REPORT TO SHAREHOLDERS

First quarter

Three-month period ended May 31, 2022

MANAGEMENT'S DISCUSSION AND ANALYSIS

First quarter ended May 31, 2022

HIGHLIGHTS[1]

- Sales for the quarter amounted to $75.0 million, an increase of $0.5 million or 0.6% compared to the same quarter of the previous fiscal year. Although comparable to prior year's first quarter performance, the Company continues to navigate through a volatile market where certain shipments for the quarter were delayed and are planned to be shipped later in the year.
- Gross profit for the quarter amounted to $20.1 million or 26.8%, stable compared to last year's $20.0 million of 26.8%. Gross profit improved for the quarter when considering the absence of Canada Emergency Wage Subsidies («CEWS») compared to $0.6 million last year. Prior year's gross profit percentage without the subsidies would have been 26.1% compared to 26.8% for the current quarter.
- Net loss[2] of $7.4 million and negative EBITDA[3] of $2.9 million for the quarter compared to a net loss[1] of $5.1 million and a negative EBITDA[2] of $0.9 million last year. The decrease in EIBTDA[3] is primarily attributable to an increase in administration costs, namely freight out costs and the absence of CEWS in the current quarter.
- Order backlog[3] remains strong at $506.0 million, an increase of $4.7 million or 0.9% since the beginning of the year. The portion of the current backlog[3] deliverable in the next twelve months is $339.2 million.
- Net new orders ("bookings")[3] of $93.4 million for the quarter, representing a book-to-bill ratio[3] of 1.25. The decrease in bookings[3] of $22.9 million or 19.7% compared to last year resulted mainly from the current geo-political uncertainties which created slower project awards. The Company nonetheless continues to observe a strong amount of activity ongoing.
- The Company's net cash amounted to a solid $47.7 million at the end of the quarter, a decrease of $5.8 million since the beginning of the fiscal year. The decrease in net cash for the quarter is primarily attributable to the lower EBITDA for the quarter. The shifting of revenues and related gross profits, as mentioned in the notes above have resulted in higher work in process and finished goods inventories by $16.3 million.

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

The following discussion provides an analysis of the consolidated operating results and financial position of Velan Inc. ("the Company") for the quarter ended May 31, 2022. This MD&A should be read in conjunction with the Company's audited consolidated financial statements for the years ended February 28, 2022 and 2021. 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 of the Company's audited consolidated financial statements. All foreign currency transactions, balances and overseas operations have been converted to U.S. dollars, the Company's reporting currency. This MD&A was approved by the Board of Directors of the Company on July 7, 2022. 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 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. Reconciliations of these amounts can be found at the end of this report. The Company has also presented supplementary financial measures which are defined 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.

ABOUT VELAN

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 12 manufacturing plants worldwide with 1,651 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 two 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 sales operation in Germany.

RESULTS OF OPERATIONS

(unless otherwise noted, all amounts are in U.S. dollars and all comparisons are to the first quarter of the last fiscal year)

	Three-month periods ended		
(thousands)	**May 31, 2022**	**May 31, 2021**	**Variance**
Sales	$75,005	$74,529	476
Gross profit	20,073	19,994	79
Administration costs	25,812	23,779	2,033
Income taxes	1,509	631	878
Net loss[1]	(7,352)	(5,073)	(2,279)
EBITDA[2]	(2,878)	(941)	(1,937)
Bookings[2]	93,446	116,374	(22,928)
Period ending backlog[2] of orders	505,950	607,162	(101,212)
(as a percentage of sales)			
Gross profit	26.8%	26.8%	-
(in dollars per share)			
Net loss[1] per share – basic and diluted	(0.34)	(0.24)	(0.10)
EBITDA[2] per share – basic and diluted	(0.13)	(0.04)	(0.09)

Backlog[2]

	As at		
(thousands)	**May 31, 2022**	**February 28, 2022**	**May 31, 2021**
Backlog[2]	505,950	501,224	607,162
For delivery within the next twelve months	339,214	321,860	360,414
For delivery beyond the next twelve months	166,736	179,364	246,748
Percentage – beyond the next twelve months	33.0%	35.8%	40.6%

The total backlog[2] increased by $4.7 million or 0.9% since the beginning of the fiscal year, amounting to $506.0 million at the end of the quarter. The increase in backlog is primarily due to a strong book-to-bill ratio[2] of 1.25 as a result of bookings outpacing sales in the current quarter. Otherwise, the increase in backlog[2] was negatively impacted by the weakening of the euro spot rate against the U.S. dollar since the beginning of the fiscal year which represented $12.8 million at the end of the quarter.

[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*

Bookings[1]

Bookings[1] amounted to $93.4 million, a decrease of $22.9 million or 19.7% compared to the first quarter of last year. This decrease is primarily attributable to upstream oil and gas and nuclear orders recorded in the Company's Italian and French operations. The current geo-political uncertainties have created slower project awards resulting in lower bookings[1] for the Company in the current quarter. The Company nonetheless continues to observe a strong amount of activity ongoing.

Sales

Sales were slightly higher for the quarter, increasing by $0.5 million or 0.6% compared to the same quarter last year. The increase in sales for the quarter is primarily attributable to increased shipments of large orders in the Company's Italian operations, partially offset by reduced shipments in the Company's North American operations. Although comparable to prior year's first quarter performance, sales were impacted in the quarter by supply chain delays, increased time to obtain government export documentation and final commercial negotiations on a handful of contracts. The revenues related to these contracts are expected to be recovered throughout the remainder of the fiscal year.

Gross profit

Gross profit remained stable for quarter, totaling $20.1 million or 26.8% compared to last year's $20.0 million or 26.8%. Gross profit remained stable due to the delivery of a comparable sales profile to last year, a balanced product mix, and continued focus on project delivery execution. The Company's gross profit also benefited from favorable foreign exchange movements which were primarily made up of unrealized foreign exchange translations related to the fluctuation of the U.S. dollar against the euro and Canadian dollar when compared to similar movements from the previous year. The gross profit in the prior period was positively impacted by the recording of $0.6 million of CEWS while the Company did not qualify for such subsidies in the current fiscal year. The subsidies were allocated between cost of sales and administration costs. Prior year's gross profit percentage without CEWS would have been 26.1% compared to 26.8% for the current quarter.

Administration costs

Administration costs for the quarter amounted to $25.8 million, an increase of $2.0 million or 8.5%. The increase in administration costs for the quarter is primarily attributable to higher outbound freight costs caused by the current global supply chain issues which are impacting freight costs and shipping delays. The administration costs in the prior year benefited from the recording of $0.4 million of CEWS while the Company did not qualify for such subsidies in the current quarter. The subsidies were allocated between cost of sales and administration costs. The increase for the quarter was partially offset by lower sales commissions recorded on the delivery of large orders over the course of the quarter.

EBITDA[1]

EBITDA[1] amounted to negative $2.9 million or $0.13 per share compared to a negative $0.9 million or $0.04 per share last year. The unfavorable movement in EBITDA[1] for the quarter is primarily attributable to the previously explained increase in administration costs.

[1] *Non-IFRS and supplementary financial measures – more information at the end of this report*

Income taxes

	Three-month periods ended			
(thousands, excluding percentages)		**May 31, 2022**		**May 31, 2021**
	$	%	$	%
Income tax at statutory rate	(1,546)	26.5	(1,175)	26.5
Tax effects of:				
Difference in statutory tax rates in foreign jurisdictions	52	(0.9)	114	(2.5)
Non-deductible (taxable) foreign exchange losses (gains)	267	(4.6)	(77)	1.7
Unrecognized tax losses	2,855	(48.9)	1,939	(43.7)
Benefit attributable to a financing structure	(67)	1.1	(66)	1.5
Other differences	(52)	0.9	(104)	2.3
Income tax expense	**1,509**	**(25.9)**	**631**	**(14.2)**

Net loss[1]

Net loss[1] amounted to $7.4 million or $0.34 per share compared to a net loss[1] of $5.1 million or $0.24 per share last year. The movement in net loss[1] was primarily attributable to the same factors as explained in the EBITDA[2] section combined with unfavorable movements in income taxes, partially offset by a favorable movement in finance costs.

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.

On May 31, 2022, the Company's order backlog[2] was $506.0 million and its net cash plus unused credit facilities amounted to $164.9 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. The Company also believes that its unused credit facilities are sufficient to navigate through lingering COVID-19 impacts and the conflict in Ukraine. 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. As at May 31, 2022, the Company is in compliance with all covenants related to its debt and credit facilities.

As part of managing its liquidity risk, the Company also monitors the financial health of its key suppliers. As at May 31, 2022, the Company does not see undue risk as a result of this assessment.

[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*

Cash flows - quarter ended May 31, 2022 compared to the quarter ended May 31, 2021

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

The Company's changes in net cash were as follows:

	Three-month periods ended	
(thousands)	**May 31, 2022**	**May 31, 2021**
Net Cash – Beginning of period	53,465	62,953
Cash provided (used) by operating activities	(3,065)	895
Cash provided (used) by investing activities	(2,187)	907
Cash provided by financing activities	1,221	6,046
Effect of exchange rate differences on cash	(1,782)	436
Net Cash – End of period	**47,652**	**71,237**

Operating activities

The unfavorable movement in cash used by operating activities for the quarter is primarily attributable to the decrease in EBITDA combined with a reduction in long-term customer deposits, partially offset by a favorable movement in non-cash working capital items.

The changes in non-cash working capital items were as follow:

	Three-month periods ended	
(thousands)	**May 31, 2022**	**May 31, 2021**
Accounts receivable	14,062	14,985
Income taxes recoverable	(561)	(910)
Inventories	(10,173)	(31,207)
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)
Changes in non-cash working capital items	**6,033**	**3,549**

The positive non-cash working capital movements for the quarter ended May 31, 2022 consisted primarily of:

- A decrease in accounts receivable primarily due to increased collections of prior year accounts;
- A higher amount of short-term customer deposits collected on certain large project orders by the Company's French operations.

The negative non-cash working capital movements for the quarter ended May 31, 2022 were primarily due to an increase in inventories required for the increase in the backlog combined with shipment delays explained under sales in the *Results of operations* section.

Investing activities

Cash used by investing activities for the quarter was primarily due to an increase in short-term investments and additions to property, plant and equipment. The fluctuation in additions to property, plant and equipment for the current quarter is primarily attributable to the timing of the receipts of certain equipment.

Financing activities

During the quarter, the Company's Italian operations borrowed $2.2 million in the form of unsecured bank loans, bearing annual interest between 0.67% and 0.71%, repayable quarterly and expiring in fiscal 2027.

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).

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 May 31, 2022 and February 28, 2022 are as follows:

	Range of exchange rates		Gain (loss) (in thousands of U.S. dollars)		Notional amount (in thousands of indicated currency)	
	May 31, 2022	February 28, 2022	May 31, 2022 $	February 28, 2022 $	May 31, 2022	February 28, 2022
Foreign exchange forward contracts						
Sell US$ for CA$ - 0 to 12 months	1.27-1.28	1.27-1.28	(152)	(470)	US$37,500	US$50,000
Buy US$ for CA$ - 0 to 12 months	1.25	1.25	88	301	US$37,500	US$50,000
Sell € for US$ – 0 to 12 months	1.15	1.15	(1)	(90)	€11,250	€15,000
Buy € for US$ – 0 to 12 months	1.13	1.13	562	252	€11,250	€15,000

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.

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 May 31, 2022, three (February 28, 2022 – three) customers accounted for more than 5% each of its trade accounts receivable, of which one customer accounted for 13.7% (February 28, 2022 – 10.8%), and the Company's ten largest customers accounted for 59.9% (February 28, 2022 – 55.7%) of trade accounts receivable. In addition, there was two customers (May 31, 2022 – nil) that 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. 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 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.

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:

	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.

VELAN

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.

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

(thousands)	As at May 31, 2022 $	As at 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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