MANAGEMENT'S DISCUSSION AND ANALYSIS

First quarter ended May 31, 2022

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

	As at	
(thousands)	**May 31, 2022 $**	**February 28, 2022 $**
Current	49,963	64,689
Past due 0 to 30 days	9,735	17,995
Past due 31 to 90 days	16,394	9,248
Past due more than 90 days	14,858	16,285
	90,950	108,217
Less: Loss allowance	(488)	(509)
	90,462	107,708
Other receivables	8,124	8,126
Total accounts receivable	**98,586**	**115,834**

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

	Three-month periods ended	
(thousands)	**May 31, 2022 $**	**May 31, 2021 $**
Balance – Beginning of the year	509	1,146
Loss allowance expense	8	-
Recoveries of trade accounts receivables	-	(22)
Write-off of trade accounts receivable	(16)	(55)
Foreign exchange	(13)	12
Balance – End of the period	**488**	**1,081**

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

CERTAIN RISKS THAT COULD AFFECT OUR BUSINESS

The Company lists the various risks that could affect its business in the year-end version of its MD&A. The Company continuously monitors and evaluates such risks, with particular current focus on the COVID-19 pandemic, the Ukraine conflict and the ongoing labour union negotiation in Montreal and Granby. The Company has no changes to report as at May 31, 2022.

INTERNAL CONTROLS AND PROCEDURES

In accordance with National Instrument 52-109 – Certification of Disclosure in Issuer’s Annual and Interim Filings, disclosure controls and procedures have been designed to provide reasonable assurance that the information presented in the Company’s interim and annual reports to shareholders is accumulated and communicated to management on a timely basis, including the Chief Executive Officer and the Chief Financial Officer, in order for appropriate decisions to be made in regards to disclosures. Internal controls over financial reporting have also been designed to provide reasonable assurance regarding the reliability of the 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 three-month period ended May 31, 2022 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 notes 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 ISSUED BUT NOT YET ADOPTED

In January 2020, the International Accounting Standards Board (“IASB”) issued *Classification of Liabilities as Current or Non-current (Amendments to IAS 1)* providing a more general approach to the classification of liabilities under IAS 1 based on the contractual arrangements in place at the reporting date. The amendments in *Classification of Liabilities as Current or Non-current (Amendments to IAS 1)* affect only the presentation of liabilities in the statement of financial position, not the amount or timing of recognition of any asset, liability income or expenses, or the information that entities disclose about those items. In July 2020, the IASB published *Classification of Liabilities as Current or Non-current – Deferral of Effective Date (Amendment to IAS 1)* deferring the effective date of the January 2020 amendments to IAS 1 by one year. The amendments to IAS 1 are effective for annual reporting periods beginning on or after January 1, 2023 with earlier adoption permitted. The Company is currently evaluating the impact of these amendments on its financial statements.

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							
	May 2022	**February 2022**	**November 2021**	**August 2021**	**May 2021**	**February 2021**	**November 2020**	**August 2020**
Sales	$75,005	$124,849	$109,971	$101,893	$74,529	$85,510	$71,560	$68,340
Net earnings (loss)[1]	(7,352)	(25,509)	4,507	5,015	(5,073)	338	9,527	(5,112)
Net earnings (loss) [1] per share								
- Basic and diluted	(0.34)	(1.19)	0.21	0.23	(0.24)	0.02	0.44	(0.24)
EBITDA[2]	(2,878)	16,592	13,291	10,657	(941)	1,648	13,784	(2,497)
EBITDA[2] per share								
- Basic and diluted	(0.13)	0.77	0.62	0.49	(0.04)	0.08	0.64	(0.12)

[1] *Net earnings or loss refer to net income or loss attributable to Subordinate and Multiple Voting Shares*
[2] *Non-IFRS and supplementary financial measures – more information at the end of this report*

NON-IFRS AND SUPPLEMENTARY FINANCIAL 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. Company has also presented supplementary financial measures which are defined at the end of this report. Reconciliation and definition can be found below.

Earnings before interest, taxes, depreciation and amortization ("EBITDA")

	Three-month periods ended	
(thousands, except amount per shares)	**May 31, 2022 $**	**May 31, 2021 $**
Net loss[1]	(7,352)	(5,073)
Adjustments for:		
Depreciation of property, plant and equipment	2,161	2,414
Amortization of intangible assets	568	558
Finance costs – net	236	529
Income taxes	1,509	631
EBITDA	**(2,878)**	**(941)**
EBITDA per share		
- Basic and diluted	(0.13)	(0.04)

The term "EBITDA" is defined as net income or loss attributable to Subordinate and Multiple Voting Shares plus depreciation of property, plant & equipment, plus amortization of intangible assets, plus net finance costs plus income taxes. The terms "EBITDA per share" is obtained by dividing EBITDA by the total amount of subordinate and multiple voting shares. The forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement.

Definitions of supplementary financial measures

The term "Net new orders" or "bookings" is defined as firm orders, net of cancellations, recorded by the Company during a period. Bookings are impacted by the fluctuation of foreign exchange rates for a given period. The measure provides an indication of the Company's sales operation performance for a given period as well as well as an expectation of future sales and cash flows to be achieved on these orders.

The term "backlog" is defined as the buildup of all outstanding bookings to be delivered by the Company. The Company's backlog is impacted by the fluctuation of foreign exchange rates for a given period. The measure provides an indication of the future operational challenges of the Company as well as an expectation of future sales and cash flows to be achieved on these orders.

The term "book-to-bill" is obtained by dividing bookings by sales. The measure provides an indication of the Company's performance and outlook for a given period.

The forward-looking statements contained in this MD&A are expressly qualified by this cautionary statement.

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

UNAUDITED CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

For the three-month period ended May 31, 2022

NOTICE OF NO AUDITOR REVIEW OF CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

In accordance with National Instrument 51-102 released by the Canadian Securities Administrators, the Company discloses that its auditors PricewaterhouseCoopers LLP have not reviewed the unaudited condensed interim consolidated financial statements for the three-month period ended May 31, 2022.

VELAN

Consolidated Statements of Financial Position

(in thousands of U.S. dollars)

	As at	
	May 31, 2022 $	February 28, 2022 $
Assets		
Current assets		
Cash and cash equivalents	49,621	54,015
Short-term investments	9,721	8,726
Accounts receivable	98,586	115,834
Income taxes recoverable	3,497	2,955
Inventories (note 6)	228,882	223,198
Deposits and prepaid expenses	6,992	6,877
Derivative assets (note 8)	650	553
	397,949	412,158
Non-current assets		
Property, plant and equipment	71,589	73,906
Intangible assets and goodwill	15,644	16,693
Deferred income taxes	4,267	4,774
Other assets	800	897
	92,300	96,270
Total assets	490,249	508,428
Liabilities		
Current liabilities		
Bank indebtedness	1,969	550
Accounts payable and accrued liabilities	78,882	80,503
Income taxes payable	2,605	3,806
Customer deposits	43,640	41,344
Provisions	17,979	18,444
Derivative liabilities (note 8)	153	560
Current portion of long-term lease liabilities	1,425	1,360
Current portion of long-term debt (note 7)	8,261	8,111
	154,914	154,678
Non-current liabilities		
Long-term lease liabilities	10,330	11,073
Long-term debt (note 7)	23,858	22,927
Income taxes payable	1,244	1,244
Deferred income taxes	3,831	4,025
Customer deposits	24,468	30,139
Provisions	13,818	13,101
Other liabilities	5,450	5,731
	82,999	88,240
Total liabilities	237,913	242,918
Total equity	252,336	265,510
Total liabilities and equity	490,249	508,428

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

VELAN

Consolidated Statements of Loss

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

	Three-month periods ended	
	May 31, 2022 $	**May 31, 2021 $**
Sales (note 9)	75,005	74,529
Cost of sales (notes 6)	54,932	54,535
Gross profit	20,073	19,994
Administration costs	25,812	23,779
Other expense (income)	(141)	121
Operating loss	(5,598)	(3,906)
Finance income	90	172
Finance costs	(326)	(701)
Finance costs – net	(236)	(529)
Loss before income taxes	(5,834)	(4,435)
Income tax expense	1,509	631
Net loss for the period	(7,343)	(5,066)
Net loss attributable to:		
Subordinate Voting Shares and Multiple Voting Shares	**(7,352)**	**(5,073)**
Non-controlling interest	9	7
Net loss for the period	(7,343)	(5,066)
Net loss per Subordinate and Multiple Voting Share		
Basic and diluted	(0.34)	(0.24)
Total weighted average number of Subordinate and Multiple Voting Shares		
Basic and diluted	21,585,635	21,585,635

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

VELAN

Consolidated Statements of Comprehensive Loss

(in thousands of U.S. dollars)

	Three-month periods ended	
	May 31, 2022 $	**May 31, 2021 $**
Comprehensive loss		
Net loss for the period	(7,343)	(5,066)
Other comprehensive loss		
Foreign currency translation	(5,831)	1,395
Comprehensive loss	(13,174)	(3,671)
Comprehensive loss attributable to:		
Subordinate Voting Shares and Multiple Voting Shares	(13,182)	(3,702)
Non-controlling interest	8	31
Comprehensive loss	(13,174)	(3,671)

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

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

VELAN

Consolidated Statements of Changes in Equity

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

	Equity attributable to the Subordinate and Multiple Voting shareholders						
	Share capital	Contributed surplus	Accumulated other comprehensive loss	Retained earnings	Total	Non-controlling interest	Total equity
Balance - February 28, 2021	72,695	6,260	(21,007)	239,136	297,084	3,137	300,221
Net income (loss) for the period	-	-	-	(5,073)	(5,073)	7	(5,066)
Other comprehensive income	-	-	1,371	-	1,371	24	1,395
Comprehensive income (loss)	-	-	1,371	(5,073)	(3,702)	31	(3,671)
Balance - May 31, 2021	72,695	6,260	(19,636)	234,063	293,382	3,168	296,550
Balance - February 28, 2022	72,695	6,260	(32,223)	218,092	264,824	686	265,510
Net income (loss) for the period	-	-	-	(7,352)	(7,352)	9	(7,343)
Other comprehensive loss	-	-	(5,830)	-	(5,830)	(1)	(5,831)
Comprehensive loss	-	-	(5,830)	(7,352)	(13,182)	8	(13,174)
Balance - May 31, 2022	72,695	6,260	(38,053)	210,740	251,642	694	252,336

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

Consolidated Statements of Cash Flow

(in thousands of U.S. dollars)

	Three-month periods ended	
	May 31, 2022 $	May 31, 2021 $
Cash flows from		
Operating activities		
Net loss for the period	(7,343)	(5,066)
Adjustments to reconcile net loss to cash provided (used) by operating activities (note 10)	(1,755)	2,412
Changes in non-cash working capital items (note 11)	6,033	3,549
Cash provided (used) by operating activities	(3,065)	895
Investing activities		
Short-term investments	(1,288)	(186)
Additions to property, plant and equipment	(920)	(1,739)
Additions to intangible assets	(9)	(288)
Proceeds on disposal of property, plant and equipment	16	3,132
Net change in other assets	14	(12)
Cash provided (used) by investing activities	(2,187)	907
Financing activities		
Net change in revolving credit facility	-	9,626
Increase in long-term debt	2,160	-
Repayment of long-term debt	(569)	(3,167)
Repayment of long-term lease liabilities	(370)	(413)
Cash provided by financing activities	1,221	6,046
Effect of exchange rate differences on cash	(1,782)	436
Net change in cash during the period	(5,813)	8,284
Net cash – Beginning of the period	53,465	62,953
Net cash – End of the period	47,652	71,237
Net cash is composed of:		
Cash and cash equivalents	49,621	80,356
Bank indebtedness	(1,969)	(9,119)
Net cash – End of the period	47,652	71,237
Supplementary information		
Interest paid	(223)	(350)
Income taxes paid	(1,817)	(1,121)

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

VELAN

NOTES TO THE CONDENSED INTERIM CONSOLIDATED FINANCIAL STATEMENTS

For the three-month period ended May 31, 2022

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 July 7, 2022.

2 Basis of preparation

These unaudited condensed interim consolidated financial statements for the three-month period ended May 31, 2022 have been prepared in accordance with International Financial Reporting Standards ("IFRS") in accordance with International Accounting Standard ("IAS") 34, *Interim Financial Reporting*. 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, 2022, 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, 2022.

3 New accounting standards and amendments issued but not yet adopted

In January 2020, the International Accounting Standards Board ("IASB") issued *Classification of Liabilities as Current or Non-current (Amendments to IAS 1)* providing a more general approach to the classification of liabilities under IAS 1 based on the contractual arrangements in place at the reporting date. The amendments in *Classification of Liabilities as Current or Non-current (Amendments to IAS 1)* affect only the presentation of liabilities in the statement of financial position, not the amount or timing of recognition of any asset, liability income or expenses, or the information that entities disclose about those items. In July 2020, the IASB published *Classification of Liabilities as Current or Non-current – Deferral of Effective Date (Amendment to IAS 1)* deferring the effective date of the January 2020 amendments to IAS 1 by one year. The amendments to IAS 1 are effective for annual reporting periods beginning on or after January 1, 2023 with earlier adoption permitted. The Company is currently evaluating the impact of these amendments on its financial statements.

4 Estimates

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 as those that applied to the annual consolidated financial statements for the year ended February 28, 2022.

Since December 2019, the coronavirus (“COVID-19”) global pandemic has caused temporary disruptions in the Company’s production and supply chain which have materially adversely affected its business and financial results. The economic slowdown triggered by the global pandemic, mainly in the oil and gas sector at the beginning of the previous fiscal year, also translated in lower non-project valve sales for the Company. More specifically, during the period of the ongoing pandemic, the Maintenance, Repair & Overhaul (“MRO”) business segment of the group was most impacted. By the second half of the fiscal year-ended February 28, 2022, however, sales started to pick-up at the midpoint of the year and reached pre-covid levels by year-end.

For the three-month period ended May 31, 2022, consolidated sales are similar to the three-month period ended May 31, 2021, however, the Company notes that MRO sales have actually improved compared to the prior fiscal year, therefore hinting at the recovery from the pandemic.

Although the Company has implemented proactive measures to protect its global workforce and mitigate the numerous effects of the pandemic, given the ongoing dynamic nature of circumstances surrounding COVID-19, it is not possible to reliably estimate the length, severity and long term impact the global pandemic may have on the Company’s results, conditions and cash flows. Therefore, the COVID-19 global pandemic should still be considered a risk factor.

During the three-month period ended May 31, 2022, the company did not apply wage for subsidies which provided a reduction of salaries. For the three-month period ended May 31, 2021, the company did apply for such subsidies which provided a reduction in salaries of $579 in Cost of sales and $439 in Administration costs.

5 Seasonality

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

6 Inventories

		As at
(thousands)	**May 31, 2022 $**	**February 28, 2022 $**
Raw materials	37,752	48,381
Work in process and finished parts	143,553	136,221
Finished goods	47,577	38,596
	228,882	**223,198**

As a result of variations in the ageing of its inventories, the Company recognized a net additional inventory provision for the three-month period ended May 31, 2022 of $753 (May 31, 2021 – $1,661), including reversals of $1,631 (May 31, 2021 - $1,140).

7 Long-term debt

	As at	
(thousands)	**May 31, 2022 $**	**February 28, 2022 $**
Canadian subsidiary		
Secured bank loan ($CAD 21,750; February 28, 2022 - $CAD 22,500)	16,986	17,134
French subsidiaries		
Unsecured bank loan (€2,671; February 28, 2022 - €2,943)	2,866	3,302
Italian subsidiary		
Unsecured bank loan (€4,820; February 28, 2022 - €2,869)	5,174	3,219
Unsecured state bank loan (€690; February 28, 2022 - €690)	741	774
Other	6,352	6,609
	32,119	31,038
Less: current portion	8,261	8,111
	23,858	**22,927**

As at May 31, 2022, the Company had drawn down nil (February 28, 2022 – nil) on the revolving credit facility and had $3,659 (February 28, 2022 – 3,980) in the form of outstanding letters of credit and letters of guarantee on a total $48,714 (February 28, 2022 – 49,365) borrowing availability. Furthermore, as at May 31, 2022, the Company was in compliance with all of its covenants.

8 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.

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

				As at May 31, 2022
(thousands)	Total $	Level 1 $	Level 2 $	Level 3 $
Financial position classification and nature				
Assets				
Derivative assets	650	-	650	-
Liabilities				
Derivative liabilities	153	-	153	-

				As at February 28, 2022
(thousands)	Total $	Level 1 $	Level 2 $	Level 3 $
Financial position classification and nature				
Assets				
Derivative assets	553	-	553	-
Liabilities				
Derivative liabilities	560	-	560	-

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.

9 Segment reporting

The Company reflects its results under a single reportable operating segment. The geographic distribution of its sales is as follows:

							Three-month period ended May 31, 2022
(thousands)	Canada $	United States $	France $	Italy $	Other $	Consolidation adjustment $	Consolidated $
Sales							
Customers -							
Domestic	5,350	21,298	9,450	35	4,272	-	40,405
Export	3,785	968	8,062	17,561	4,224	-	34,600
Intercompany (export)	6,325	2,498	29	376	13,948	(23,176)	-
	15,460	**24,764**	**17,541**	**17,972**	**22,444**	**(23,176)**	**75,005**

							Three-month period ended May 31, 2021
(thousands)	Canada $	United States $	France $	Italy $	Other $	Consolidation adjustment $	Consolidated $
Sales							
Customers -							
Domestic	4,906	21,351	10,965	4	4,503	-	41,729
Export	12,229	-	10,223	8,357	1,991	-	32,800
Intercompany (export)	8,391	2,182	6	74	12,102	(22,755)	-
	25,526	**23,533**	**21,194**	**8,435**	**18,596**	**(22,755)**	**74,529**

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

	Three-month periods ended	
(thousands)	**May 31, 2022 $**	**May 31, 2021 $**
Depreciation of property, plant and equipment	2,161	2,414
Amortization of intangible assets	568	558
Deferred income taxes	317	(246)
Loss (gain) on disposal of property, plant and equipment	54	(186)
Net change in long-term provisions and customer deposits	(4,133)	-
Net change in derivative assets and liabilities	(504)	(229)
Net change in other liabilities	(218)	101
	(1,755)	**2,412**

11 Changes in non-cash working capital items

	Three-month periods ended	
(thousands)	**May 31, 2022 $**	**May 31, 2021 $**
Accounts receivable	14,062	14,985
Inventories	(10,173)	(31,207)
Income taxes recoverable	(561)	(910)
Deposits and prepaid expenses	(302)	(2,455)
Accounts payable and accrued liabilities	413	14,830
Income taxes payable	(1,098)	(152)
Customer deposits	3,790	8,747
Provisions	(98)	(289)
	6,033	**3,549**

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Velan Inc. is listed on the Toronto stock exchange under the symbol VLN

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