NANOTECH

September 30, 2018

Annual Report

For purposes of this management discussion and analysis ("MD&A"), "Nanotech", the "Company", "we", or "us" refers to Nanotech Security Corp. and its subsidiaries. This year and 2018 mean the fiscal year ended September 30, 2018. Last year and 2017 mean the fiscal year ended September 30, 2017, and 2016 means the fiscal year ended September 30, 2016. This quarter or the current quarter means the three months ended September 30, 2018.

ADVISORY

This MD&A, dated December 18, 2018, should be read in conjunction with the cautionary statement regarding forward-looking statements below and the Company's consolidated financial statements for the year ended September 30, 2018. The results reported herein have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB") and are presented in Canadian dollars. All quarterly information disclosed in the MD&A is unaudited.

Additional information relating to the Company is filed on SEDAR at www.sedar.com.

FORWARD-LOOKING STATEMENTS

The following discussion and analysis of the financial conditions and results of operations contains forward-looking statements concerning anticipated developments in the Company's operations in future periods, the adequacy of Nanotech's financial resources, and the events or conditions that may occur in the future. Forward-looking statements are frequently, but not always, identified by words such as "expects", "anticipates", "believes", "intends", "estimates", "predicts", "potential", "targeted", "plans", "possible" and similar expressions, or statements that events, conditions, or results "will", "may", "could" or "should" occur or be achieved.

These forward-looking statements include, without limitation, statements about the Company's market opportunities, strategies, competition, and the Company's views that its optics-based technologies will continue to show promise for large scale production. Other forward-looking statements imply that the Company will remain capable of being financed and/or will be able to partner development until profitability is eventually realized. The principal risks related to these forward-looking statements are the loss of a key customer, that the Company's products receive market acceptance and that its intellectual property claims will be sufficiently broad or enforceable to provide the necessary protection or attract the necessary capital.

These forward-looking statements are based on the beliefs, expectations and opinions of management on the date the statements are made. Consequently, all forward-looking statements made in this discussion and analysis of the financial conditions and results of operations or the documents incorporated by reference, are qualified by this cautionary statement and there can be no certainty that actual results or developments the Company anticipates will be realized. For additional information with respect to certain of these risks or factors reference should be made to the "Business Risks and Uncertainties" section of the MD&A and the notes to the audited consolidated financial statements for the year ended September 30, 2018, as well as with the Company's continuous disclosure materials filed from time to time with Canadian securities regulatory authorities, which are available online at www.sedar.com. Nanotech disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise, other than as required by law. Caution needs to be used when taking forward-looking statements into account when evaluating the Company.

GENERAL OVERVIEW

Nanotech is incorporated under the laws of British Columbia, listed on the TSX Venture Exchange (trading symbol: NTS) and quoted in the United States on the OTCQX Market (trading symbol: NTSFF). The Company's head office is located at #505 - 3292 Production Way, Burnaby, BC, Canada V5A 4R4. The Company's registered and records office is #1500 - 1055 West Georgia, Vancouver, BC, Canada V6E 4N7.

Nanotech researches, creates, and produces nano-optic structures and colour-shifting materials used in authentication and brand enhancement applications across a wide range of markets including banknotes, tax stamps, secure government documents, commercial branding, and the pharmaceutical industry.

The Company's KolourOptik® technology employs arrays of billions of nano-indentations that are impressed or embossed onto a substrate material such as polymer, paper, metal, or fabric. By using sophisticated algorithms to direct an electron beam, the Company creates visual images with colour-shifting effects such as 3D, perceived movement, and can also display high-definition colours including skin tones, and whites and blacks, which are not possible using holographic technology.

The Company's optical thin film ("OTF") security features are manufactured using precision engineered nanometer thick layers of metals and ceramics to form filters designed to uniquely manipulate visible and non-visible light. This unique manipulation of light properties is used to create specialized security features in the form of threads, stripes and patches that are applied to banknotes and other secure documents. By using sophisticated electron beam and sputtered deposition methods, Nanotech precisely controls the construction and inherent properties to provide custom tailored colour-shifting solutions. An individual looking at these threads, stripes and patches sees an obvious colour-shift (e.g. green to magenta) when it is tilted or rotated.

On September 21, 2017, the directors of the Company made the determination that it would pursue the possible sale of its subsidiary, Tactical Technologies Inc. ("Tactical"), to a third party. At September 30, 2017, Tactical was classified as a separate disposal group held for sale and as a discontinued operation. Accordingly, the Company's comparative consolidated statements of operations and comprehensive loss have been restated to exclude the discontinued operations for the year ended September 30, 2017. On June 29, 2018, the assets used in connection with Tactical's surveillance equipment and van conversion business were sold to an employee of Tactical for a nominal amount, and on September 28, 2018, Tactical was wound up and struck from the corporate register.

Report on 2018 Goals

Management established the following goals for the 2018 fiscal year:

1. **Grow revenues by 20% to 40%.** 2018 revenue was 25% higher than 2017.
2. **Begin to collect licensing revenue from the tax stamp and commercial markets.** Nanotech has entered into distribution agreements in India with two suppliers to the tax stamp markets and are pursuing both tax stamp and commercial market revenue from this geographic market.
3. **Maintain a strong focus on earnings with a target of 15% to 20% Adjusted EBITDA margin.** Achieved a 22% Adjusted EBITDA margin for 2018.
4. **Continue to pursue a volume OTF partnering opportunity with Hueck Folien for banknotes.** Management continues to support its manufacturing partner Hueck Folien in an ongoing effort to improve the quality of their high-volume production. Progress was made in 2018, however at this time the Company is no longer actively trying to qualify as an OTF supplier for the Chinese 100 Yuan banknote, and instead will pursue other volume and licensing opportunities with Hueck Folien.
5. **Invest in several key marketing hires to ensure internal resources are in place to develop the products, sales channels, and marketing materials necessary to penetrate commercial markets.** Joe Vosburgh joined the Company as Vice President Marketing, bringing over 20 years experience in the successful development and commercialization of breakthrough technologies. Monika Russell, who has 15 years public company experience, also joined as Vice President Finance, allowing Troy Bullock, President and CFO, to expand his responsibilities.
6. **Continue to open new corporate development opportunities by partnering with established companies to enable Nanotech to enter new markets.** The Company announced a distribution agreement appointing Holostik India Limited and Kumbhat Holographics Co. Ltd. as Nanotech's authorized distributors and converters for the non-banknote market in India.

RESULTS OF OPERATIONS

Select financial information for the years ended September 30, 2018, 2017 and 2016:

Select Financial Information	2018	2017	2016
Revenue	$ 9,199,710	$ 7,343,791	$ 2,888,896
Cost of sales	2,051,890	1,429,371	884,132
	7,147,820	5,914,420	2,004,764
Expenses			
Research and development	1,407,430	1,475,437	1,996,715
General and administration	2,532,156	2,308,846	2,307,368
Sales and marketing	2,018,055	2,043,514	2,078,612
Depreciation and amortization	1,485,024	2,755,882	3,010,263
	7,442,665	8,583,679	9,392,958
Loss from continuing operations before other expenses	(294,845)	(2,669,259)	(7,388,194)
Other (income) expenses	(371,901)	1,184,594	433,513
Income (loss) from continuing operations before income taxes	77,056	(3,853,853)	(7,821,707)
Deferred income tax recovery	-	-	162,797
Net income (loss) from continuing operations	77,056	(3,853,853)	(7,658,910)
Loss from discontinued operations	(123,322)	(900,279)	(170,895)
Net loss	$ (46,266)	$ (4,754,132)	$ (7,829,805)
Adjusted EBITDA[1]	$ 1,998,785	$ 1,168,222	$ (3,648,411)

[1]Adjusted EBITDA is a non-IFRS measure as described in the Non-IFRS Financial Measures section of this MD&A.

Financial Position as at September 30	2018	2017	2016
Cash, cash equivalents and short-term investments	$ 9,613,621	$ 10,883,919	$ 3,312,691
Total debt	-	-	6,595,142
	$ 9,613,621	$ 10,883,919	$ (3,282,451)
Total assets	$ 30,229,055	$ 30,059,624	$ 24,511,586
Total liabilities	1,325,139	1,860,086	8,089,503
Total equity	28,903,916	28,199,538	16,422,083

Revenue

The Company currently derives a significant portion of its revenue from paid authentication development projects with issuing authorities. During the year ended September 30, 2017, the Company disclosed a development contract for up to $30.0 million over a period of up to five years. These development activities incorporate both nano-optic and OTF technologies and are focused on developing authentication features for future banknotes.

Revenues for the year ended September 30, 2018 increased by $1,855,919 or 25% to $9,199,710, compared to $7,343,791 in the same period last year. Revenue growth was primarily due to increased revenue from paid development activities, partially offset by a reduction in OTF revenue.

Gross Margin

Gross margin for the year ended September 30, 2018 increased by $1,233,400 or 21% to $7,147,820, compared to $5,914,420 in the same period last year. Overall, the gross margin percentage was 78% for the year ended September 30, 2018, a decrease from 81% in the same period last year.

Research and Development

Research and development expenditures for the year ended September 30, 2018 decreased by $68,007, or 5% to $1,407,430 compared to $1,475,437 in the same period last year, due to a larger portion of salaries and other expenses being allocated to cost of sales for increased paid development projects.

General and Administration

General and administration expenditures for the year ended September 30, 2018 increased $223,310, or 10% to $2,532,156 compared to $2,308,846 in the same period last year, due to the expansion of Nanotech's Burnaby, BC laboratory and an increase in salaries expenses associated with additional staff hired in 2018.

Sales and Marketing

Sales and marketing expenditures for the year ended September 30, 2018 were $2,018,055, a decrease of $25,459 or 1% which was consistent with $2,043,514 in the same period last year.

Depreciation and Amortization

Depreciation and amortization included in operating expenditures for the year ended September 30, 2018 was $1,485,024, compared to $2,755,882 in the same period last year. Depreciation included in cost of sales for the year ended September 30, 2018 was $128,146, compared to $160,401 for the same period last year. The reduction in depreciation and amortization expenditures reflects the Company's declining balance depreciation policy and the intangible assets being completely amortized as at September 30, 2017.

Other (Income) Expenses

Other income for the year ended September 30, 2018 was $371,901, an increase of $1,556,495, compared to other expenses of $1,184,594 in the same period last year. The increase was primarily due to the repayment of the convertible debentures and long-term debt in 2017, which reduced the interest expense by $1,053,254 in the current year, while increased cash on hand resulted in a $83,002 increase in interest income in the current year. In addition, foreign exchange gains recorded for the year to date were $419,838 higher than in the same period last year.

Adjusted EBITDA

Adjusted EBITDA for the year ended September 30, 2018 was $1,998,785, compared to $1,168,222 during the same period last year. The improvement reflects an increase in development contract revenue, partially offset by an increase in general and administration expenditures.

Net Loss from Discontinued Operations

Net loss from discontinued operations for the year ended September 30, 2018 was $123,322, compared to a net loss of $900,279 during the same period last year. The decrease in net loss was primarily due a reduction in overall expenses for the current year as Tactical was restructured following the Company's decision to sell the business.

Net Loss

Net loss for the year ended September 30, 2018 was $46,266, compared to a net loss of $4,754,132 during the same period last year. The decrease in net loss reflects an increase in Adjusted EBITDA in combination with lower interest and amortization expenses.

QUARTERLY RESULTS

	Q4 2018	Q3 2018	Q2 2018	Q1 2018	Q4 2017	Q3 2017	Q2 2017	Q1 2017
($ thousands, except per share data)								
Revenue	$ 3,085	$ 1,938	$ 1,943	$ 2,233	$ 2,662	$ 2,569	$ 1,419	$ 694
Net income (loss) from continuing operations	770	(456)	(333)	96	127	(749)	(1,559)	(1,673)
Net income (loss)	770	(627)	(285)	96	(301)	(905)	(1,695)	(1,853)
Adjusted EBITDA(1)	1,306	100	133	460	1,132	858	(268)	(554)
Basic earnings (loss) per share:								
Continuing operations	0.01	(0.01)	0.00	0.00	0.00	(0.01)	(0.03)	(0.03)
Net income (loss)	0.01	(0.01)	0.00	0.00	0.00	(0.02)	(0.03)	(0.03)
Diluted earnings (loss) per share:								
Continuing operations	0.01	(0.01)	0.00	0.00	0.00	(0.01)	(0.03)	(0.03)
Net income (loss)	0.01	(0.01)	0.00	0.00	0.00	(0.02)	(0.03)	(0.03)

(1)Adjusted EBITDA is a non-IFRS measure as described in the Non-IFRS Financial Measures section of this MD&A.

Revenue and Adjusted EBITDA were impacted by the timing of development contract revenue and recurring OTF orders in the quarters presented, as there is an inherent variability in development contract revenue with government organizations and in the receipt of recurring OTF orders. Net income (loss) from continuing operations and net income (loss) were further affected by the repayment of the convertible debentures in the third quarter of 2017 and long-term debt in the fourth quarter of 2017, which reduced interest expense. There are no seasonal effects in the Company's business over the quarters presented.

Comparison of Fourth Quarter Results, Year-over-year

Revenue for the fourth quarter of 2018 was $3,085,140, compared to $2,661,660 in the same period of 2017. The difference is primarily due to increased paid development revenue and OTF revenue in the current quarter, which is a result of the inherent variability in timing of development contract revenue and recurring OTF orders.

Net income from continuing operations for the fourth quarter of 2018 was $770,086, compared to $126,583 in the fourth quarter of 2017. The difference was due to increased revenue, reduced depreciation and amortization expenses and reduced foreign exchange loss in the current quarter.

Net income for the fourth quarter of 2018 was $770,086, compared to net loss of $300,694 in the fourth quarter of 2017. The difference was due to increased revenue, reduced depreciation and amortization expenses, reduced foreign exchange loss in the current quarter and reduced loss from discontinued operations due to the wind up of Tactical in the current quarter.

Adjusted EBITDA for the fourth quarter of 2018 was $1,305,841, compared to $1,132,249 in the same period of 2017. The difference is primarily due to increased revenue in the current quarter.

RELATED PARTY TRANSACTIONS

For the year ended September 30, 2018, the Company had no transactions with related parties as defined in IAS 24, *Related Party Disclosures*, except those pertaining to transactions with key management personnel in the ordinary course of their employment, or as disclosed below.

(a) Remuneration of key management personnel:

	2018	2017
Salaries, accrued bonuses, and employee benefits	$ 1,208,306	$ 1,233,741
Share-based payments	493,881	699,138
	$ 1,702,187	$ 1,932,879

(b) As of September 30, 2018, amounts owing to a company controlled by an officer and director of the Company included in accounts payable and accrued liabilities were $191,433 (2017 - $262,854) in the ordinary course of his employment arrangement.

(c) Legal and professional fees, taxes and disbursements totaling $81,776 for the year ended September 30, 2018 (2017 - $160,664) were incurred with a law firm of which a director of the Company is a partner. As of September 30, 2018, amounts owing to this company included in accounts payable and accrued liabilities were $50,780 (2017 - $93,219).

The above transactions are in the normal course of business and are measured at the exchange amount which is the amount of consideration established and agreed to by the related parties.

LIQUIDITY AND CAPITAL RESOURCES

The Company's principal sources of liquidity are cash provided by operations, including collection of accounts receivable, and access to equity capital resources. The Company's primary short-term cash requirement is to fund any potential shortfall from operations, working capital, and capital expenditures. Cash is also used to finance other long-term strategic business initiatives.

Summary of Statements of Cash Flows

	2018	2017
Cash provided by (used in) continuing operations	$ 1,453,736	$ (172,904)
Cash provided by (used in) discontinued operations	76,694	(574,313)
Cash provided by (used in) operating activities	1,530,430	(747,217)
Cash used in investing activities	(10,300,677)	(106,944)
Cash provided by financing activities	-	8,339,784
Effect of foreign exchange on cash and cash equivalents	(98,908)	85,605
Cash and cash equivalents, beginning of year	10,883,919	3,312,691
Cash and cash equivalents, end of year	$ 2,014,764	$ 10,883,919

Operating Activities

Cash provided by operating activities was $1,530,430 for the year ended September 30, 2018, compared to cash used in operating activities of $747,217 for the same period last year. This improvement was a result of increased development revenue.

Investing Activities

Cash used in investing activities was $10,300,677 for the year ended September 30, 2018, compared to $106,944 used in the same period last year. During the year, management invested excess cash of $7,598,857 in cashable term deposits held with a Canadian chartered bank to generate additional interest income. The term deposits have maturity dates between October 23, 2018 and June 25, 2019. Interest rates range between 1.8% and 2.0%. Equipment purchases in 2018 were related to a new electron beam lithography system, a revenue-generating steam boiler for our Thurso facility, and a research and development embossing line.

Financing Activities

Cash provided by financing activities was $nil for the year ended September 30, 2018, compared to $8,339,784 during the same period last year. The prior year reflects the proceeds of a private placement, offset by the repayment of convertible debentures and a note payable. In addition, cash flows for the prior year included proceeds upon the exercise of stock options.

Capital Resources and Liquidity

The Company's objectives when managing capital are to safeguard the ability to continue as a going concern, to provide adequate return to shareholders, to meet external capital requirements, and to preserve financial flexibility in order to benefit from potential opportunities that may arise. Our principal cash requirements are for operations, working capital, and capital expenditures.

The Company's officers are responsible for managing the Company's capital and do so through quarterly meetings and regular review of financial information. The Board of Directors is responsible for overseeing this process. In managing its capital, the Company considers changes in economic conditions, risks that impact operations, and future significant capital investment opportunities. During the year ended September 30, 2018, management invested excess cash in cashable term deposits to generate additional interest income. There were no other changes in our approach to capital management.

		2018		2017
Cash	$	292,688	$	914,378
Cash equivalents		1,722,076		9,969,541
Short-term investments		7,598,857		-
	$	9,613,621	$	10,883,919

As at September 30, 2018, the Company had no lines of credit and no exposure to asset-backed commercial paper.

The Company had commitments of $804,724 as at September 30, 2018 primarily under operating leases related to office space. Management has reviewed its projected funding requirements for the next twelve months and expects that, through the generation and collection of revenues, the Company will maintain sufficient liquidity to meet its requirements.

Non-IFRS Financial Measures

In addition to results reported in accordance with IFRS, the Company discloses Adjusted EBITDA as a supplemental indicator of its financial performance.

The Company defines Adjusted EBITDA as net income (loss) excluding the impact of interest and financing costs (net of interest income), foreign exchange gain (loss), income taxes, depreciation and amortization, share-based compensation, and net income (loss) from discontinued operations. The Company believes Adjusted EBITDA is a useful measure as it provides information to management about the operating and financial performance of the Company and its ability to generate operating cash flow to fund future working capital needs, as well as fund future growth. Adjusted EBITDA may also be used by investors and analysts for the purpose of valuing the Company.

Readers are cautioned that these non-IFRS definitions are not recognized measures under IFRS, do not have standardized meanings prescribed by IFRS, and should not be construed to be alternatives to net earnings determined in accordance with IFRS or as indicators of performance or liquidity or cash flows. The Company's method of calculating these measures may differ from methods used by other entities and accordingly Nanotech's measures may not be comparable to similarly titled measures used by other entities or in other jurisdictions. The Company uses these measures because it believes they provide useful information to both management and investors with respect to the operating and financial performance of the Company.

	2018	2017
Net loss	$ (46,266)	$ (4,754,132)
Finance (income) expense	(121,878)	1,014,779
Foreign exchange (gain) loss	(250,023)	169,815
Depreciation and amortization	1,611,891	2,916,283
Share-based compensation	681,739	921,198
Net loss from discontinued operations	123,322	900,279
Adjusted EBITDA	$ 1,998,785	$ 1,168,222

Financial Instruments

The Company considers the management of financial risk to be an important part of its overall corporate risk management policy. The nature and extent of risks arising from financial instruments and their related risk management are described in note 12 of the consolidated financial statements for the year ended September 30, 2018. In the year ended September 30, 2018, there was no material change to the nature of the risks arising from our classification of financial instruments, or related risk management objectives.

CAPITAL STRUCTURE AND OUTSTANDING SHARE DATA

The Company maintains an equity incentive plan consisting of a stock option plan and a restricted share unit ("RSU") plan to grant options and RSUs to eligible participants. The obligations under the RSU plan can be settled at the Company's discretion through either cash or issuance of common shares. The Company intends to settle the obligation through the issuance of common shares.

During the year ended September 30, 2018, 567,500 options (2017 – 413,500) and 238,782 RSUs (2017 – 499,200) were granted. During the year ended September 30, 2018, 22,060 RSUs and nil options (2017 – nil RSUs and 590,000 options) were forfeited or expired during the year.

The common shares, options, and RSUs outstanding and exercisable as at the following dates are:

	September 30, 2018		September 30, 2017	
	Number	Weighted average exercise price	Number	Weighted average exercise price
Common shares outstanding	68,771,501		68,395,825	
Options				
Outstanding	2,607,500	$ 1.35	2,040,000	$ 1.35
Exercisable	2,273,750	$ 1.35	1,770,125	$ 1.37
RSUs				
Outstanding	370,606	N/A	529,560	N/A

As at September 30, 2018, the following RSUs were available to grant:

Total RSUs approved by shareholders	2,100,000
Shares issued to date under the RSU plan	(1,139,947)
Reserved for issuance under the RSU plan	960,053
RSUs outstanding	(370,606)
RSUs available to grant	589,447

As at September 30, 2018, the following options were available to grant:

10.0% of common shares issued and outstanding	6,877,150
Shares reserved for issuance under the RSU plan	(960,053)
Options outstanding	(2,607,500)
Options available to grant	3,309,597

As at December 18, 2018, the Company has 68,771,501 common shares issued and outstanding. There are no preferred shares issued and outstanding.

SIGNIFICANT ACCOUNTING POLICIES AND THE USE OF ESTIMATES

The preparation of financial statements in accordance with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, revenues, and expenses. Estimates and assumptions are continually evaluated and are based on historical experience and various factors that management believes to be reasonable under the circumstances. However, due to the nature of estimates, actual results may differ from these estimates.

The Company's significant accounting policies are contained in note 3 to the consolidated financial statements. Significant areas requiring the use of judgment in application of accounting policies and assumptions and estimates are discussed below.

Going Concern

Financial statements are prepared on a going concern basis unless management either intends to liquidate the Company or to cease trading, or has no realistic alternative to do so. Assessment of the Company's ability to continue as a going concern requires the consideration of all available information about the future, which is at least, but not limited to, twelve months from the end of the reporting period. This information includes estimates of future cash flows and other factors, the outcome of which is uncertain. When management is aware, in making its assessment of material uncertainties related to events or conditions that may cast significant doubt upon the Company's ability to continue as a going concern, those uncertainties are disclosed.

Impairment of Non-financial Assets

Goodwill is the residual amount that results when the purchase price of an acquired business exceeds the sum of the amounts allocated to the assets acquired, less liabilities assumed, based on their fair values. Goodwill is not amortized and is tested for impairment at least annually, or more frequently if events or changes in circumstances indicate that the asset might be impaired. Goodwill is considered to be impaired when the carrying amount of the cash generating unit or group of cash generating units to which the goodwill has been allocated exceeds its fair value. An impairment loss, if any, would be recognized as a separate line item in the statement of earnings.

Intangible assets, acquired individually or with a group of other assets, are initially recognized and measured at cost. The cost of a group of intangible assets acquired in a transaction, including those acquired in a business combination that meet the specified criteria for recognition apart from goodwill, is allocated to the individual assets acquired based on their relative fair values. Intangible assets with finite useful lives are amortized over their estimated useful lives and are tested for impairment when events or changes in circumstances indicate that an asset might be impaired. The amortization methods and estimated useful lives of intangible assets are reviewed annually.

The Company performs impairment tests for goodwill and other non-financial assets periodically as described above. Impairment tests involve considerable use of judgment and require management to make estimates and assumptions. The fair values of cash generating units are derived from certain valuation models, which consider various factors such as discount rates, future earnings, and revenue growth rates. Changes in estimates and assumptions can affect the reported value of goodwill and other non-financial assets.

Provisions

The Company records a provision when an obligation to a third party exists, the payment is probable, and the amount can be reasonably estimated. The Company records a provision based upon the best estimate of the expenditure required to settle the present obligation at the balance sheet date. While management believes these estimates are reasonable, differences in actual results or changes in estimates could have an impact on the liabilities and results of operations recorded by the Company.

Share-based Compensation

The Company measures the fair value of its share-based compensation awards using the Black-Scholes option pricing model and recognizes the fair value expense on a straight-line basis over the relevant vesting period. Management uses judgment to determine the inputs to the Black-Scholes option pricing model including expected award lives, underlying share price volatility and forfeiture rates. Changes in these assumptions could have a material impact on the calculation of fair value and the amount of compensation expense recorded in earnings.

Investment Tax Credits

The Company recognizes investment tax credits when there is reasonable assurance that they will be realized. Investment tax credits may be carried forward to reduce future Canadian federal and provincial income taxes payable. The Company applies judgment when determining whether the reasonable assurance threshold has been met to recognize investment tax credits. The Company must interpret eligibility requirements in accordance with Canadian income tax laws and must assess whether future taxable income will be available against which the investment tax credits can be utilized. Any changes in these interpretations and assessments could have a material impact on the amount and timing of investment tax credits recognized in the consolidated financial statements.

Income Taxes

The Company is subject to taxation in numerous jurisdictions and exercises judgment in estimating the provision for federal, provincial, and foreign income taxes. Income tax laws and regulations can be complex and are potentially subject to different interpretation between the Company and the respective tax authority. Provisions for tax are made using the Company's best estimate of the amount of tax expected to be paid or recovered based on an assessment of all relevant factors. However, the precision and reliability of the estimates are subject to uncertainty and may change as additional information becomes known.

Deferred tax assets are recognized only when it is probable that sufficient taxable profit will be available in future periods against which deductible temporary differences may be utilized. The recognition of deferred income tax assets involves considerable use of judgment and requires management to make estimates and assumptions, including estimates of projected taxable income, the timing of the reversal of temporary differences, the tax rates and laws in each respective jurisdiction, and the impact of tax planning strategies. The amount of recognized deferred tax assets may change from period to period due to the uncertainties surrounding these assumptions.

Inventory

Inventory is measured at the lower of cost and net realizable value. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses, taking into account the most reliable evidence available at each reporting date. The future realization of inventory may be affected by future technology or other market-driven changes that may reduce future selling prices. While management believes that the estimates of net realizable value as at the balance sheet date are reasonable, differences in estimates could have an impact on the inventory valuation and results of operations of the Company.

Property, Plant, and Equipment

Property, plant, and equipment is measured at cost less accumulated depreciation and accumulated impairment losses. Depreciation expense is recognized based on management's best estimate of the useful lives of the depreciable assets. The Company reviews the estimated useful life annually and recognizes any adjustment as appropriate. While management believes that estimates of useful lives of depreciable assets as at the balance sheet date are reasonable, differences in estimates could impact the valuation of depreciable assets and the results of operations of the Company.

NEW ACCOUNTING STANDARDS

In July 2014, the IASB issued IFRS 9 – *Financial Instruments*, which replaces the earlier versions of IFRS 9 (2009, 2010, and 2013) and completes the IASB's project to replace IAS 39 – *Financial Instruments: Recognition and Measurement*. IFRS 9 includes a logical model for classification and measurement of financial assets and a single, forward-looking 'expected credit loss' impairment model. IFRS 9 is effective for annual periods beginning on or after January 1, 2018 and must be applied retrospectively with some exemptions.

The Company will adopt the standard on October 1, 2018, using the modified retrospective application method under which comparatives are not restated and a cumulative catch up adjustment is recorded on October 1, 2018, for any differences identified including adjustments to opening retained earnings balances. The Company has analyzed the impact of adopting IFRS 9 and anticipates there will not be any material changes as a result of adopting this new standard.

In May 2014, the IASB issued IFRS 15 - *Revenue from Contracts with Customers*, which supersedes IAS 18 - *Revenue,* IAS 11 - *Construction Contracts* and other interpretive guidance associated with revenue recognition. IFRS 15 provides a single, principles-based five-step model to be applied to all contracts with customers to determine how and when an entity should recognize revenue. The standard also provides guidance on whether revenue should be recognized at a point in time or over time as well as requirements for more informative, relevant disclosures. IFRS 15 is effective for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. The Company has completed an assessment of the impact that the initial application of IFRS 15 will have on its financial statements and does not expect there will be a significant impact, other than additional required disclosures. The Company will adopt IFRS 15 in its financial statements for the annual period beginning on October 1, 2018, using the full retrospective transitional approach.

In January 2016, the IASB issued IFRS 16 - *Leases*, which supersedes IAS 17 - *Leases*. IFRS 16 establishes principles for the recognition, measurement, presentation and disclosure of leases. The standard establishes a single model for lessees to bring leases on balance sheet while lessor accounting remains largely unchanged and retains the finance and operating lease distinctions. IFRS 16 is effective for annual periods beginning on or after January 1, 2019 with earlier adoption permitted, but only if also applying IFRS 15 - *Revenue from Contracts with Customers*. The Company is currently evaluating the impact of IFRS 16 on its financial statements and plans to adopt the new standard on the required effective date.

BUSINESS RISKS AND UNCERTAINTIES

The Company is subject to a number of risks and uncertainties that can significantly affect its business, financial condition and future financial performance. The Company has a comprehensive process to identify, manage, and mitigate risk, wherever possible. The risks and uncertainties described below are not necessarily the only risks the Company faces. Additional risks and uncertainties that are presently unknown to the Company or deemed immaterial by the Company may adversely affect the Company's business.

History of Operating Losses and Negative Cash Flow

Nanotech continues to be an expenditure-based entity which incurred substantial losses since inception and may continue to incur losses and experience negative cash flows. The Company cannot predict if or when it will operate profitably, reliably generate positive cash flows, or be able to implement its business strategy successfully. Pursuit of the business strategy requires Nanotech to incur significant expenditures for research and product development, marketing, and general administrative activities. As a result, there is a need to continue to grow revenues and gross margins to achieve and sustain profitability and positive operating cash flows, and the Company may need to raise additional capital.

Financing Arrangements

Execution of the business plan and commercial viability could be jeopardized if Nanotech is unable to raise additional funds for working capital, R&D projects, sales, marketing and product development activities, as well as other business opportunities. Mitigation of this risk is attempted by generating funds from a variety of sources including through debt financing, the sale of common equity, government funding, collaboration partners, vendor financing and revenues from the Company's commercial products.

If the cash generated from the Company's business becomes insufficient to fund future capital requirements, the Company will require additional financing. The Company's ability to access capital markets on terms that are acceptable will be dependent on prevailing market conditions, as well as the Company's future financial condition. Although the Company does not have any reason to anticipate unusual difficulties in raising funds in the future, there can be no assurance that capital will be available on suitable terms and conditions or at all.

Acquisitions

The Company has in the past and may continue to expand its operations and business by acquiring additional businesses, products, or technologies. There can be no assurance that the Company will be able to identify, acquire, obtain required regulatory approvals, profitably manage additional businesses, or successfully integrate any acquired businesses, products or technologies into the Company without substantial expenses, delays or other operational, regulatory, or financial problems. Furthermore, acquisitions may involve a number of additional risks, including diversion of management's attention, failure to retain key personnel, unanticipated events or circumstances, unidentified pre-closing liabilities and other legal liabilities, some or all of which could have an adverse effect on the Company's business, results of operations and financial condition. In addition, there can be no assurance that any acquired businesses, products, or technologies will achieve anticipated revenues and income growth. Acquisitions could also result in potentially dilutive issuances of equity securities. The failure of the Company to manage its acquisitions strategy successfully could have a material adverse effect on the Company's business, results of operations and financial condition.

Fixed Costs

The Company requires a staff of specialized employees, as well as specialized manufacturing and test facilities, to perform under its contracts. In order to maintain its ability to compete, the Company must continuously retain the services of a core group of specialists. This reduces the Company's flexibility to reduce workforce costs in the event of a slowdown or downturn in its business. In addition, the manufacturing and test facilities the Company owns or leases under long-term agreements are fixed costs that cannot be adjusted quickly to account for significant variance in production requirements or economic conditions.

Dependence on Key Personnel

The success of the Company is largely dependent on the abilities and experience of its executive officers and other key personnel. Competition for highly skilled management, technical, research and development, and other personnel is intense in the Company's industry. There can be no assurance that the Company can retain its current executive officers or key personnel, or attract and retain additional executive officers or key personnel as needed. The loss of certain executive officers or key personnel could have an adverse impact upon the Company's growth, operations and profitability.

Significant Competition

Many of the Company's competitors are larger and have substantially greater resources than the Company. Furthermore, it is possible that other domestic or foreign companies or governments, some with greater experience in the industry in which the Company operates and many with greater financial resources than the Company possesses, could seek to produce products that compete with the Company's products, including the use of new technology which could render the Company's products less competitively viable. Some of the Company's foreign competitors currently benefit from, and others may benefit in the future from, subsidies or protective measures by their home countries. Furthermore, government agencies may at any time decide to perform similar work as the Company either for themselves or for other government agencies, effectively competing with the Company.

The Company's financial performance is dependent on its ability to generate a sustainable order rate for its manufacturing operations. This can be challenging and may fluctuate on an annual and quarterly basis as the number of contracts awarded varies and is difficult to predict. There is also competitive pressure on pricing and other material contractual terms, such as those terms allocating risk between the manufacturer and its customers.

Economic and Political Conditions

Customer demand for the Company's products may be affected by economic and political conditions on an international, national, and/or regional level. For example, changes in interest rates, foreign exchange rates, credit availability, the level of government spending, the cyclical nature of capital markets, and political decisions may adversely influence the Company's sales or the Company's ability to access certain funding.

Insurance

The Company maintains an extensive program of insurance coverage in the normal course of business, consistent with similar businesses. In addition, the insurance program covers some of the unique risks encountered by the Company. Although the limits and deductibles of such insurance have been established through risk analysis and the recommendation of professional advisors, there can be no assurance that such insurance will remain available to the Company at commercially reasonable rates or that the amount of such coverage will be adequate to cover all liability incurred by the Company. If the Company is held liable for amounts exceeding the limits of its insurance coverage or for claims outside the scope of that coverage, its business, results of operations, and financial condition could be adversely affected.

Market Acceptance

The Company cannot accurately predict whether its products and services will achieve significant market acceptance or whether there will be a market for its products and services on terms the Company finds acceptable. Market acceptance of the Company's products and services depends on a number of factors, including the quality, sophistication, price and availability of substitute products and services. Lack of significant market acceptance, delays in acceptance, failure of certain markets to develop or the Company's need to make significant investments to achieve acceptance by the market would negatively affect its business, financial condition and results of operations.

Customer Dependence and Concentration

In 2018, one customer represented 79% of our total revenue (2017 – two customers represented 75% and 21% of total revenues). The loss of a significant customer or any significant contract cancellations could negatively affect revenue and results of operations.

Government Contracts and Funding

Changes in government policies, priorities or regulations, funding levels through agency or program budget reductions, the imposition of budgetary constraints or the lack of government appropriations, the delay and/or deferment in governmental contract approvals or government programs could have a material adverse effect on the Company's financial condition, results of operations, or future growth. A decline in governmental support and funding for programs in which the Company or its customers participate could result in contract terminations, delays in contract rewards, failure to exercise contract options, cancellation of planned procurements and fewer new business opportunities, any of which could have a material adverse effect on the Company's financial condition and results of operations.

Quality Issues and Contract Performance

The Company sells complex products that could contain defects in design, manufacture and implementation. The products the Company develops and manufactures are technologically advanced and complex. Defects may also occur in components and products that the Company purchases from third parties. The Company employs sophisticated design and testing processes. However, there can be no assurance that the Company's products will be successfully implemented or will pass required acceptance criteria. There can be no assurance that the Company will be able to detect and fix all defects in the products it sells. Failure to do so could result in lost revenue, harm to reputation, significant warranty and other expenses, and could have a material adverse impact on the Company's financial condition and operating results. In addition, a failure with respect to any product may adversely affect the perception by the Company's customers of the quality of its products and may materially and adversely affect the Company's ability to win new contracts.

Security Environment

Many of the Company's customers have specific security requirements relating to the work that can be performed for them. These requirements can change quickly and with little notice causing a reduction or even elimination of potential work for the Company and the ability of the Company to participate in future business. Any reduction or elimination of work could have an adverse effect on the revenues and margins of the Company.

Cyber Security

The Company faces the risk of a security breach or other significant disruption of its IT networks and related systems, whether through cyber-attack or cyber intrusion via the internet, malware, computer viruses and email attachments to persons with access to the Company's systems. Security breaches or other significant disruptions of the Company's IT networks and related systems could have a material adverse effect on the Company's business and results of operations.

Although the Company makes significant efforts to maintain the security and integrity of its IT networks and related systems, there can be no assurance that its security efforts and measures will be effective or that attempted security breaches or disruptions will not be successful or damaging. The Company may also need to expend significant resources to protect against security breaches.

Technological Change

The banknote, branding and security markets in which the Company operates are characterized by changing technology and evolving industry standards. The Company's actual and planned products embody complex technology which may not always be compatible with current and evolving technical standards developed by others. Failure or delays by the Company to meet or comply with the requisite and evolving industry or user standards could have a material adverse effect on the Company's business, results of operations and financial condition. The Company's ability to anticipate changes in technology, technical standards and the needs of the industries it serves or proposes to serve will be a significant factor in the Company's ability to compete or expand into new markets.

Retention of Markets and Development of New Offerings

The Company may experience design, manufacturing, marketing and other difficulties that could delay or prevent the development, introduction or acceptance of new products and enhancements. There can be no assurance the Company will be able to anticipate and achieve the technological advances necessary to remain competitive and profitable, that new products or enhancements will be developed and manufactured on schedule or on a cost-effective basis, or that the Company's existing products will not become technologically obsolete. The Company's failure to accurately predict the needs of current and prospective customers, and to develop products or enhancements that address those needs, may result in the loss of current customers or the inability to secure new customers.

Intellectual Property Rights

To protect the Company's proprietary rights, the Company relies on a combination of patent protections, copyrights, trade secrets, trademark laws, confidentiality agreements with employees and third parties, and protective contractual provisions such as those contained in licence agreements with consultants, subcontractors, vendors and customers. Despite these efforts, the Company's intellectual property rights may be invalidated, circumvented, challenged, infringed, or required to be licensed to others, which could have a material adverse effect on the Company's business, financial condition or operating results. An infringement or misappropriation could harm any competitive advantage the Company currently derives or may derive from its proprietary rights. Litigation may be necessary to enforce or protect the Company's intellectual property rights, protect its trade secrets or determine the validity and scope of the proprietary rights of others. Such litigation may be time-consuming and expensive to prosecute or defend and could result in the diversion of the Company's time and resources.

If any of the Company's technology violates proprietary rights, including copyrights and patents, third parties may assert infringement claims against the Company. Any claims from third parties may also result in limitations on the Company's ability to use the intellectual property subject to these claims. The Company may be required to redesign its products or obtain licences from third parties to continue offering the Company's products without substantially re-engineering such products or defending itself and its customers against infringement claims and liability for damages. This may affect the Company's operations and, in addition, the Company could suffer substantial costs in defending itself against infringement claims.

ADDITIONAL INFORMATION

Outlook

Nanotech's position in the banknote market continues to improve. The Company's strategy to disrupt the multibillion-dollar banknote market and become a key supplier of banknote security features is on track, and the Company is gaining recognition in the industry as having innovative technologies to address the needs of central banks around the world.

In commercial markets, the Company continues to make advancements in positioning its KolourOptik technology as an upgrade and replacement to traditional holograms. In 2019, the Company expects to introduce new and innovative products into the banknote and commercial markets as well as make a significant investment into building out its sales organization.

Management has established the following goals for the 2019 fiscal year:

- **Create a direct salesforce.** Nanotech will create a salesforce to accelerate the sales process by focusing on direct sales in addition to working with key partners. The Company will also put in place a more scalable sales process that will focus on diversifying its customer base and demonstrating its differentiation through commercial sales. To date Nanotech has focused on large opportunities and developing customized offerings on indeterminate timelines. The Company will develop a more traditional sales pipeline, creating the necessary process and channel development strategies to target both small and large customers with defined products.

- **Banknote market.** The Company has two areas of focus in the banknote market:
  - **Contract development activities.** Nanotech currently generates most of its revenue from development contracts with a single customer, with the goal of incorporating a Nanotech security feature on their banknote. This work is progressing well. The customer has narrowed the scope of development activities, which should see the Company move to manufacturing production level volume samples in fiscal 2020.
  - **Expand and enhance our banknote product line.** The Company plans to brand its currently unbranded products such as OTF and extend the product line with a new version of the Company's branded banknote product, M^2. This will enable central banking customers to have a menu of options for their needs and cost parameters.
- **Commercial markets.** The Company plans to launch a new line of product offerings featuring KolourOptik technology targeted directly at the commercial market. As well, the Company is in the process of securing a reliable and timely manufacturing solution for commercial size quantities of KolourOptik labels. Previously, Nanotech relied on large partners that were prohibitively expensive or took several months for delivery, making selling to commercial customers difficult. By implementing these strategies, Nanotech will be able to sell directly to commercial customers and deliver a complete security label to showcase customers' brand identity.

- **Financial outlook.** Management continues to believe the Company's technology has significant potential in many markets. Successfully incorporating a security feature into a banknote will lead to longer-term recurring, predictable revenue. Diversification into commercial markets is also expected to stabilize revenues and earnings. In the short-term, while management builds out the sales strategy and product offering, the Company's financial performance may be highly variable. Management has forecasted the following for 2019:
  - **Based on current visibility and conservatively assuming no additional contracts that could be won during the year, revenue may decrease by 10% to 20% compared to 2018.** Nanotech will continue to generate most of its 2019 revenue from development contracts with a single customer. While the Company is getting closer to reaching the goal of incorporating a Nanotech security feature on this customer's banknote, advancement towards this goal corresponds with the customer narrowing the scope of development activities with an intention to select a final security feature. This selection will see the Company move to manufacturing production volume samples in fiscal 2020. While focusing on one security feature is a positive development, because the scope of work has been reduced, overall 2019 revenues may be negatively impacted. Nanotech continues to operate under an agreement to provide up to $30 million in research and development services. Only $10.5 million of this revenue has been recognized as of September 30, 2018.

  - **Adjusted EBITDA loss of approximately $1.0 million.** Potential declining revenue and increased investment in the Company's sales efforts and product offerings could reduce near-term profitability.

With a strong balance sheet, including $9,613,621 in cash and short-term investments and no debt, the Company is well positioned to develop and pursue its sales strategies in 2019.

Public Securities Filings

Additional information about Nanotech, is available on the Company's website at www.nanosecurity.ca, or on SEDAR at www.sedar.com.

Consolidated Financial Statements of

Nanotech Security Corp.

Years ended September 30, 2018 and 2017

Nanotech Security Corp.
September 30, 2018 and 2017

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INDEPENDENT AUDITORS' REPORT

To the Shareholders of Nanotech Security Corp.

We have audited the accompanying consolidated financial statements of Nanotech Security Corp., which comprise the consolidated statements of financial position as at September 30, 2018 and September 30, 2017, the consolidated statements of operations and comprehensive loss, changes in shareholders' equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards, and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Nanotech Security Corp. as at September 30, 2018 and September 30, 2017 and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.

KPMG LLP

Chartered Professional Accountants

December 18, 2018
Vancouver, Canada

Nanotech Security Corp.

Consolidated Statements of Operations and Comprehensive Loss
Years ended September 30, 2018 and 2017

(In Canadian dollars)

	2018	2017
Revenue (note 16)	$ 9,199,710	$ 7,343,791
Cost of sales (note 17)	2,051,890	1,429,371
	7,147,820	5,914,420
Expenses (note 17)		
Research and development	1,407,430	1,475,437
General and administration	2,532,156	2,308,846
Sales and marketing	2,018,055	2,043,514
Depreciation and amortization (note 7 and 8(b))	1,485,024	2,755,882
	7,442,665	8,583,679
Loss from continuing operations before other expenses	(294,845)	(2,669,259)
Other (income) expenses		
Foreign exchange (gain) loss	(250,023)	169,815
Finance (income) expense (note 9)	(121,878)	1,014,779
	(371,901)	1,184,594
Net income (loss) from continuing operations	77,056	(3,853,853)
Net loss from discontinued operations (note 19(c))	(123,322)	(900,279)
Net loss	(46,266)	(4,754,132)
Other comprehensive loss:		
Items that may be subsequently reclassified to earnings:		
Unrealized foreign exchange gain (loss) on translation of foreign operation (note 19(c))	(98,908)	85,605
Total comprehensive loss	$ (145,174)	$ (4,668,527)
Basic and diluted earnings (loss) per share:		
Continuing operations	$ 0.00	$ (0.07)
Discontinued operations	$ 0.00	$ (0.01)
Net loss	$ 0.00	$ (0.08)
Weighted average number of common shares		
Basic and diluted	68,425,673	59,056,353

See accompanying notes to the consolidated financial statements.

Nanotech Security Corp.

Consolidated Statements of Financial Position
as at September 30, 2018 and 2017

(In Canadian dollars)

	2018	2017
Assets		
Current assets:		
Cash and cash equivalents	$ 2,014,764	$ 10,883,919
Short-term investments (note 5)	7,598,857	-
Accounts receivable (note 12(b))	1,962,969	1,374,442
Inventory (note 6)	173,636	151,708
Prepaid expenses and other assets	125,514	187,874
Assets held for sale (note 19(a))	-	216,225
	11,875,740	12,814,168
Property, plant and equipment (note 7)	16,964,857	15,856,998
Goodwill (note 8(a))	1,388,458	1,388,458
	$ 30,229,055	$ 30,059,624
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	$ 1,265,282	$ 1,431,466
Deferred revenue	-	157,171
Liabilities directly associated with assets held for sale (note 19(a))	16,204	200,226
	1,281,486	1,788,863
Non-current liabilities:		
Tenant inducement	43,653	71,223
	1,325,139	1,860,086
Shareholders' equity		
Share capital (note 10(a))	61,892,395	61,426,483
Contributed surplus	2,930,964	2,715,137
Deficit	(35,919,443)	(35,873,177)
Accumulated other comprehensive loss	-	(68,905)
	28,903,916	28,199,538
	$ 30,229,055	$ 30,059,624

Related party transactions (note 14)
Commitments (note 18)
See accompanying notes to the consolidated financial statements.

Approved on behalf of the Board of Directors:

"Doug Blakeway"	*"Ken Tolmie"*
Doug Blakeway, Director	Ken Tolmie, Director

Nanotech Security Corp.

Consolidated Statements of Changes in Shareholders' Equity
Years ended September 30, 2018 and 2017

(In Canadian dollars)

	Number of shares	Share capital	Contributed surplus	Deficit	Accumulated other comprehensive loss	Total shareholders' equity
Balance as at October 1, 2016	53,864,285	$ 45,210,507	$ 2,485,131	$ (31,119,045)	$ (154,510)	$ 16,422,083
Net loss	-	-	-	(4,754,132)	-	(4,754,132)
Unrealized foreign exchange gain on translation	-	-	-	-	85,605	85,605
Private placement	11,586,870	12,486,784	-	-	-	12,486,784
Shares issued on conversion of convertible debentures	2,252,000	2,815,000	-	-	-	2,815,000
Share-based compensation - options (note 10(b)(i))			364,649			364,649
Share-based compensation - RSUs (note 10(b)(ii))	-	-	556,549	-	-	556,549
Options exercised (note 10(b)(i))	272,000	346,287	(123,287)	-	-	223,000
RSUs vested (note 10(b)(ii))	420,670	567,905	(567,905)	-	-	-
Balance as at September 30, 2017	68,395,825	$ 61,426,483	$ 2,715,137	$ (35,873,177)	$ (68,905)	$ 28,199,538
Balance as at October 1, 2017	68,395,825	$ 61,426,483	$ 2,715,137	$ (35,873,177)	$ (68,905)	$ 28,199,538
Net loss	-	-	-	(46,266)	-	(46,266)
Unrealized foreign exchange loss on translation	-	-	-	-	(98,908)	(98,908)
Share-based compensation - options (note 10(b)(i))			264,627			264,627
Share-based compensation - RSUs (note 10(b)(ii))	-	-	417,112	-	-	417,112
Foreign exchange reclassified upon disposal of foreign operation (note 19(c))	-	-	-	-	167,813	167,813
RSUs vested (note 10(b)(ii))	375,676	465,912	(465,912)	-	-	-
Balance as at September 30, 2018	68,771,501	$ 61,892,395	$ 2,930,964	$ (35,919,443)	$ -	$ 28,903,916

See accompanying notes to the consolidated financial statements.

Nanotech Security Corp.

Consolidated Statements of Cash Flows
Years ended September 30, 2018 and 2017

(In Canadian dollars)

	2018	2017
Cash flows provided by (used in):		
Operating activities:		
Net income (loss) from continuing operations	$ 77,056	$ (3,853,853)
Items not involving cash:		
Depreciation and amortization	1,611,891	2,917,883
Share-based compensation	681,739	921,198
Accretion of convertible debentures	-	589,858
Other	(27,570)	(27,570)
Non-cash working capital changes (note 15(a))	(889,380)	(720,420)
	1,453,736	(172,904)
Net cash provided by (used in) discontinued operations (note 19(b))	76,694	(574,313)
Cash provided by (used in) operating activities	1,530,430	(747,217)
Investing activities:		
Purchase of property and equipment (note 7 and 15(d))	(2,701,820)	(106,944)
Acquisition of short-term investments (note 5)	(7,598,857)	-
Cash used in investing activities	(10,300,677)	(106,944)
Financing activities:		
Issuance of shares for options exercised	-	223,000
Proceeds on financing, net of costs (note 9)	-	12,486,784
Repayment of note payable (note 9)	-	(3,000,000)
Repayment of convertible debentures (note 9)	-	(1,370,000)
Cash provided by financing activities	-	8,339,784
Effect of foreign exchange on cash and cash equivalents	(98,908)	85,605
Increase (decrease) in cash and cash equivalents	(8,869,155)	7,571,228
Cash and cash equivalents, beginning of year	10,883,919	3,312,691
Cash and cash equivalents, end of year	$ 2,014,764	$ 10,883,919

See supplementary cash flow information (note 15)
See accompanying notes to the consolidated financial statements.

1. Summary of business:

Nanotech Security Corp. (the "Company" or "Nanotech") is incorporated under the laws of British Columbia with common shares listed on the TSX Venture Exchange (trading symbol: NTS) and quoted in the United States on the OTCQX Market (trading symbol: NTSFF). The Company's head office is located at #505 - 3292 Production Way, Burnaby, British Columbia, Canada V5A 4R4.

Nanotech researches, creates, and produces nano-optic structures and colour-shifting materials used in authentication and brand enhancement applications across a wide range of markets including banknotes, tax stamps, secure government documents, commercial branding, and the pharmaceutical industry.

2. Basis of preparation:

(a) *Statement of compliance:*

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). The financial statements were approved by the Company's Board of Directors and authorized for issue on December 18, 2018.

(b) *Basis of measurement:*

These consolidated financial statements are presented in Canadian dollars and have been prepared on a historical cost basis, except for certain financial instruments which are measured at fair value.

(c) *Use of estimates, assumptions and judgments*:

The preparation of financial statements requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the date of the financial statements and the reported amounts of revenue and expenses during the reporting period. Actual results could differ from those estimates. The estimates and underlying assumptions are reviewed by management on an ongoing basis. Revisions to accounting estimates are accounted for prospectively. The key sources of estimation uncertainty that have a significant risk of causing material adjustment to the carrying amounts of assets and liabilities are discussed below:

(i) Valuation of goodwill:

Goodwill arising on an acquisition of a business is carried at cost, as established at the date of acquisition of the business less impairment losses, if any. For purposes of impairment testing, goodwill is allocated to each of the Company's cash-generating units ("CGU") that is expected to benefit from the synergies of the combination. A CGU to which goodwill has been allocated is tested for impairment annually, or more frequently when there is an indication that the CGU may be impaired.

2. Basis of preparation (continued):

(c) *Use of estimates, assumptions and judgments (continued):*

(i) Valuation of goodwill (continued):

Management evaluates goodwill for impairment annually as of September 30th. Impairment tests involve considerable use of judgement and require management to make estimates and assumptions. The fair values of CGUs are derived from certain valuation models, which consider various factors such as discount rates, future earnings, and revenue growth rates. While management uses their best estimate and assumptions to assess goodwill impairment, there are inherent uncertainties in projecting future cash flows.

(ii) Judgments:

Management uses judgment when applying accounting policies and when making estimates and assumptions as described above. The most significant areas that require judgment include determination of functional currency, the estimated useful life of property, plant and equipment, and determination of CGUs and segments.

(d) *Basis of consolidation:*

These consolidated financial statements include the accounts of the Company and its wholly-owned subsidiary, Tactical Technologies Inc. ("Tactical") up to September 28, 2018, the date of its dissolution (note 19). All intercompany balances and transactions are eliminated on consolidation. The financial statements of the subsidiaries are included in the consolidated financial statements from the date that control commences.

(e) *Foreign currency translation:*

The consolidated financial statements of the Company are presented in Canadian dollars. The functional currency of the Company is the Canadian dollar. Tactical's functional currency was the U.S. dollar.

(i) Transactions in foreign currency:

Each entity within the consolidated group records transactions using its functional currency, being the currency of the primary economic environment in which it operates. Foreign currency transactions are translated into the respective functional currency of each entity using the foreign currency rates prevailing at the date of the transaction. Period end balances of monetary assets and liabilities in foreign currency are translated to the respective functional currencies using period end foreign currency rates. Foreign currency gains and losses arising from settlement of foreign currency transactions are recognized in earnings.

(ii) Foreign operations translation:

The assets and liabilities of foreign operations are translated into Canadian dollars at period end foreign currency rates. Revenues and expenses of foreign operations are translated into Canadian dollars at average rates for the period. Foreign currency translation gains and losses are recognized in other comprehensive loss. The relevant amount in accumulated other comprehensive loss is reclassified into earnings upon disposition of a foreign operation (note 19(c)).

3. Significant accounting policies:

(a) *Revenue recognition:*

Revenue is measured at the fair value of consideration received or receivable, net of discounts and after eliminating intercompany sales.

The Company's contracts with customers may include multiple deliverables that fall within one or more of the revenue categories described below. Where revenue arrangements have separate identifiable components, the consideration received is allocated to each identifiable component and the applicable revenue recognition criteria are applied to each of the components.

Revenue from the sale of products is recognized when all of the following conditions have been met:

- title and risk involving the products are transferred to the buyer;
- the Company's managerial involvement over the goods ceases to exist;
- the amount of revenue can be measured reliably;
- it is probable that the economic benefits associated with the transaction will flow to the Company; and
- the costs incurred in respect of the transaction can be measured reliably.

If there is a requirement for customer acceptance of any products shipped, revenue is recognized only after customer acceptance has been received. Payments received in advance of the satisfaction of the Company's revenue recognition criteria are recorded as deferred revenue.

Revenue from development contracts are recognized by reference to the stage of completion based on services performed to date as a percentage of total services to be performed or on a straight-line basis over the term of the contract, if revenue is determined to be earned evenly.

(b) *Earnings (loss) per common share:*

Basic net earnings (loss) per common share is calculated using the weighted average number of common shares outstanding during the year.

Diluted net loss per share reflects the potential dilution of common share equivalents, such as outstanding stock options and restricted share units ("RSU"), in the weighted average number of common shares outstanding during the year, if dilutive. For this purpose, the "treasury stock method" is used for the assumed proceeds upon the exercise of outstanding stock options that are used to purchase common shares at the average market price during the period. For the periods recording a loss, basic and diluted figures are the same, as the exercise of all stock options and RSUs would be anti-dilutive.

(c) *Research and development:*

Research costs are expensed in the period incurred. Development costs are capitalized and recorded as an intangible asset only if technical feasibility has been established and the Company expects to generate probable future economic benefits from the asset created on completion of development. The costs capitalized include materials, direct labour, directly attributable overhead expenditures, and borrowing costs on qualifying assets. Other development costs are expensed in the period incurred. During the years ended September 30, 2018 and 2017, all development costs have been expensed.

3. Significant accounting policies (continued):

(d) *Government assistance and investment tax credits:*

Government assistance includes government grants and investment tax credits and is recognized when there is reasonable assurance that the Company will comply with the relevant conditions and that the government assistance will be received. Government assistance that meets the recognition criteria and relates to current expenses is recorded as a reduction of research and development expense.

Government assistance that meets the recognition criteria and relates to the acquisition of an asset is recorded as a reduction of the cost of the related asset. If government assistance becomes repayable, the inception to date impact of assistance previously recognized in earnings is reversed immediately in the period that the assistance becomes repayable.

Investment tax credits are recorded using the cost-reduction method whereby the credits are deducted from the cost of the related asset or expenditure when there is reasonable assurance that the investment tax credit will be realized. Where a valuation allowance has been recorded against prior year's investment tax credits, the Company applies the credits on a first-in first-out basis with a recovery of prior year's investment tax credits recognized as an income tax recovery.

(e) *Financial instruments:*

Financial assets and financial liabilities are initially measured at fair value and are subsequently re-measured based on their classification as described below. Transaction costs that are directly attributable to the acquisition or issuance of a financial asset or liability, other than financial assets and liabilities recorded at fair value through earnings, are added or deducted from the fair value of the respective financial asset or financial liability on initial recognition. Transaction costs that are directly attributable to the acquisition of a financial asset or financial liability recorded at fair value through earnings are recognized immediately in earnings.

Financial assets and liabilities are offset and the net amount is reported in the Statement of Financial Position when there is a legally enforceable right to offset the recognized amounts and there is an intention to settle on a net basis or realize the asset and settle the liability simultaneously.

(i) Financial assets:

Financial assets are classified into the following categories: financial assets at fair value through earnings, loans and receivables, and available-for-sale. The classification depends on the nature and purpose of the financial asset and is determined at the time of initial recognition.

- Financial assets at fair value through earnings:
  Financial assets are classified as fair value through earnings when held for trading or if designated into this category. Financial assets classified as financial assets at fair value through earnings are measured at fair value with any gains or losses arising on remeasurement recognized in earnings. The Company does not have any financial assets classified as fair value through earnings.

3. Significant accounting policies (continued):

(e) *Financial instruments (continued):*

(i) Financial assets (continued):

- Loans and receivables:
  Loans and receivables include cash and cash equivalents, short-term investments, and accounts receivable. Loans and receivables are initially measured at fair value and are subsequently remeasured at amortized cost using the effective interest method, less any impairment losses. The Company has classified cash and cash equivalents and accounts receivables as loans and receivables.

- Available-for-sale financial assets:
  Available-for-sale financial assets are non-derivative financial assets that are either designated in this category or not classified into any of the other categories. Available-for-sale financial assets are measured at fair value with any gains or losses on remeasurement recognized in other comprehensive income until the financial asset is derecognized or is determined to be permanently impaired, at which time the gain or loss accumulated in equity is transferred to earnings. The Company does not have any financial assets classified as available-for-sale assets.

Financial assets are derecognized when the rights to receive cash flows from the assets have expired or have been transferred, and the Company has transferred substantially all of the risks and rewards of ownership.

(ii) Financial liabilities:

Financial liabilities are classified as either financial liabilities at fair value through earnings or as other financial liabilities.

- Other financial liabilities:
  Other financial liabilities include trade and other payables, non-trade payables, and long-term debt. They are initially measured at fair value and are subsequently measured at amortized cost using the effective interest method. The Company has classified accounts payables and accrued liabilities as other financial liabilities.

(iii) Embedded derivatives:

Derivatives embedded in non-derivative host contracts are treated as separate derivatives when they meet the definition of a derivative, their risks and characteristics are not closely related to those of the host contracts and the contracts are not measured at the fair value through earnings. Embedded derivatives are recorded at the fair value through earnings. During the years ended September 30, 2018 and 2017, the Company did not have any embedded derivatives.

(f) *Cash and cash equivalents:*

Cash and cash equivalents consist of cash balances with banks, investments with original maturities of three months or less, and investments that are both readily convertible to cash and subject to insignificant changes in market value.

3. Significant accounting policies (continued):

(g) *Short-term investments*

Short-term investments consist of short-term interest-bearing term deposits which are highly liquid with maturity dates greater than three months but less than one year at the time of purchase.

(h) Inventory:

Inventory is measured at the lower of cost and net realizable value and consists primarily of raw materials used in the manufacturing of optical thin film. Raw materials cost is determined on a weighted average basis. The cost of work in progress and finished goods includes the cost of raw material, direct labour and an allocation of related overheads. Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion and selling expenses.

(i) *Property, plant and equipment:*

Property, plant and equipment are measured at cost less accumulated depreciation and accumulated impairment losses. The initial cost of an asset comprises its purchase price and any costs directly attributable to bringing the asset into working condition for its intended use. Assets acquired in a business combination are measured at the fair value of the assets at the time of acquisition. Repairs and maintenance costs are charged directly to the statement of operations as incurred. Depreciation is calculated using the following methods and annual rates:

	Estimated useful life
Software	100% declining balance
Laboratory and office equipment	20 – 55% declining balance
Manufacturing equipment	10% declining balance
Building	4% declining balance
Leasehold improvements	straight line over the lesser of lease term or estimated useful life

The Company reviews the estimated useful lives and the depreciation methods of its property, plant and equipment annually.

(j) *Intangible assets and goodwill:*

(i) Intangible assets:

Intangible assets with finite lives consist of acquired intellectual property and are measured at cost less accumulated amortization and accumulated impairment losses. Cost for intangible assets acquired in a business combination represents the fair value of the asset at the time of the acquisition. Intangible assets with finite lives are amortized over four years. At September 30, 2018 and 2017, the Company did not have any indefinite life intangible assets other than goodwill.

(ii) Goodwill:

Goodwill arising on an acquisition of a business is carried at cost, as established at the date of acquisition of the business less accumulated impairment losses, if any. Goodwill is not amortized but is tested for impairment annually or whenever there is an indication of impairment.

3. Significant accounting policies (continued):

(k) *Impairment:*

(i) Financial assets:

Financial assets not carried at fair value through earnings are assessed for impairment at each reporting date. A financial asset is impaired if objective evidence indicates that a loss event which negatively affected the estimated future cash flows has occurred after the initial recognition of the asset. For financial assets measured at amortized cost, the impairment loss is the difference between the carrying amount and the present value of the estimated future cash flows, discounted at the original effective interest rate. If an impairment has occurred, the carrying amount of the asset is reduced to its recoverable amount, with the amount of the loss recognized in earnings. A permanent impairment loss for an available-for-sale investment is recognized by transferring the cumulative loss previously recognized in other comprehensive income to earnings.

(ii) Non-financial assets:

Goodwill and non-financial assets are tested for impairment annually, or whenever events or changes in circumstances indicate that an asset's carrying amount may be less than its recoverable amount. Management uses judgment to estimate the inputs to these assessments and any changes to these inputs could have a material impact on the impairment calculation. For impairment testing, non-financial assets that do not generate independent cash flows are grouped together into a CGU, which represent the level at which largely independent cash flows are generated. Goodwill is allocated to groups of CGUs based on the level at which it is monitored for internal reporting purposes. An impairment loss is recognized in earnings to the extent that the carrying value of an asset, CGU or group of CGUs exceeds its estimated recoverable amount. The recoverable amount of an asset, CGU or group of CGUs is the greater of its value in use and its fair value less cost to sell. Value in use is calculated as the present value of the estimated future cash flows discounted at appropriate discount rates. An impairment loss relating to a specific asset reduces the carrying value of the asset.

An impairment loss relating to a CGU or group of CGUs reduces the carrying value of the goodwill allocated to the CGU or group of CGUs, then reduces the carrying value of the other assets of the CGU or group of CGUs on a pro-rata basis. An impairment loss in respect of goodwill is not reversed. A previously recognized impairment loss related to other non-financial assets is assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss related to other non-financial assets is reversed if there is a subsequent increase in recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying value does not exceed the carrying value that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

(l) *Provisions:*

Provisions represent liabilities for which the amount or timing is uncertain. Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that an outflow of resources embodying economic benefits will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. Where appropriate, the future cash flow estimates are adjusted to reflect risks specific to the liability.

3. Significant accounting policies (continued):

(m) *Share-based payments:*

The Company makes share-based payments to directors, consultants and employees. The compensation expense for share-based payment is determined based on the fair value at the grant date using the Black-Scholes option-pricing model and is recorded in the statement of operations over the vesting period. Management uses judgment to determine the inputs to the Black-Scholes option-pricing model including the expected award lives, underlying share price volatility and forfeiture rates. Volatility is estimated by considering the Company's historic share price volatility over similar periods to the expected life of the awards under consideration. Changes in these assumptions will impact the calculation of fair value and the amount of compensation expense recognized in earnings. When stock options are exercised, any consideration paid by directors, consultants and employees, as well as the related stock-based compensation, is credited to share capital.

(n) *Restricted share units:*

During the year ended September 30, 2015, the Company adopted a RSU plan. The obligations under the RSU plan can be settled at the Company's discretion through either cash or the issuance of common shares. The Company measures the cost of equity-settled share-based transactions by reference to the fair value of the equity instruments at the date at which they are granted and is recorded in the statement of operations over the vesting period. For RSUs, the Company uses the TSX Venture Exchange share price at the grant date as fair value of the RSUs. The resulting fair value is then adjusted for an estimated forfeiture amount. Determination of the forfeiture rate is based on historical experience. The actual number of RSUs that vest is likely to be different from estimation.

(o) *Income taxes:*

Income tax expense is comprised of current and deferred tax. Current and deferred tax are recognized into earnings except to the extent that it relates to a business combination or items recognized directly in other comprehensive income or share capital.

Current tax is the expected tax payable or receivable on the taxable income or loss for the year, using tax rates enacted or substantively enacted at the reporting date, and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized in respect of temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes.

Deferred tax is not recognized for the following temporary differences; the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable earnings, and differences relating to investments in subsidiaries and jointly controlled entities to the extent that it is probable that they will not reverse in the foreseeable future. In addition, deferred tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

3. Significant accounting policies (continued):

(o) *Income taxes (continued):*

Deferred tax assets are recognized for unused tax losses, tax credits and deductible temporary differences, to the extent that it is probable that future taxable profits will be available against which they can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

(p) *Leases:*

Leasing contracts are classified as either finance or operating leases based on the substance of the contractual arrangement at inception date. A lease is classified as a finance lease if it transfers substantially all of the risks and rewards of ownership of the leased asset. Where the contracts are classified as finance leases, upon initial recognition, the asset and liability are recorded at the lower of fair value and the present value of the minimum lease payments, net of executory costs. Finance lease payments are apportioned between interest expense and repayments of the liability. Where the contracts are classified as operating leases, they are not recognized in the Company’s Consolidated Statements of Financial Position and lease payments are charged to earnings as they are incurred on a straight-line basis over the lease term.

(q) *Segment reporting:*

The Company’s continuing operations currently consists of one operating segment.

(r) *Assets held for sale and discontinued operations:*

(i) Assets held for sale:

The Company classifies assets, or disposal groups, as held for sale when it expects to recover their carrying amounts primarily through sale rather than through continuing use. To meet criteria to be held for sale, the sale must be highly probable, and the assets or disposal groups must be available for immediate sale in their present condition. The Company must be committed to a plan to sell the assets or disposal group, and the sale should be expected to qualify for recognition as a completed sale within one year from the date of classification.

The Company measures assets or disposal groups at the lower of their carrying amount and fair value less costs to sell. Any impairment loss on a disposal group is first allocated to goodwill, and then to remaining assets and liabilities on a pro-rata basis, except that no loss is allocated to inventories or financial assets. Impairment losses on initial classification as held for sale and subsequent losses on remeasurement are recognized in the statement of income. Upon classifying asset or disposal groups as held for sale, the Company presents the assets separately as a single amount and the associated liabilities separately as a single amount on the Consolidated Statements of Financial Position. Comparative period Consolidated Statements of Financial Position are not restated. Assets held for sale are not depreciated, depleted, or amortized.

3. Significant accounting policies (continued):

(r) *Assets held for sale and discontinued operations (continued):*

(ii) Discontinued operations:

A discontinued operation is a component of the Company's business that represents a separate major line of business or geographical area of operations that has been disposed of or classified as held for sale. The operations and cash flows can be clearly distinguished from the rest of the Company, both operationally and for financial reporting purposes. When the Company classifies an operation as a discontinued operation, it represents the comparative Consolidated Statements of Operations as if the operation had been discontinued from the start of the comparative year. In doing this, the Company excludes the results for the discontinued operations and any gain or loss from disposal from the consolidated statements of operations from continuing operations and presents them on a separate line as profit or loss (net of tax) from the discontinued operation. Per share information and changes to other consolidated comprehensive loss related to discontinued operations are presented separately from continuing operations. Cash flows from discontinued operations are presented separately from cash flows from continuing operations in the Consolidated Statements of Cash Flows.

4. New standards and interpretations not yet adopted:

(a) *IFRS 9 – Financial Instruments:*

In July 2014, the IASB issued IFRS 9 – *Financial Instruments*, which replaces the earlier versions of IFRS 9 (2009, 2010, and 2013) and completes the IASB's project to replace IAS 39 – *Financial Instruments: Recognition and Measurement*. IFRS 9 includes a logical model for classification and measurement of financial assets and a single, forward-looking 'expected credit loss' impairment model. IFRS 9 is effective for annual periods beginning on or after January 1, 2018 and must be applied retrospectively with some exemptions.

The Company will adopt the standard on October 1, 2018 using the modified retrospective application method, under which comparatives are not restated and a cumulative catch up adjustment is recorded on October 1, 2018, for any differences identified including adjustments to opening retained deficit balances. The Company has analyzed the impact of adopting IFRS 9 and anticipates that there will not be any material changes as a result of adopting this new standard.

(b) *IFRS 15 – Revenue from contracts with customers:*

In May 2014, the IASB issued IFRS 15 – *Revenue from Contracts with Customers*, which supersedes IAS 18 – *Revenue,* IAS 11 – *Construction Contracts* and other interpretive guidance associated with revenue recognition. IFRS 15 provides a single, principles-based five-step model to be applied to all contracts with customers to determine how and when an entity should recognize revenue. The standard also provides guidance on whether revenue should be recognized at a point in time or over time as well as requirements for more informative, relevant disclosures. IFRS 15 is effective for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. The Company has completed an assessment of the impact that the initial application of IFRS 15 will have on its financial statements and does not expect that there will be a significant impact, other than additional required disclosures. The Company will adopt IFRS 15 in its financial statements for the annual period beginning on October 1, 2018 using the full retrospective transitional approach.

(Expressed in Canadian dollars)

4. New standards and interpretations not yet adopted (continued):

(c) *IFRS 16 – Leases:*

In January 2016, the IASB issued IFRS 16 – *Leases*, which supersedes IAS 17 – *Leases*. IFRS 16 establishes principles for the recognition, measurement, presentation and disclosure of leases. The standard establishes a single model for lessees to bring leases on balance sheet while lessor accounting remains largely unchanged and retains the finance and operating lease distinctions. IFRS 16 is effective for annual periods beginning on or after January 1, 2019 with earlier adoption permitted, but only if also applying IFRS 15 – *Revenue from Contracts with Customers*. The Company is currently evaluating the impact of IFRS 16 on its financial statements and plans to adopt the new standard on the required effective date.

5. Short-term Investments

Short-term investments of $7,598,857 (2017 - $nil) consist of cashable term deposits held with a Canadian chartered bank. The term deposits have maturity dates between October 23, 2018 and June 25, 2019. Interest rates range between 1.8% and 2.0%.

6. Inventory:

	2018	2017
Raw materials	$ 160,550	$ 123,619
Work in progress	13,086	28,089
	$ 173,636	$ 151,708

As at September 30, 2018, work in progress includes $nil of depreciation (2017 - $1,600).

There were no inventory write-downs during the years ended September 30, 2018 and 2017.

For the year ended September 30, 2018, the Company recognized inventories of $2,051,890 (2017 - $1,429,371) through cost of sales.

(Expressed in Canadian dollars)

7. Property, plant and equipment:

	Land	Building and leasehold improvement	Manufacturing equipment	Laboratory, software, and office equipment	Total
Cost:					
Balance as at October 1, 2016	$ 141,700	$ 3,807,378	$ 15,922,956	$ 520,413	$ 20,392,447
Additions	-	92,009	-	14,935	106,944
Assets held for sale	-	(27,809)	-	(290,293)	(318,102)
Balance as at September 30, 2017	141,700	3,871,578	15,922,956	245,055	20,181,289
Additions	-	487,549	2,083,180	149,021	2,719,750
Balance as at September 30, 2018	$ 141,700	$ 4,359,127	$ 18,006,136	$ 394,076	$ 22,901,039
Accumulated depreciation:					
Balance as at October 1, 2016	$ -	$ 354,128	$ 2,307,509	$ 392,498	$ 3,054,135
Depreciation expense	-	167,144	1,361,544	27,956	1,556,644
Assets held for sale	-	(27,810)	-	(258,678)	(286,488)
Balance as at September 30, 2017	-	493,462	3,669,053	161,776	4,324,291
Depreciation expense	-	203,203	1,329,549	79,139	1,611,891
Balance as at September 30, 2018	$ -	$ 696,665	$ 4,998,602	$ 240,915	$ 5,936,182
Net book value:					
September 30, 2018	$ 141,700	$ 3,662,462	$ 13,007,534	$ 153,161	$ 16,964,857
September 30, 2017	$ 141,700	$ 3,378,116	$ 12,253,903	$ 83,279	$ 15,856,998

Additions, disposals and depreciation for the years ended September 30, 2018 and 2017 are for continuing operations.

Included in amortization is an impairment charge of $29,872 recorded during the year against certain assets in order to bring them down to their recoverable values (2017 - $nil).

(Expressed in Canadian dollars)

8. Intangible assets and goodwill:

(a) *Goodwill impairment:*

The Company performs a goodwill impairment test at least annually on September 30 and whenever there is an indication of impairment. No impairment of goodwill was identified as a result of the Company's most recent annual impairment test.

The key assumptions used in performing the impairment tests:

- Recoverable amount:
  Management's past experience and future expectations of the business' performance are used to make a best estimate of the expected revenues, earnings before interest, taxes, depreciation and amortization, and operating cash flows covering a five year forecast period, with a terminal value extrapolated into the future over the estimated useful life of the CGU using a steady growth rate.

- Discount rate:
  Management applied a discount rate of 12% (2017 – 12%) in calculating the value in use. This is a pre-tax rate which reflects the time value of money and risk associated with the business. Management has determined its discount rate to reflect the risk of an emerging technology company.

- Revenue growth:
  Revenue growth is projected taking into account the average growth levels experienced over the past five years and the estimated growth for the next five years based on projected market acceptance. It is assumed that sales pricing and margins would decrease as volume orders are realized.

- Sensitivity analysis:
  Management performs sensitivity analysis on the key assumptions. Sensitivity analysis indicates reasonable changes to key assumptions will not result in an impairment loss.

(b) *Finite life intangible assets:*

Finite life intangible assets consist of intellectual property acquired by the Company in a 2013 business acquisition. The estimated fair value of $5,444,954 was amortized over four years and was fully depreciated by September 30, 2017. Amortization of $1,361,239 was recorded during the year ended September 30, 2017.

9. Finance (income) expense:

	2018	2017
Interest income from cash and cash equivalents and short-term investments	$ (132,774)	$ (49,772)
Other interest expenses	10,896	11,950
Interest on note payable	-	106,774
Interest on convertible debenture	-	355,969
Accretion of convertible debentures	-	589,858
	$ (121,878)	$ 1,014,779

(Expressed in Canadian dollars)

9. Finance (income) expense (continued):

On June 9, 2016, the Company completed an initial tranche of a non-brokered private placement of unsecured subordinated convertible debentures in the amount of $2,505,000, with a second and final tranche closing on June 21, 2016 in the amount of $1,680,000 for total gross proceeds of $4,185,000, which were payable upon maturity on May 31, 2018.

The convertible debentures accrued interest at a rate of 12% per annum payable quarterly in arrears and were convertible into common shares of the Company at a price of $1.25 per share. The Company had the option to pre-pay the principal sum, in whole or in part, twelve months following the closing, after providing twenty business days notice to the holder.

On May 18, 2017, the Company provided notice to the debenture holders of the Company's intention to repay the convertible debentures on June 21, 2017. On May 18, 2017, the Company recorded accretion expense to bring the carrying value of the debentures to face value of $4,185,000.

Several debenture holders elected to convert their debentures into common shares at $1.25 per share. As a result, the Company issued 2,252,000 common shares valued at $2,815,000. The remaining $1,370,000 was repaid on June 21, 2017.

On August 21, 2017, the Company repaid a fully secured note payable in the amount of $3,000,000 which required interest only payments at a fixed rate of 4% per annum.

10. Share capital:

(a) *Share capital:*

Authorized:

Unlimited number of common shares with no par value

Unlimited number of preferred shares with no par value

Common shares issued and fully paid:

	Number of shares		Amount
Balance as at October 1, 2016	53,864,285	$	45,210,507
Private placement	11,586,870		12,486,784
Debentures converted	2,252,000		2,815,000
Options exercised	272,000		346,287
RSUs vested	420,670		567,905
Balance as at September 30, 2017	68,395,825	$	61,426,483
RSUs vested	375,676		465,912
Balance as at September 30, 2018	68,771,501	$	61,892,395

There are no preferred shares issued and outstanding.

On May 18, 2017, the Company completed a bought deal private placement with a syndicate of underwriters pursuant to which the Company issued 11,586,870 common shares at a price of $1.15 per share, for gross proceeds to the Company of $13,324,901. The Company incurred share issue costs of $838,117.

(Expressed in Canadian dollars)

10. Share capital (continued):

(b) *Share-based payment plans:*

(i) Stock option plan:

Under the Company's share incentive plan, the maximum number of shares that may be reserved for grant of options at any point in time is 10.0% of the outstanding shares less any shares reserved for issuance under the RSU plan. The following stock options were outstanding as at September 30, 2018:

	Number of options	Weighted average exercise price
Balance as at October 1, 2016	2,488,500	$ 1.29
Granted	413,500	1.48
Exercised	(272,000)	0.82
Forfeited or expired	(590,000)	1.42
Balance as at September 30, 2017	2,040,000	$ 1.35
Granted	567,500	1.35
Balance as at September 30, 2018	2,607,500	$ 1.35

The following table summarizes information pertaining to the Company's stock options outstanding as at September 30, 2018:

	Options outstanding			Options exercisable	
Range of exercise prices	Number of options outstanding	Weighted average remaining contractual life (years)	Weighted average exercise price	Number of options exercisable	Weighted average exercise price
$1.01 - $1.25	1,126,500	2.23	$ 1.14	1,001,500	$ 1.13
$1.26 - $1.65	1,481,000	1.89	1.52	1,272,250	1.53
	2,607,500	2.04	$ 1.35	2,273,750	$ 1.35

The Company calculates the fair value of the options at the grant date using the Black-Scholes option-pricing model. The table below outlines the weighted average assumptions used to estimate the fair value of options granted during the years ended September 30, 2018 and 2017:

	2018	2017
Risk free interest rate	1.9%	1.2%
Expected life	4.6 years	4.4 years
Vesting period	1.6 years	1.5 years
Expected volatility	43%	46%
Expected dividends	Nil	Nil
Average fair value	$ 0.52	$ 0.58
Forfeiture rate	10.2%	11.4%

(Expressed in Canadian dollars)

10. Share capital (continued):

(b) *Share-based payment plans (continued):*

(i) Stock option plan (continued):

The Company charged the following share-based payments to expenses in connection with the Company's stock option plan, with a corresponding increase in contributed surplus:

	2018	2017
Total compensation - stock options	$ 264,627	$ 364,649

(ii) Restricted share unit plan:

Under the Company's RSU plan, the maximum number of shares that may be reserved for issuance is fixed at 2,100,000. As at September 30, 2018, 589,447 RSUs remain available to be granted. The obligations under the RSU plan can be settled at the Company's discretion through either cash or issuance of common shares. The Company intends to settle the obligation through the issuance of common shares.

RSUs outstanding as at September 30, 2018:

	Number of RSUs
Balance as at October 1, 2016	451,030
Granted	499,200
Vested	(420,670)
Balance as at September 30, 2017	529,560
Forfeited	(22,060)
Granted	238,782
Vested	(375,676)
Balance as at September 30, 2018	370,606

During the year ended September 30, 2017 the Company granted 499,200 RSUs. The weighted average fair value was $1.48 per share. 25% of these RSUs vested on September 1, 2017, 35% vested on September 1, 2018, and the remaining 40% will vest on September 1, 2019.

During the year ended September 30, 2018 the Company granted 238,782 RSUs. The weighted average fair value was $1.40 per share. 25% of these RSUs vested on September 1, 2018, 35% will vest on September 1, 2019, and the remaining 40% will vest on September 1, 2020.

(Expressed in Canadian dollars)

10. Share capital (continued):

(b) *Share-based payment plans (continued):*

(ii) Restricted share unit plan (continued):

Using an estimated forfeiture rate of 10.0% for the years ended September 30, 2018 and 2017, the Company charged the following share-based payments to operating expenses in connection with the Company's RSU plan, with a corresponding increase in contributed surplus:

	2018	2017
Total compensation - RSUs	$ 417,112	$ 556,549

11. Capital risk management:

The Company's objectives and policies for managing capital are to maintain a strong capital base to maintain investor, creditor and market confidence, to sustain future development of the business and to safeguard the Company's ability to support the Company's normal operating requirements on an ongoing basis.

The capital of the Company consists of the items included in the Consolidated Statements of Financial Position in the shareholders' equity section. The Company manages its capital structure and makes changes based on economic conditions, risks that impact the consolidated operations and future significant capital investment opportunities. To manage the Company's capital requirements, the Company has in place a planning and budgeting process which helps determine the funds required to ensure the Company has the appropriate liquidity to meet its operating and growth objectives. The Company's officers are responsible for managing the Company's capital and do so through quarterly meetings and regular review of financial information. The Board of Directors is responsible for overseeing this process.

12. Financial instruments and risk exposures:

(a) *Fair value measurement:*

The Company's financial assets include cash and cash equivalents, short-term investments, and accounts receivable. The Company's financial liabilities include accounts payable and accrued liabilities.

Cash and cash equivalents, short-term investments, and accounts receivable are classified as loans and receivables, measured at amortized cost using the effective interest rate method. Accounts payable and accrued liabilities are classified as other financial liabilities, measured at amortized cost using the effective interest rate method. The effective interest rate is the rate that exactly discounts the estimated future cash payments or receipts through the expected life of the financial instrument or a shorter period, where appropriate, to the net carrying amount of the financial asset or liability.

The carrying value of the Company's financial assets and liabilities is considered to be a reasonable approximation of fair value due to their immediate or short-term maturity, or their ability for liquidation at comparable amounts.

(b) *Credit risk:*

Credit risk is the risk of a financial loss if a customer or counterparty to a financial instrument fails to meet its obligations under a contract. This risk primarily arises from the Company's receivables from customers.

(Expressed in Canadian dollars)

12. Financial instruments and risk exposures (continued):

(b) *Credit risk (continued):*

The Company's exposure to credit risk is dependent upon the characteristics of each customer. Each customer is assessed for credit worthiness, using third party credit scores and through direct monitoring of their financial well-being on a continual basis. In some cases, where customers fail to meet the Company's credit worthiness benchmark, the Company may choose to transact with the customer on a prepayment basis or to seek other means of guarantees.

The Company does not have credit insurance or other financial instruments to mitigate its credit risk as management has determined that the exposure is minimal due to the composition of its customer base.

The Company regularly reviews the collectability of its accounts receivable and establishes an allowance account for credit losses based on its best estimate of any potentially uncollectable accounts. As at September 30, 2018, the balance of the allowance account for credit losses was $nil (2017 - $nil).

Pursuant to their respective terms, accounts receivable was aged as at September 30, 2018 and 2017:

	2018	2017
0 – 30 days	$ 1,127,001	$ 754,381
31 – 60 days	553,536	397,102
61 – 90 days	-	-
Greater than 90 days	282,432	222,959
Total accounts receivable	$ 1,962,969	$ 1,374,442

There is a possibility of increased customer credit risk due to the ongoing global recessionary trends. As at September 30, 2018, the Company's accounts receivable are made up of approximately 46% (2017 - 70%) government trade receivables and the balance of the outstanding accounts receivable are spread over several other customers.

During the year ended September 30, 2018, the Company had one customer who represented greater than 10% of total revenues. This customer represents approximately 79% of total revenues (2017 - two customers represented approximately 75% and 21%).

The Company may also have credit risk relating to cash and cash equivalents and short-term investments, which it manages by dealing with large banks and investing in highly liquid investments. The Company's objective is to minimize its exposure to credit risk in order to prevent losses on financial assets by placing its investments in highly liquid instruments such as guaranteed investment funds. The Company's cash and cash equivalents carrying value as at September 30, 2018 totaled $2,014,764 (2017 - $10,883,919), short-term investments of $7,598,857 (2017 - $nil) and accounts receivables of $1,962,969 (2017 - $1,374,442), representing the maximum exposure to credit risk of these financial assets.

(c) *Liquidity risk:*

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they fall due.

The Company has in place a planning and budgeting process which helps determine the funds required to ensure the Company has the appropriate liquidity to meet its operating and growth objectives.

(Expressed in Canadian dollars)

12. Financial instruments and risk exposures (continued):

(c) *Liquidity risk (continued):*

As at September 30, 2018, the Company had cash and cash equivalents of $2,014,764 (2017 - $10,883,919), short-term investments of $7,598,857 (2017 - $nil), and accounts receivable of $1,962,969 (2017 - $1,374,442) for a total of $11,576,590 (2017 - $12,258,361). The liquidity and additional financing are adequate for the settlement of short-term financial obligations.

(d) *Currency risk:*

Currency risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate due to changes in foreign exchange rates.

The Company is exposed to currency risk as a result of components of cost being denominated in currencies other than the Canadian dollar, primarily the United States dollar. The Company holds cash and has liabilities (primarily accounts payable and accrued liabilities) in currencies other than the Canadian dollar, primarily the United States dollar. In addition, the Company also has United States dollar denominated accounts receivable that are subject to currency risk.

The Company manages currency risk by holding cash in foreign currencies to support forecasted foreign currency denominated liabilities and does not use derivative instruments to reduce its exposure to foreign currency risk.

(e) *Interest rate risk:*

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company's exposure to the risk of changes in market interest rates relates primarily to cash equivalents and short-term investments. The Company does not enter into any interest rate swaps to mitigate interest rate risk.

13. Income taxes:

(a) *Income tax expense:*

Income tax expense differs from the expected expense if the Canadian federal and provincial statutory income tax rates were applied to earnings from continuing operations before income taxes. The principal factors causing these differences are shown below:

	2018	2017
Income (loss) from continuing operations before income taxes	$ 77,056	$ (3,853,853)
Statutory tax rate	26.73%	26.53%
Expected tax expense (recovery)	20,597	(1,022,427)
Effective tax rate change and other	(381,819)	(30,450)
Permanent differences	171,849	260,525
Non-refundable investment tax credits	(139,148)	-
Changes in deferred tax assets arising from discontinued operations	(469,263)	-
Changes recognized in equity	-	(224,463)
Change in unrecognized deferred tax assets	797,784	1,016,815
Income tax recovery	$ -	$ -

(Expressed in Canadian dollars)

13. Income taxes (continued):

(b) *Recognized deferred tax assets and liabilities:*

The Company has recognized deferred taxes in respect of the following:

	2018	2017
Deferred tax assets:		
Non-capital losses carried forward	$ 2,790,683	$ 2,890,617
Deferred tax liabilities:		
Property, plant, and equipment and intangible assets	(2,790,683)	(2,890,617)
Net deferred tax asset	$ -	$ -

(c) *Deferred income tax assets and liabilities:*

The Company did not recognize deferred tax assets for the following deductible temporary differences:

	2018	2017
Non-capital loss carry forwards	$ 8,520,026	$ 8,789,958
Net capital loss carry forwards	5,732,539	2,385,221
Non-refundable investment tax credits	668,251	-
Other temporary differences	7,345,635	8,223,233
Unrecognized deferred income tax assets	$ 22,266,451	$ 19,398,412

(d) *Loss carry forwards:*

As at September 30, 2018, the Company has tax loss carry forwards of approximately $18,948,528 (2017 - $19,583,000). The Company's tax loss carry forwards will expire, if not utilized, commencing in 2029. The Company recognizes the benefit of tax losses only to the extent of anticipated future taxable income. As at September 30, 2018, the Company has capital losses of approximately $5,732,539 (2017 - $2,385,221) that may be carried forward indefinitely to apply against future years' capital gains.

(e) *R&D and tax credit attributes:*

As at September 30, 2018, the Company had unclaimed tax deductions of scientific research and experimental development expenditures of $2,322,000 (2017 - $1,908,000) that is available to reduce taxable income in future years and may be carried forward indefinitely. As at September 30, 2018, the Company has federal investment tax credits of $555,000 (2017 - $418,000) and provincial investment tax credits of $114,000 that may be carried forward to apply against future years' income tax payable. These investment tax credits begin to expire in 2031 and 2022 respectively.

(Expressed in Canadian dollars)

14. Related party transactions:

(a) *The remuneration of key management personnel:*

	2018	2017
Salaries, accrued bonuses, and employee benefits	$ 1,208,306	$ 1,233,741
Share-based payments	493,881	699,138
	$ 1,702,187	$ 1,932,879

(b) As of September 30, 2018, amounts owing to a company controlled by an officer and director of the Company included in accounts payable and accrued liabilities were $191,433 (2017 - $262,854) in the ordinary course of his employment arrangement.

(c) Legal and professional fees, taxes and disbursements totaling $81,776 for the year ended September 30, 2018 (2017 - $160,664) were incurred with a law firm of which a director of the Company is a partner. As of September 30, 2018, amounts owing to this company included in accounts payable and accrued liabilities were $50,780 (2017 - $93,219).

The above transactions are in the normal course of business and are measured at the exchange amount which is the amount of consideration established and agreed to by the related parties.

15. Supplementary cash flow information:

(a) *Change in non-cash working capital:*

	2018	2017
Accounts receivable	$ (588,527)	$ (904,902)
Inventory	(21,928)	150
Prepaid expenses and other assets	62,360	(85,143)
Accounts payable and accrued liabilities (note 15(d))	(184,114)	112,304
Deferred revenue	(157,171)	157,171
	$ (889,380)	$ (720,420)

(b) *Interest and income taxes:*

	2018	2017
Interest received	$ 98,892	$ 42,475
Interest paid	2,905	461,980

The Company did not pay any income taxes during the years ended September 30, 2018 and 2017.

(c) *Cash and cash equivalents:*

Cash and cash equivalents consist of cash balances with banks, investments with original maturities of three months or less, and investments that are both readily convertible to cash and subject to insignificant changes in market value:

	2018	2017
Cash	$ 292,688	$ 914,378
Cash equivalents	1,722,076	9,969,541
	$ 2,014,764	$ 10,883,919

(Expressed in Canadian dollars)

15. Supplementary cash flow information (continued):

(d) *Supplemental disclosure of non-cash financing activities:*

As at September 30, 2018, property, plant and equipment included in accounts payable was $17,930 (2017 - $nil).

16. Segmented information

The Company's continuing operations currently consist of one operating segment. For the year ended September 30, 2018, sales within Canada were $1,113,177 (2017 - $328,531) and sales outside Canada were $8,086,533 (2017 - $7,015,260).

17. Nature of expenses:

The expenses presented below represent total cost of sales, sales and marketing, research and development, general and administration expenses, and depreciation and amortization.

	2018	2017
Salaries and benefits	$ 3,480,731	$ 3,452,013
Share-based compensation	681,739	921,198
Depreciation and amortization	1,613,491	2,916,283
Travel and entertainment	332,586	282,233
Professional fees and insurance	858,417	613,837
Public company costs	573,305	668,058
Rent and utilities	645,560	520,957
Maintenance and office expenses	234,917	278,353
Materials consumed	1,073,809	360,118
	$ 9,494,555	$ 10,013,050

18. Commitments:

(a) As at September 30, 2018, the Company is committed under operating leases, primarily related to office space, and other purchases for the following amounts:

2019	$ 335,549
2020	217,966
2021	96,196
2022	90,277
2023	64,736
	$ 804,724

(b) Certain nano-optic products are subject to a 3% sales royalty in favor of Simon Fraser University where certain elements of the nano-optic technology originated. No royalties were paid during the years ended September 30, 2018 and 2017.

(Expressed in Canadian dollars)

19. Discontinued operations:

On September 21, 2017, the Directors of the Company made the determination that it would pursue the possible sale of the assets of its subsidiary, Tactical, to a third party. At September 30, 2017, Tactical was classified as a separate disposal group held for sale and as a discontinued operation.

On June 29, 2018, the assets used in connection with Tactical's surveillance equipment and van conversion business were sold to an employee of Tactical for a nominal amount and on September 28, 2018, Tactical was wound-up and struck from the corporate register.

The major classes of assets and liabilities of Tactical classified as held for sale as at September 30, 2018 are as follows:

(a) Assets and liabilities of Tactical classified as held for sale:

	2018	2017
Cash	$ -	$ 30,280
Accounts receivable	-	116,538
Inventory	-	54,525
Prepaid expenses	-	12,401
Property, plant and equipment	-	2,481
Assets held for sale	$ -	$ 216,225
Accounts payable and accrued liabilities	$ 16,204	$ 200,226
Liabilities directly associated with assets held for sale	$ 16,204	$ 200,226
Cumulative loss in accumulated other comprehensive loss	$ -	$ (68,905)

(b) Net cash flows provided by (used in) discontinued operations:

	2018	2017
Net loss from discontinued operations	$ (123,322)	$ (900,279)
Depreciation	-	12,804
Foreign exchange reclassified upon disposal of foreign operation	167,813	-
Non-cash working capital changes	32,203	313,162
	$ 76,694	$ (574,313)

(Expressed in Canadian dollars)

19. Discontinued operations (continued):

(c) Net loss on discontinued operations, net of income taxes, is as follows:

	2018	2017
Revenue	$ 827,256	$ 1,259,066
Cost of sales	454,573	874,133
Gross Profit	372,683	384,933
Expenses		
Research and development	-	269,310
General and administration	311,217	542,227
Sales and marketing	14,994	246,630
Depreciation	-	12,804
	326,211	1,070,971
Income (loss) before other expenses	46,472	(686,038)
Other expenses	3,419	3,465
Gain on disposal of foreign operation (note 19(d))	(1,438)	-
Loss on remeasurement to fair value less costs to dispose	-	210,776
Foreign exchange reclassified on disposal of foreign operation	167,813	-
	169,794	214,241
Net loss from discontinued operations	$ (123,322)	$ (900,279)
Other comprehensive income (loss):		
Unrealized foreign exchange gain (loss) on translation of foreign operation	(98,908)	85,605
Net comprehensive loss from discontinued operations	$ (222,230)	$ (814,674)

(d) The effect of the disposal of Tactical on the financial position of the Company on June 28, 2018 is as follows:

Cash proceeds	$ 1
Cash	(66,385)
Accounts receivable	(22,933)
Inventory	(51,749)
Prepaid expenses	(894)
Accounts payable and accrued liabilities	143,400
Net assets disposed	1,439
Gain on disposal of foreign operations	$ (1,438)