-	(90)	-	(90)
Dividends								
Multiple Voting Shares	-	-	-	-	(1,048)	(1,048)	-	(1,048)
Subordinate Voting Shares	-	-	-	-	(413)	(413)	-	(413)
Balance - November 30, 2019	21,605,035	72,906	6,170	(33,571)	247,871	293,376	4,004	297,380
Balance - February 28, 2018	21,621,935	73,090	6,057	(19,790)	256,668	316,025	5,592	321,617
Adjustment related to the transition to IFRS 15	-	-	-	-	4,741	4,741	-	4,741
Adjusted balance - March 1, 2018	21,621,935	73,090	6,057	(19,790)	261,409	320,766	5,592	326,358
Net loss for the period	-	-	-	-	(6,401)	(6,401)	(170)	(6,571)
Other comprehensive income	-	-	-	(9,181)	-	(9,181)	(95)	(9,276)
	21,621,935	73,090	6,057	(28,971)	255,008	305,184	5,327	310,511
Effect of share-based compensation (note 8 (d))	-	-	13	-	-	13	-	13
Dividends								
Multiple Voting Shares	-	-	-	-	(1,044)	(1,044)	-	(1,044)
Subordinate Voting Shares	-	-	-	-	(389)	(389)	-	(389)
Non-controlling interest	-	-	-	-	-	-	(927)	(927)
Balance - Novembre 30, 2018	21,621,935	73,090	6,070	(28,971)	253,575	303,764	4,400	308,164

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

Velan Inc.

Condensed Interim Consolidated Statements of Cash Flow

(Unaudited)
(in thousands of U.S. dollars)

	Three-month periods ended November 30		Nine-month periods ended November 30	
	2019 **$**	**2018** **$**	**2019** **$**	**2018** **$**
Cash flows from				
Operating activities				
Net loss for the period	(708)	(342)	(5,210)	(6,571)
Adjustments to reconcile net loss to cash provided (used) by operating activities (note 10)	3,590	2,676	10,503	9,679
Changes in non-cash working capital items (note 11)	7,536	(4,519)	8,080	(8,499)
Cash provided (used) by operating activities	10,418	(2,185)	13,373	(5,391)
Investing activities				
Short-term investments	2,207	11	569	500
Additions to property, plant and equipment	(5,711)	(1,111)	(7,425)	(6,401)
Additions to intangible assets	(175)	(13)	(308)	(112)
Proceeds on disposal of property, plant and equipment, and intangible assets	109	19	148	144
Net change in other assets	(156)	18	(1,484)	596
Cash used by investing activities	(3,726)	(1,076)	(8,500)	(5,273)
Financing activities				
Dividends paid to Subordinate and Multiple Voting shareholders	(495)	(484)	(1,457)	(2,614)
Dividends paid to non-controlling interest	-	-	-	(927)
Repurchase of shares (note 8 (c))	(90)	-	(90)	-
Short-term bank loans	(146)	426	(638)	1,411
Increase in long-term debt	-	3,509	1,122	4,116
Repayment of long-term debt	(579)	(857)	(2,438)	(2,787)
Repayment of long-term lease liabilities (note 3)	(485)	-	(1,143)	-
Cash provided (used) by financing activities	(1,795)	2,594	(4,644)	(801)
Effect of exchange rate differences on cash	(779)	(711)	(2,067)	(3,122)
Net change in cash during the period	4,118	(1,378)	(1,838)	(14,587)
Net cash – Beginning of the period	34,910	51,334	40,866	64,543
Net cash – End of the period	39,028	49,956	39,028	49,956
Net cash is composed of:				
Cash and cash equivalents	77,143	68,450	77,143	68,450
Bank indebtedness	(38,115)	(18,494)	(38,115)	(18,494)
	39,028	49,956	39,028	49,956
Supplementary information				
Interest received (paid)	(480)	52	(938)	(116)
Income taxes paid	(1,025)	(4,422)	(4,532)	(8,776)

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

For the three-month and nine-month periods ended November 30, 2019

1 General information

These unaudited condensed interim financial statements represent the consolidation of the accounts of Velan Inc. (the "Company") and its subsidiaries. The Company is an international manufacturer of industrial valves and is a public company listed on the Toronto Stock Exchange under the symbol "VLN". It was incorporated under the name Velan Engineering Ltd. on December 12, 1952 and continued under the *Canada Business Corporations Act* on February 11, 1977. It changed its name to Velan Inc. on February 20, 1981. Velan Inc. maintains its registered head office at 7007 Cote de Liesse, Montreal, Quebec, Canada, H4T 1G2. The Company's ultimate parent company is Velan Holdings Co. Ltd.

These unaudited condensed interim consolidated financial statements were approved for issue by the Company's Board of Directors on January 9, 2020. The Company's auditors have not performed a review of these unaudited condensed interim consolidated financial statements.

2 Basis of preparation

These unaudited condensed interim consolidated financial statements for the three-month and nine-month periods ended November 30, 2019 have been prepared in accordance with International Financial Reporting Standards ("IFRS") in accordance with International Accounting Standard ("IAS") 34, *Interim Financial Reporting*. Except as disclosed in Note 3 below, these unaudited condensed interim consolidated financial statements have been prepared using the same basis of presentation, accounting policies, and methods of computation as outlined in Note 2, *Summary of significant accounting policies*, in the Company's annual consolidated financial statements for the year ended February 28, 2019, which have also been prepared in accordance with IFRS. Accordingly, these unaudited condensed interim consolidated financial statements should be read in conjunction with the Company's annual consolidated financial statements for the year ended February 28, 2019.

3 Changes in accounting policies

(i) In January 2016, the IASB issued IFRS 16, *Leases*, which sets out the principles for the recognition, measurement, presentation and disclosure of leases for both parties to a contract. It eliminates the classification of leases as either operating leases or finance leases and introduces a single lessee accounting model for lessees. It substantially carries forward the lessor accounting requirements. Accordingly, a lessor continues to classify its leases as operating leases or finance leases, and to account for those two types of leases differently. IFRS 16 replaces IAS 17, *Leases*, IFRIC 4, *Determining whether an Arrangement contains a Lease*, SIC-15, *Operating Leases – Incentives*, and SIC-27, *Evaluating the Substance of Transactions Involving the Legal Form of a Lease*.

The new standard was adopted effective March 1, 2019 and the Company elected the modified retrospective transition method on the effective date, without restatement of the comparative figures. As such, comparative information continues to be reported under previous accounting standards.

At inception of a contract, the Company assesses whether a contract is, or contains, a lease based on whether the contract includes the right to control the use of an identified asset for a period of time in exchange for consideration.

In situations where the Company is a lessee, the result is the recording, at the lease commencement date, of a right-of-use asset and a lease liability for the present value of the future lease payments on the statement of financial position for most of its contracts that were considered operating leases under IAS 17. In order to determine the present value of the future lease payments, the Company uses the interest rate implicit in the lease or, if that rate cannot be readily determined, the Company uses the incremental borrowing rate of each of its subsidiaries. The Company depreciates its right-of-use asset on the lesser of the lease term or the useful life of the asset using the straight-line method since it closely reflects the expected pattern of consumption of the future economic benefits.

(in thousands of U.S. dollars, excluding number of shares and per share amounts)

The right-of-use asset may be periodically reduced by impairment losses, if any, and adjusted for certain remeasurement of the lease liability. The lease liability is measured at amortized cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index, rate or estimate. The lease liability is remeasured with a corresponding adjustment to the carrying value of the right-of use asset. If the carrying value of the right-of-use asset has been reduced to zero, the remaining adjustment is recorded in the statement of income (loss).

Cash payments for the principal portion of the lease liability are presented within the financial activities and the interest portion of the lease liability is presented within the operating activities of the statement of cash flows. Payments associated with short-term leases and leases of low value assets are not included in the measurement of the lease liability and are presented in operating activities in the statement of cash flows.

At the date of initial application, the Company elected to measure the right-of-use asset in an amount equal to the lease liability. The Company also applied the following practical expedients when applying IFRS 16 to leases previously classified as operating leases under IAS 17:

a) The Company elected to apply the standard to contracts that were previously identified as leases under IAS 17 and IFRIC 4 and elected to not apply the standard to contracts that were not previously identified as leases under IAS 17 and IFRIC 4.
b) The Company has elected to exclude intangible assets from the scope of this standard.
c) The Company used the exemptions proposed by the standard on lease contracts for which the lease terms end within 12 months as the date of initial application, and lease contracts for which the underlying asset is of low value.
d) The Company used hindsight to determine the lease terms if the contract contained options to extend or terminate the lease term.

The following table reconciles the Company’s operating lease obligations at February 28, 2019 to the lease liabilities recognized on initial application of IFRS 16 at March 1, 2019.

Operating Lease Commitments disclosed as at February 28, 2019	**15,763**
Discounted using the lessee's weighted average incremental borrowing rate of 2.49% at the date of initial application	(4,249)
(Less): Short-term leases and low-value leases recognized on straight-line basis as expense	(331)
Add: Adjustments as a result of a different treatment of extension and termination options	3,980
Lease liability recognized as at March 1, 2019	**15,163**
Of which are:	
Current portion of long-term lease liabilities	1,290
Long-term lease liabilities	13,873

(in thousands of U.S. dollars, excluding number of shares and per share amounts)

The recognized right-of-use assets relate to the following types of assets:

	As at November 30, 2019 $	As at March 1, 2019 $
Land	6,678	6,528
Buildings	7,168	7,150
Furniture & Fixtures	217	48
Data Processing Equipment	164	241
Rolling Stock	1,617	1,196
Total Right of use asset	15,844	15,163

The following table summarizes the impact of adopting IFRS 16 on the Company's consolidated statement of financial position as at March 1, 2019. Prior amounts have not been restated. The Company's transition to IFRS 16 did not impact the Company's retained earnings.

	February 28, 2019 $	Adjustment due to IFRS 16 $	March 1, 2019 $
Non-current assets			
Property, Plant and Equipment	83,537	15,163	98,700
Current liabilities			
Current portion of long-term lease liabilities	-	1,290	1,290
Non-current liabilities			
Long-term lease liabilities	-	13,873	13,873

(ii) In June 2017, IFRIC issued IFRIC 23, *Uncertainty over Income Tax Treatments*. This interpretation clarifies how the recognition and measurement requirements of IAS 12, *Income Taxes*, are applied where there is uncertainty over income tax treatments that have yet to be accepted by tax authorities.

The Company has adopted the interpretation of IFRIC 23 on March 1, 2019 and concluded that it has no impact on previously reported results.

4 Critical accounting estimates and judgements

The preparation of interim financial statements requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expense. Actual results may differ from these estimates.

In preparing these unaudited condensed interim consolidated financial statements, the significant judgements made by management in applying the Company's accounting policies and the key sources of estimation uncertainty were the same, with the exception of the restructuring and transformation costs disclosed in note 14, as those that applied to the annual consolidated financial statements for the year ended February 28, 2019.

(in thousands of U.S. dollars, excluding number of shares and per share amounts)

5 Seasonality

The Company’s sales are not subject to seasonality. Quarterly sales can vary greatly based on the timing of revenue recognition on large project orders.

6 Operating segment information

Consistent with the prior fiscal year, the Company reflects its results under a single reportable operating segment.

7 Inventories

	November 30, 2019 $	February 28, 2019 $
Raw materials	33,452	35,858
Work in process and finished parts	110,473	96,863
Finished goods	36,998	32,862
	180,923	165,583

As a result of variations in the ageing of its inventories, the Company recognized a net additional inventory provision for the nine-month period ended November 30, 2019 of $3,365 (November 30, 2018 – $1,514), including reversals of $3,252 (November 30, 2018 - $5,795). The Company recognized a net additional inventory provision for the three-month period ended November 30, 2019 of $518 (November 30, 2018 – $330), including reversals of $1,695 (November 30, 2018 - $2,913).

8 Capital stock

a) Authorized – in unlimited number
Preferred Shares, issuable in series
Subordinate Voting Shares
Multiple Voting Shares (five votes per share), convertible into Subordinate Voting Shares

b) Issued

	November 30, 2019 $	February 28, 2019 $
6,038,468 Subordinate Voting Shares (February 28, 2019 – 6,055,368) (notes 8 (c) and 8(d))	65,780	65,964
15,566,567 Multiple Voting Shares	7,126	7,126
	72,906	73,090

(in thousands of U.S. dollars, excluding number of shares and per share amounts)

c) Pursuant to its Normal Course Issuer Bid, the Company is entitled to repurchase for cancellation a maximum of 151,384 of the issued Subordinate Voting Shares of the Company, representing approximately 2.5% of the issued shares of such class as at October 10, 2019, during the ensuing 12-month period ending October 22, 2020. During the three-month and nine-month periods ended November 30, 2019, 16,900 (November 30, 2018 – nil) Subordinate Voting Shares were purchased for a cash consideration of $90 (November 30, 2018 - nil) and cancelled.

d) The Company established a fixed share option plan (the "Share Option Plan") in 1996, amended in fiscal 2007, to allow for the purchase of Subordinate Voting Shares by certain of its full-time employees, directors, officers and consultants.

The subscription price for Subordinate Voting Shares granted under options is the greater of (i) the weighted average trading price for such Subordinate Voting Shares for the five days preceding the date of grant during which the Subordinate Voting Shares were traded on the Toronto Stock Exchange ("TSX") or (ii) the trading price for the Subordinate Voting Shares on the last day the Subordinate Voting Shares were traded on the TSX immediately preceding the date of grant.

Under the Share Option Plan, the maximum number of Subordinate Voting Shares issuable from time to time is a fixed maximum percentage of 5% of the aggregate of the Multiple Voting Shares and the Subordinate Voting Shares issued and outstanding from time to time.

The granting of options is at the discretion of the Board of Directors which, at the date of grant, establishes the term and vesting period. Vesting of options generally commences 12 months after the date of grant and accrues annually over the vesting period provided there is continuous employment. The maximum term permissible is 10 years.

For the nine-month period ended November 30, 2019, a compensation cost of $2 (November 30, 2018– $13) was recorded in the consolidated statement of income (loss) and credited to contributed surplus. For the three-month period ended November 30, 2019, a compensation cost of $0 (November 30, 2018 – $4) was recorded in the consolidated statement of income (loss) and credited to contributed surplus.

The table below summarizes the status of the Share Option Plan.

	Number of shares	**Weighted average exercise price**	**Weighted average contractual life in months**
Outstanding – February 28, 2019	140,000	$14.63 (CA$19.26)	14.4
Outstanding – November 30, 2019	140,000	$14.50 (CA$19.26)	5.4
Exercisable – November 30, 2019	130,000	$14.73 (CA$19.57)	

e) On July 13, 2017, the Company adopted a performance share unit ("PSU") plan allowing the Board of Directors, through its Corporate Governance and Human Resources ("CGHR") Committee, to grant PSUs to certain of its full-time employees. A PSU is a notional unit whose value is based on the volume weighted average price of the Company's Subordinate Voting Shares on the Toronto Stock Exchange for the 20 trading days immediately preceding the grant date. The PSU plan is non-dilutive since vested PSUs shall be settled solely in cash. Each PSU grant shall vest at the end of a three-year performance cycle, which will normally start on March 1 of the year in which such PSU is granted and end on the last day of February of the third year following such grant, subject to the achievement of certain performance objectives over such cycle, as determined by the Company's CGHR Committee.

As at November 30, 2019, the Company had a total of 24,879 (February 28, 2019 – 24,611) PSUs outstanding, representing a total liability of $39 (February 28, 2019 – $71) which is included in accounts payable and accrued liabilities. For the nine-month period ended November 30, 2019, a compensation cost recovery of $32 (November 30, 2018 – $24) was recorded in the consolidated statement of income (loss) and decreased accounts payable and accrued liabilities. For the three-month period ended November 30, 2019, a compensation cost of $4 (November 30, 2018 – compensation cost recovery of $7) was recorded in the consolidated statement of income (loss) and increased (November 30, 2018 – decreased) accounts payable and accrued liabilities. No payments have been made in relation to PSUs since the inception of the plan. No PSUs were forfeited, and no PSUs have vested during the three-month and the nine-month periods ended November 30, 2019 and 2018.

f) On July 13, 2017, the Company adopted a deferred share unit ("DSU") plan allowing the Board of Directors, through its CGHR Committee, to grant DSUs to certain of its independent directors and full-time employees. A DSU is a notional unit whose value is based on the volume weighted average price of the Company's Subordinate Voting Shares on the Toronto Stock Exchange for the 20 trading days immediately preceding the grant date. The DSU plan is non-dilutive since vested DSUs shall be settled solely in cash. Each DSU grant shall vest at the earlier of:

- the sixth anniversary of its grant date; or
- the day the holder of the DSU attains the retirement age, which, unless otherwise determined by the CGHR Committee, is the earliest of age 65, or the age at which the combination of years of service at the Company plus his or her age is equal to 75, being understood that the retirement age shall not be less than 55 years old.

For more certainty, a grant made to an independent director or full-time employee who has reached the retirement age will vest immediately, unless otherwise determined by the CGHR Committee at or after the time of grant. Notwithstanding the foregoing, grants of DSUs made to non-employee directors of the Company vest on their grant date.

As at November 30, 2019, the Company had a total of 51,900 (February 28, 2019 – 28,768) DSUs outstanding, representing a total liability of $127 (February 28, 2019 – $98) which is included in accounts payable and accrued liabilities. For the nine-month period ended November 30, 2019, a compensation cost of $29 (November 30, 2018 – $21) was recorded in the consolidated statement of income (loss) and increased accounts payable and accrued liabilities. For the three-month period ended November 30, 2019, a compensation cost of $8 (November 30, 2018 – compensation cost recovery of $27) was recorded in the consolidated statement of income (loss) and increased (November 30, 2018 – decreased) accounts payable and accrued liabilities. No payments have been made in relation to DSUs (November 30, 2018 – payment of $9) and no DSUs were forfeited during the three-month and nine-month periods ended November 30, 2019 and 2018 and 18,428 (February 28, 2019 – 11,178) DSUs have vested as at November 30, 2019.

9 Contingent liabilities

Two of the Company's U.S. subsidiaries have been named as defendants in a number of asbestos-related legal proceedings pertaining to products they formerly sold. Management believes it has a strong defence, and the subsidiaries have previously been dismissed from a number of similar cases. Because of the many uncertainties inherent in predicting the outcome of these proceedings, as well as the course of asbestos litigation in the United States, management believes that it is not possible to make an estimate of the subsidiaries' asbestos liability. Accordingly, no provision has been set up in the accounts.

During the nine-month period ended November 30, 2019, legal and related costs for these matters amounted to $6,944 (November 30, 2018 – $6,253). During the three-month period ended November 30, 2019, legal and related costs for these matters amounted to $3,601 (November 30, 2018 – $1,908).

Lawsuits and proceedings or claims arising from the normal course of operations are pending or threatened against the Company.

On December 3, 2014, San Diego Gas & Electric Company ("SDG") filed a claim against Velan Valve Corp., a wholly-owned subsidiary of the Company, in the Superior Court of the State of California, concerning high pressure valves supplied to SDG and installed at its Palomar Energy Center ("Facility").

This lawsuit alleged damages to the Facility in excess of $9,000 related to allegedly defective valves supplied by Velan Valve Corp. The claim was for alleged strict product liability and alleged negligence. During the nine-month period ended November 30, 2019, the Company has recorded a final net settlement of $850 in regard to the claim.

(in thousands of U.S. dollars, excluding number of shares and per share amounts)

10 Adjustments to reconcile net loss to cash provided (used) from operating activities

	Three-month periods ended November 30,		Nine-month periods ended November 30,	
	2019 $	2018 $	2019 $	2018 $
Depreciation of property, plant and equipment	2,871	2,606	8,045	8,105
Amortization of intangible assets	504	433	1,499	1,332
Deferred income taxes	(79)	302	779	216
Share-based compensation expense (note 8 (d))	0	4	2	13
Loss on disposal of property, plant and equipment	(102)	(29)	(69)	(10)
Net change in derivative assets and liabilities	31	(637)	136	(269)
Net change in other liabilities	365	(3)	111	292
	3,590	2,676	10,503	9,679

11 Changes in non-cash working capital items

	Three-month periods ended November 30,		Nine-month periods ended November 30,	
	2019 $	2018 $	2019 $	2018 $
Accounts receivable	(4,663)	4,041	12,553	10,981
Inventories	(4,337)	(2,623)	(15,293)	493
Income taxes recoverable	(2,474)	(4,201)	(741)	(8,391)
Deposits and prepaid expenses	(330)	624	191	875
Accounts payable and accrued liabilities	10,512	7,532	1,544	5,999
Income taxes payable	(536)	(999)	168	(1,874)
Customer deposits	9,649	(5,795)	12,432	(11,477)
Provisions	(196)	(777)	(1,275)	(2,166)
Accrual for performance guarantees	(89)	(2,321)	(1,499)	(2,939)
	7,536	(4,519)	8,080	(8,499)

(in thousands of U.S. dollars, excluding number of shares and per share amounts)

12 Related party transactions and balances

Transactions and balances with related parties are in the ordinary course of business. Related party transactions and balances not otherwise disclosed separately in these consolidated financial statements are as follows:

	Nine-month periods ended November 30, 2019 $	2018 $
Affiliated company owned by certain relatives of the controlling shareholder		
Purchases – Material components	575	757
Key management[1] compensation		
Salaries and other short-term benefits	3,402	3,093
Share-based compensation – Options	2	13
Share-based compensation – PSUs and DSUs	(3)	(3)

	November 30, 2019 $	February 28, 2019 $
Accounts payable and accrued liabilities		
Affiliated companies	81	98

13 Fair value of financial instruments

The fair value hierarchy has the following levels:

- Level 1 – quoted market prices in active markets for identical assets or liabilities;
- Level 2 – inputs other than quoted market prices included in Level 1 that are observable for the asset or liability, either directly (as prices) or indirectly (derived from prices); and
- Level 3 – unobservable inputs such as inputs for the asset or liability that are not based on observable market data. The level in the fair value hierarchy within which the fair value measurement is categorized in its entirety is determined on the basis of the lowest level input that is significant to the fair value measurement in its entirety.

[1] Key management includes directors (executive and non-executive) and certain senior management.

(in thousands of U.S. dollars, excluding number of shares and per share amounts)

The fair value of financial assets and financial liabilities measured on the consolidated statements of financial position are as follows:

				As at November 30, 2019
Financial position classification and nature	**Total $**	**Level 1 $**	**Level 2 $**	**Level 3 $**
Assets				
Derivative assets	-	-	-	-
Liabilities				
Derivative liabilities	30	-	30	-

				As at February 28, 2019
Financial position classification and nature	**Total $**	**Level 1 $**	**Level 2 $**	**Level 3 $**
Assets				
Derivative assets	189	-	189	-
Liabilities				
Derivative liabilities	83	-	83	-

Fair value measurements of the Company's derivative assets and liabilities are classified under Level 2 because such measurements are determined using published market prices or estimates based on observable inputs such as interest rates, yield curves, and spot and future exchange rates. The carrying value of the Company's financial instruments is considered to approximate fair value, unless otherwise indicated.

14 Restructuring and transformation costs

On January 10, 2019, the Company announced measures to improve its operational efficiency and optimize its manufacturing footprint in North America. The Company's current production is gradually being reorganized from four North American plants to three more specialized plants that will be structured to better support the new business units' market strategies. The production of certain non-project valves produced in North America, as well as less complex project valves are also being transferred to India. Restructuring and transformation costs include temporary project resources and their travel and lodging costs as well as the moving costs related to dismantling and transportation of machinery and equipment to reflect the optimized manufacturing footprint plan. The Company is estimating $4,000 to $7,000 of severance costs before taxes for this fiscal 2020 but did not record a provision at the end of the nine-month period ending November 30, 2019 since the plan was not yet finalized at this date. The workforce reduction and plants consolidation commenced at the beginning of this fiscal year, but the most significant portion of these costs to date have been incurred in the third quarter of the current fiscal year and is aimed to be completed at the end of fiscal year 2021. Restructuring costs and transformation costs amounted to $2,480 for the nine-month period ended November 30, 2019 and $1,406 for the three-month period ended November 30, 2019.

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