



ENABLENCE TECHNOLOGIES INC.

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL  
CONDITION AND RESULTS OF OPERATIONS ("MD&A")

FOR THE THREE AND SIX MONTHS ENDED DECEMBER 31, 2018

DATED: February 28, 2019

## **MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS**

The following is a discussion and analysis of the financial condition of Enableness Technologies Inc. ("Enableness" or the "Company") at December 31, 2018 compared to June 30, 2018 and results of operations for the three and six months ended December 31, 2018 compared to the three and six months ended December 31, 2017.

This MD&A should be read in conjunction with our unaudited condensed consolidated financial statements and accompanying notes for the three months ended September 30, 2018 as well as our audited consolidated financial statements and accompanying notes for the year ended June 30, 2018. References made herein to "Enableness", the "Company", "we" and "our" mean Enableness, its subsidiaries, collectively, unless the context indicates otherwise. All amounts (including numbers of common shares, options and warrants) included in the MD&A are in thousands, except per share amounts or as otherwise indicated. All financial amounts are in US\$, unless stated otherwise. Other continuous disclosure filings for the Company are available on [www.sedar.com](http://www.sedar.com)

While the financial statements have been prepared on the basis of accounting principles applicable to a going concern, several conditions indicate the existence of material uncertainties that cast significant doubt about the Company's ability to continue as a going concern. The Company's continued existence is dependent upon its ability to secure additional financing and to attain profitable operations. Management is active in addressing these issues although there is no assurance that they will be successful. If the going concern assumption were not appropriate for these financial statements, adjustments might be necessary in the carrying values of assets and liabilities and the balance sheet classifications. The current situation and the plans to resolve it are contained in the Outlook section of this MD&A.

The effective date of this MD&A is February 28, 2019.

### **FORWARD-LOOKING STATEMENTS**

This MD&A includes certain forward-looking statements that are based upon current expectations, which involve risks and uncertainties associated with our business and the environment in which the business operates. Any statements contained herein that are not statements of historical facts may be deemed to be forward-looking statements, including those identified by the expressions "anticipate", "believe", "plan", "estimate", "expect", "intend" and similar expressions to the extent they relate to the Company or its management. The forward-looking statements are not historical facts, but reflect management's current expectations regarding future results or events. These forward-looking statements are subject to a number of risks and uncertainties that could cause actual results or events to differ materially from current expectations. The Company does not undertake or accept any obligation to release publicly any updates or revisions to any forward-looking statements to reflect any change in the Company's expectations, except as prescribed by applicable securities laws.

Key assumptions made in preparing the forward-looking statements contained in this MD&A include, but are not limited to, the following:

- The Company will be able to raise sufficient financing to meet its financial obligations as they come due, and will be able to renegotiate the current liability with EDC as well as certain financial obligations as they come due.
- The Company will continue to successfully reduce product costs to improve the Company's gross margin and/or avoid any margin erosion associated with competitive pricing pressure.
- Enableness will develop and deliver new products on time in order to satisfy the requirements of current and future customers and contribute to near-term profitability.

- Enablence will be able to attract and retain key people
- To raise financing to allow the Company fully implement its business plan

## **SUBSEQUENT EVENTS**

Subsequent to December 31, 2018, the Company received \$1,069 in unsecured short term bridge loans with interest accruing at a rate of 10% of which \$285 was provided by a related party.

On October 3, 2018, the Company received a default notice from EDC as a result of scheduled principal and interest payments having not been made. The notice requires Enablence to make payment of the amount in arrears of \$549 (\$719 CAD) plus a per diem default fee until full payment of this amount has been made. On October 26, 2018, as a result of the default, EDC provided Enablence with a demand for repayment on the total value of the loan, inclusive of interest, of \$3,997. At the same time, EDC provided the Company with a forbearance on the loan, providing the Company three months to rectify the default subject to meeting certain ongoing terms and conditions (see 9(b)). The Company is still in discussions with EDC regarding the loan and an additional extension.

On February 28, 2019, the CEO of the Company was granted stock options to purchase 8 million common shares of the Company at an exercise price of \$0.05 CDN and an expiry date of February 28, 2029. The options vest in 4 equal annual installments, on subsequent anniversary dates of the grant, commencing with the first 25% vesting on February 28, 2020.

## **OVERVIEW**

### ***ENABLENCE'S BUSINESS***

Enablence designs, manufactures, and sells optical components and subsystems for all three segments of optical networks - access, metro, and long-haul markets - to a global customer base. It utilizes its patented technologies, including planar lightwave circuit ("PLC") intellectual property, know-how and trade secrets in the production of an array of photonic components. The Company's product lines address access - connecting homes and businesses to the network; metro - communication rings within cities of different sizes; and long-haul - linking cities, countries and continents. The Company offers leading expertise in transmission, switching & routing, wavelengths management, and signal performance management for networks ranging from 1.25 to 100 gigabits per second. The Company's current product line includes multiple wavelength channel transmission and receiving optical subassembly (TOSA/ROSA), and wavelength management products.

Enablence's PLC optical chip technology enables the integration of sub-components (such as waveguides, photodetectors, lasers, and trans-impedance amplifiers) onto one silicon-based platform, which forms a hybrid photonic integrated circuit ("PIC") chip. The Company's core technology is portable to many markets that require filtering technology to separate and multiplex various optical signals. The chip-based integration capabilities of the Enablence platform technology makes it a solution for an array of applications including telecommunications, cloud data centers, sensor systems, biomedical and aerospace applications.

## **RESULTS OF OPERATIONS**

### **Summary of Unaudited Quarterly Results**

The following table sets forth unaudited summary results of operations for the past eight quarters. The information for the fiscal period ended March 31, 2017 and subsequent quarters has been

taken from our unaudited consolidated financial statements that, in management's opinion, have been prepared on a basis consistent with the unaudited consolidated financial statements for the three months ended December 31, 2018.

All normal recurring adjustments necessary for a fair presentation of information presented, have been included in the amounts stated below to present fairly the unaudited quarterly results when read in conjunction with the above-noted consolidated financial statements.

	<u>31-Mar</u> <u>2017</u>	<u>30-Jun</u> <u>2017</u>	<u>30-Sep</u> <u>2017</u>	<u>31-Dec</u> <u>2017</u>	<u>31-Mar</u> <u>2018</u>	<u>30-Jun</u> <u>2018</u>	<u>30-Sep</u> <u>2018</u>	<u>31-Dec</u> <u>2018</u>
Revenue	\$ 738	\$ 1,236	\$ 1,926	\$ 1,230	\$ 174	\$ 58	\$ 148	\$ 90
Gross Margin	(246)	(171)	106	(649)	(460)	(1,155)	(557)	(656)
GM %	(33.3%)	(13.8%)	5.5%	(52.8%)	(264.4%)	(1991.4%)	(376.4%)	(728.9%)
Expenses								
Research & development	1,027	1,414	1,435	927	739	695	697	678
Sales & marketing	69	79	47	60	76	71	70	73
General & administration	532	712	567	588	513	554	479	441
Stock-based compensation	81	53	33	33	13	3	4	3
Expenses	1,709	2,258	2,082	1,608	1,341	1,323	1,250	1,195
Operating loss	(1,955)	(2,429)	(1,976)	(2,257)	(1,801)	(2,478)	(1,807)	(1,851)
Finance and other expense	(217)	(44)	(358)	(412)	(407)	(551)	(448)	(484)
Gain on sale of property, plant and equip.	-	-	-	-	-	62	-	-
Foreign exchange (loss) gain	(11)	19	5	(37)	(57)	(110)	94	(297)
Net loss	(2,183)	(2,454)	(2,329)	(2,706)	(2,265)	(3,077)	(2,161)	(2,632)
Weighted average shares outstanding	560,541	589,403	621,929	621,929	621,928	621,928	635,624	635,624
Basic and diluted income (loss) per share	\$0.00	(\$0.01)	(\$0.00)	(\$0.00)	(\$0.00)	(\$0.00)	(\$0.00)	(\$0.00)
Adjusted EBITDA <sup>(1)</sup>	(1,685)	(2,163)	(1,747)	(2,028)	(1,576)	(2,354)	(1,708)	(1,761)

(1) Adjusted EBITDA does not have a standardized meaning according to IFRS and is defined and reconciled to net income (loss) below.

## NON-GAAP FINANCIAL MEASURES

Management reports and analyzes its financial results and performance using a range of financial measures. Some of these measures, such as revenues, net income and cash flow from operating activities, are defined by IFRS. Other measures are not defined by IFRS.

One key non-IFRS measure used by management is "Adjusted EBITDA". The Company discloses Adjusted EBITDA as a supplemental non-GAAP financial performance measure because the Company believes it is a useful metric by which to compare the performance of our business from period to period. The Company understands that measures similar to Adjusted EBITDA are broadly used by analysts, rating agencies and investors in assessing our performance. Accordingly, we believe that the presentation of Adjusted EBITDA provides useful information to investors.

Adjusted EBITDA comprises: net income (loss) excluding the following: finance income and expense, income tax recovery and expense, depreciation, amortization, losses on write-off or sale of equipment, foreign exchange gains and losses in earnings, and stock-based compensation expense. Therefore, it may not be comparable to similar measurements presented by other companies. The reconciliation of Adjusted EBITDA with the IFRS measure of net income (loss) is as follows:

	<b>31-Mar 2017</b>	<b>30-Jun 2017</b>	<b>30-Sep 2017</b>	<b>31-Dec 2017</b>	<b>31-Mar 2018</b>	<b>30-Jun 2018</b>	<b>30-Sep 2018</b>	<b>31-Dec 2018</b>
Net loss for the period	(2,183)	(2,454)	(2,329)	(2,706)	(2,265)	(3,077)	(2,161)	(2,632)
Add (deduct):								
Net interest and other expense	217	44	358	412	407	551	448	484
Amortization	189	213	196	196	212	121	95	87
Gain on sale of equipment	-	-	-	-	-	(62)	-	-
Foreign exchange (gain) loss	11	(19)	(5)	37	57	110	(94)	297
Stock-based compensation expense	81	53	33	33	13	3	4	3
<b>"Adjusted EBITDA"</b>	<b>(1,685)</b>	<b>(2,163)</b>	<b>(1,747)</b>	<b>(2,028)</b>	<b>(1,576)</b>	<b>(2,354)</b>	<b>(1,708)</b>	<b>(1,761)</b>

## SUMMARY OF RESULTS FOR THE THREE AND SIX MONTHS ENDED DECEMBER 31, 2018 COMPARED TO THE THREE AND SIX MONTHS ENDED DECEMBER 31, 2017

The following table sets forth a summary of key earnings information from our consolidated financial statements for the three and six months ended December 31, 2018 and 2017.

	<b>Three months ended</b>			<b>Six months ended</b>			
	<b>December 31, 2018</b>	<b>2017</b>	<b>Increase (decrease)</b>	<b>December 31, 2018</b>	<b>2017</b>	<b>Increase (decrease)</b>	
Revenues	\$ 90	\$ 1,230	\$ (1,140)	\$ 238	\$ 3,156	\$ (2,918)	(92%)
Cost of revenues	746	1,879	(1,133)	1,451	3,699	(2,248)	(61%)
Gross margin	<b>(656)</b>	<b>(649)</b>	<b>(7)</b>	<b>(1,213)</b>	<b>(543)</b>	<b>(670)</b>	55%
	<i>(729%)</i>	<i>(53%)</i>		<i>(510%)</i>	<i>(17%)</i>		
Operating expenses:							
Research and development	678	927	(249)	1,375	2,362	(987)	(42%)
Sales and marketing	73	60	13	143	107	36	34%
General and administrative	441	588	(147)	920	1,155	(235)	(20%)
Stock based compensation	3	33	(30)	7	66	(59)	(89%)
Total operating expenses	<b>1,195</b>	<b>1,608</b>	<b>(413)</b>	<b>2,445</b>	<b>3,690</b>	<b>(1,245)</b>	(34%)
Loss from operations	<b>(1,851)</b>	<b>(2,257)</b>	<b>406</b>	<b>(3,658)</b>	<b>(4,233)</b>	<b>575</b>	(14%)
Other income (expenses):							
Finance and other income (expense)	(50)	(54)	4	(50)	(55)	5	
Finance expense	(434)	(358)	(76)	(882)	(715)	(167)	19%
Foreign exchange gain(loss)	(297)	(37)	(260)	(203)	(32)	(171)	
Net loss	<b>(2,632)</b>	<b>(2,706)</b>	<b>74</b>	<b>(4,793)</b>	<b>(5,035)</b>	<b>242</b>	(5%)
Other comprehensive income (net of tax):							
Foreign currency translation gain(loss)	954	(43)	997	637	212	425	67%
Comprehensive loss	\$ <b>(1,678)</b>	\$ <b>(2,749)</b>	\$ <b>1,071</b>	\$ <b>(4,156)</b>	\$ <b>(4,823)</b>	\$ <b>667</b>	(16%)

Enableness converts foreign currency-denominated transactions related to the statement of comprehensive loss at the average exchange rates for the periods. As such, changes in the exchange rate between the United States dollar and the Canadian dollar can have an impact on the reported results for each fiscal period as well as changes in the exchange rate between the Chinese renminbi (RMB). The average exchange rate for the six months ended December 31, 2018 in terms of the Canadian dollar equivalent of US\$1 was CAD \$1.3142 (December 31, 2017 – CAD \$1.2715) and in terms of the Chinese RMB equivalent of US\$1 was RMB \$0.1458 (December 31, 2017 – RMB \$0.1506)

## REVENUE

Revenue for the three months ended December 31, 2018 was \$90 as compared to \$1,230 for the same period of the prior year and revenue for the six months ended December 31, 2018 was \$238 as compared to \$3,156 for the same period of the prior year. The reduced level of revenue compared to the prior year's periods is due to the U.S. trade restrictions placed on the Company's

major customer during the second half of calendar year 2018. These US trade restrictions were removed and the customer is now in the process of using up current inventory, prior to placing new orders of 10x10 TOSA ROSA product with Enablence. The Company is also in the process of qualifying new product with other key customers and expecting to ramp production of those later this calendar year.

The geographic split of revenue (based on ship-to location of the customer) is as follows:

	Three months ended		Six months ended	
	December 31, 2018	December 31, 2017	December 31, 2018	December 31, 2017
	\$	\$	\$	\$
Americas	86	193	144	203
Asia Pacific	4	1,034	94	2,514
Europe, Middle East, Africa	-	3	-	439
	<b>90</b>	<b>1,230</b>	<b>238</b>	<b>3,156</b>

### **GROSS MARGIN**

The Company's cost of revenues is comprised of a number of elements, some of which vary directly with the level of revenues, such as material costs and the cost of products manufactured by third parties, and some of which do not vary significantly with the level of revenues, including many overhead costs such as compensation of operations staff, amortization and facilities costs.

Gross margin for the three months ended December 31, 2018 was (\$656) as compared to (\$649) for the same period of the prior year. Gross margin for the six months ended December 31, 2018 was (\$1,213) as compared to (\$543) for the same period of the prior year.

This increase in the gross margin loss for the current year's period compared to the prior year's same period is primarily a result a large part of the fixed cost component of the fabrication facility being absorbed into cost of sales due to reduced sales and inventory production levels.

### **OPERATING EXPENSES**

**R&D** expense for the three months ended December 31, 2018 was \$678 as compared to \$927 for the same period of the prior year, a decrease of \$249. R&D expense for the six months ended December 31, 2018 was \$1,375 as compared to \$2,362 for the same period of the prior year, a decrease of \$987. The decrease is primarily due to the impact of Irix service agreement costs incurred in the prior year's period but not the current year's period, as well as lower R&D materials spending during the current year's period.

**Sales & Marketing** expense for the three months ended December 31, 2018 was \$73 as compared to \$60 for the same period of the prior year, and for the six months ended December 31, 2018 was \$143 compared to \$107 for the same period of the prior year.

**General & Administration** expense for the three months ended December 31, 2018 was \$441 as compared to \$588 for the same period of the prior year, and for the six months ended December 31, 2018 was \$920 compared to \$1,155 for the same period of the prior year.

The decrease primarily relates to lower professional fees and staff levels during the current year's periods.

**Stock-based compensation** expense for the six months ended December 31, 2018 was \$33 as compared to \$66 for the same period of the prior year. The decrease in the current year's expense

compared to the prior year mainly relates to option grants issued in prior years that have now been fully expensed.

## **FINANCE AND OTHER INCOME**

Enableness invests cash and cash equivalents in short-term investments with financial institutions. Interest income is a function of prevailing interest rates and the amount of funds invested.

## **FINANCE EXPENSE**

The Company's interest expense is a function of the balance of debt, and applicable interest rates, and the average foreign exchange rate between the underlying currency of the debt security and the U.S. dollar.

Interest and finance expense for the three months ended December 31, 2018 was \$434 as compared to \$358 for the same period of the prior year, an increase of \$76. Interest and finance expense for the six months ended December 31, 2018 was \$882 as compared to \$715 for the same period of the prior year, an increase of \$167. The increase primarily relates to a combination of the interest on the convertible debentures, notes payable as well as EDC loans as compared to the prior year's same period.

Notes payable were as follows at December 31, 2018:

	<b>December 31</b>	June 30,
	<b>2018</b>	2018
	<b>\$</b>	<b>\$</b>
Short-term Loans (a)	<b>6,672</b>	4,369
Loan from Export Development Canada (b)	<b>3,939</b>	3,804
	<b>10,611</b>	8,173
Less current portion	<b>10,611</b>	8,173
Long-term portion	-	-

- (a) During the fiscal year ended June 30, 2017, the Company obtained non-interest bearing, unsecured short-term loans in the amount of \$4,044 (\$5,231 CAD) from certain related and unrelated parties of which \$1,320 (\$1,755 CAD) of the loans were repaid during the year, \$385 was converted to equity, \$1,156 was exchanged for a convertible debenture, leaving an unpaid balance of \$1,194 (\$1,549 CAD) at June 30, 2017. The exchange of debt instruments represented a substantial modification to the terms of the existing financial liability. As a result it was accounted for as a modification. No gain or loss was recognized on the modification. On April 1, 2017, the terms of the loan were changed to start accruing interest at the rate of 10% per annum. The remaining balance of \$1,194 at June 30, 2017 was paid in July 2017 which included principal of \$1,138 and interest of \$56. During the year ended June 30, 2018, the Company obtained 10% interest bearing unsecured short term loans in the amount of \$1,497 of which \$558 was from a related party, and obtained non-interest bearing unsecured short term loans in the amount of \$2,700, of which a fee of \$125 is payable on the May 2018 maturity of \$1,250 of this loan. During the six months ended December 31, 2018 the Company obtained 10% interest bearing unsecured short term loans in the amounts of \$2,175 of which \$453 were from a related parties. As at December 31, 2018 a total amount of \$6,575 remains owing on these loans which includes \$170 of accrued interest and \$125 of accrued fees.
- (b) On March 3, 2016, the Company closed a secured term loan facility with Export Development Canada ("EDC") of \$3 million CAD. In August 2016, the loan facility was increased to \$5 million CAD. The loan facility is designed to finance up to 85% of the value of purchase orders from a

major telecommunications equipment provider, ZTE Corporation, a strategic investor in the Company. The loan facility is available in the form of a term loan for a period of 18 months from the date of the initial draw down which was in March 2016. Repayment of principal is to commence 18 months after the first draw on the loan. Principal then is to be repaid in 17 equal monthly instalments. Interest is payable monthly at the rate of prime plus 10% resulting in a rate of 13.95% at December 31, 2018 (June 30, 2018 -13.45%). The loan facility is secured against all of the assets of the Company and is guaranteed by the Company's subsidiaries. On October 30, 2017, the Company received a principal repayment extension from EDC resulting in the first monthly principal repayment being deferred to commence in March 2018. On March 9, 2018 the Company received an additional principal repayment extension from EDC resulting in the first monthly principal repayment being deferred to commence in August 2018. In accordance with IAS 39, *Financial Instruments: Recognition and Measurement*, the amendment was considered a modification of debt. At December 31, 2018 the principal amount drawn on the EDC term facility is \$4,005 inclusive of interest. On October 3, 2018, the Company received a default notice from EDC as a result of scheduled principal and interest payments having not been made. The notice requires Enablence to make payment of the amount in arrears of \$549 (\$719 CAD) plus a per diem default fee until full payment of this amount has been made. On October 26, 2018, as a result of the default, EDC provided Enablence with a demand for repayment on the total value of the loan, inclusive of interest to date at that time of \$3,997. At the same time, EDC provided the Company with a forbearance on the loan, providing the Company three months to rectify the default subject to meeting certain ongoing terms and conditions.

### **FOREIGN EXCHANGE GAIN (LOSS)**

Foreign exchange gains and losses include realized and unrealized gains and losses on foreign exchange, including those that arise as a result of converting assets and liabilities denominated in currencies other than the functional currency of the entity into the functional currency of the entity at the balance sheet date and realized gains or losses arising from the settlement of these balances during the period.

During the three and six months ended December 31, 2018 the Company recorded a foreign exchange loss of \$297 and \$203, respectively, as compared to a loss of \$37 and \$32 being recorded in the three and six months periods of the prior year.

### **INCOME TAXES**

There were no income taxes payable or recoverable during the current or prior year's six months ended December 31, 2018.

### **NET LOSS**

The net loss from operations for the three months ended December 31, 2018 was \$2,632 as compared to a net loss of \$2,706 for the same period of the prior year. The net loss from operations for the six months ended December 31, 2018 was \$4,793 as compared to a net loss of \$5,035 for the same period of the prior year.

### **FOREIGN CURRENCY TRANSLATION GAIN**

During the three and six months ended December 31, 2018 the Company recorded a foreign exchange translation gain of \$954 and a gain of \$637, respectively, as compared to a loss of \$43 and a gain of \$212, respectively, in the same periods of the prior year. This was as a result of conversion of the Company's operations that are being transacted in non-US\$ currencies (Canadian dollar and Chinese Renminbi), being converted to the Company's reporting currency, which is US\$.



## LOSS PER COMMON SHARE

The table below presents the basic and diluted loss per common share for each of the comparative fiscal periods.

	Three months ended December 31,		Six months ended December 31,	
	2018	2017	2018	2017
Basic and diluted loss per common share:				
From continuing operations	\$(0.00)	\$(0.00)	\$(0.01)	\$(0.01)
Weighted Average Number of Common Shares	635,624	621,929	638,667	621,929

Due to the net loss from operations, warrants and options, are anti-dilutive.

## OUTLOOK

The Company's financial position continues to remain challenged. The Company will need to raise additional financing to carry out its business plan. In the event the Company is unable to raise the additional financing, the Company will have to look at other alternatives including the possibility of ceasing operations. The Company also continues to be highly dependent on additional equity financing in the longer term, until revenues and gross margins increase to a point at which operations become profitable. There is no certainty that additional funding in the immediate or longer term will be secured (see Subsequent Events and Finance Expense sections regarding recent debt financing).

During early fiscal 2018, the Company continued the development of its core competency in PLC design and fabrication, with the main target markets being in the cloud data center interconnection as well the emerging 5G Wireless networks. The latter is in the early stages of deployment in major markets around the globe, including both the United States, Europe, and China, and are expected to be on the fast track of growth in 2020 and the following years. The Company has developed a series of compact optical multiplexers and demultiplexers to be used in multi-channel high-speed optical transceivers for these markets. After completing product qualifications with a number of US-based customers the Company plans to start commercial production and expect production volumes to increase over the next four quarters. The Company believes that the above-mentioned products represent a potential sizeable revenue growth opportunity for the Company, for at least the next 3 years.

Driven by the global trend in data center construction, we are seeing growing demand for PLC chips for use in datacenter interconnection application and 5G applications. We believe that our PLC platform and proprietary PIC technology enable cost-effective solutions to meet the rapid growth in datacenter transceiver demand. Our ability to develop low-cost data center solutions, as well as securing customer orders for data center applications is important as we seek to diversify our revenue stream and to achieve financial success in the datacenter marketplace.

The performance of our CWDM and LWDM multiplexer and demultiplexers products have been tested by a number of key customers and the feedback to date has been very positive. Most recently we have received a framework order for \$4 million dollars from one of these strategic customers, which is to be fulfilled over the next 12 months. We are anticipating additional orders from other key customers in the near future.

Our goal over the next 12 months is to fully utilize our fab with production orders, which we are expecting to come from PLC chip business as well as the CWDM and LWDM MUX and DEMUX products. We will focus on product qualification with the end customer and their contract manufacturers. Once our products are fully qualified, we believe customers will provide volume orders, and our goal is to increase production by the fourth calendar quarter of 2019.

Our challenges are on multiple fronts including system level qualification at the end customer, the process level qualification at the contract manufacturers, and scaling our internal production. We are confident that we can pass the customer trial qualifications.

The management team at Enablence is excited about the data center interconnection and 5G opportunities. Our customers are keen to use our products and we will strive to meet their needs. Our strategic goal over the next 4 quarters is to improve the utilization of our fab and attain quarterly profitability.

## LIQUIDITY

The Company's objectives when managing its liquidity and capital structure are to generate sufficient cash to fund the Company's operating, debt service and organic growth requirements. During the six months ended December 31, 2018 the Company obtained short term debt financing in the amount of \$2,175.

The authorized share capital of the Company consists of an unlimited number of common shares and an unlimited number of preferred shares, issuable in series. December 31, 2018, there are 641,927 common shares and no preferred shares outstanding.

The Company has sustained significant losses since its inception, and expects to continue to incur losses in its next few quarters. The Company's ability to reach profitability is dependent on successful introduction of new products, improved margins, revenue growth and additional financing. There can be no assurance that Enablence will gain adequate market acceptance for its new products or be able to generate sufficient gross margins to reach profitability.

Enablence has not generated positive cash flow from operations since its inception, and has relied on cash from the issuance of shares and debt to fund its operations. The table below sets out the cash and cash equivalents, and working capital at December 31, 2018 and June 30, 2018.

	<b>December 31, 2018</b>	<b>June 30, 2018</b>
Cash and Cash Equivalents	<b>\$142</b>	\$103
Restricted cash	<b>4</b>	4
	<b>146</b>	107
Working capital (deficiency)	<b>(18,115)</b>	(14,812)

The working capital deficiency from operations at December 31, 2018 was \$18,115 as compared to working capital deficiency of \$14,812 at June 30, 2018. This reduction in the working capital during the six months ended December 31, 2018 as compared to the prior year's same period was mainly due to the cash used in operations as well as the increase in debt financing outstanding at the end of the current year.

The chart below highlights the Company's cash flows during the six months ended December 31, 2018 and 2017.

	Three months ended December 31,		Six months ended December 31,	
	2018	2017	2018	2017
<b>Cash used in Operating activities</b>	<b>(1,595)</b>	(1,795)	<b>(3,148)</b>	(4,724)
<b>Investing activities</b>				
Purchase of property, plant and equipment	(29)	(119)	(94)	(237)
	<b>(29)</b>	(119)	<b>(94)</b>	(237)
<b>Financing activities</b>				
Advances from (repayments on) short term loa	1,404	1,203	2,278	209
Advances from long term loans	-	-	-	-
Net proceeds from issuance of shares	-	-	755	-
Proceeds from the exercise of warrants	-	-	-	-
	<b>1,404</b>	1,203	<b>3,033</b>	209
Effect of foreign currency translation	189	(212)	248	(212)
Net change in cash and cash equivalents	<b>(31)</b>	(923)	<b>39</b>	(4,964)

At December 31, 2018, the Company had cash available of \$142 (not including \$4 of restricted cash). The Company consumed \$3,148 in operating activities for the six months ended December 31, 2018 compared to \$4,724 for the same period of the prior year.

During the six months ended December 31, 2018 the Company obtained 10% interest bearing unsecured short term loans in the amounts of \$2,175 of which \$453 were from a related parties. As at December 31, 2018 a total amount of \$6,575 remains owing on these loans which includes \$170 of accrued interest and \$125 of accrued fees.

#### Convertible Debenture financing during prior fiscal year

On June 30, 2017 the Company issued a total of \$5,780 (\$7,500 CAD) of unsecured convertible debentures (the "Debentures") of which \$4,624 of the Debentures were issued through a private placement for cash, and \$1,156 were issued as a result of a debt settlement agreement with a related party creditor to settle outstanding short term loans received by the Company during the year ended June 30, 2017. The Debentures bear interest at a rate of 10% per annum, are payable quarterly commencing on September 30, 2017, and are convertible, at the option of their holder, into common shares of the Company (the "Shares") at a price of \$0.08 CAD per Share. The Debentures mature on June 30, 2020.

As the Debentures are convertible into common shares at the option of the holder, they have been accounted for into their component parts. Management determined the fair value of the Company's liability to make future payments of principal and interest to be \$4,694 and the fair value of the holders' conversion option to be \$1,086. The carrying value of the debentures is accreted to the principal amount over the term to conversion through a charge to interest expense. The carrying value of the equity component of \$1,086 is recorded to contributed surplus. The Company determined the carrying value of the liability by discounting the stream of future cash payments of interest and principal at an estimated market rate of 18% for a similar liability that does not have an associated conversion/equity component. The carrying value of the debentures will be accreted to the principal amount over the term to conversion through a charge to interest expense. Professional and financing costs of \$378 were incurred to complete the issuance of the Debentures. The portion of the financing fees that relate to the Debentures have been split between debt and equity in the same proportion as the Debentures were split between debt and

equity. The debt financing costs of \$307 is being amortized over the three year term of the debt. The equity financing costs of \$71 have been charged to contributed surplus.

During the six months ended December 31, 2018, the Company recorded accretion of \$453 to interest expense and \$47 of amortization of the debt financing costs. Of the \$825 interest earned since June 30, 2017, \$29 has been paid and the unpaid balance of \$796 is overdue and included in accrued interest. As at December 31, 2018, the total convertible debenture liability is \$5,590.

### Equity Financing

On July 30, 2018 the Company closed an equity financing at a price of \$0.05 CAD per share for gross proceeds in the amount of \$758 (\$1,000 CAD) resulting in the issuance of 20,000 common shares. There was no equity financing raised during the fiscal year ended June 30, 2018.

## **BOARD AND MANAGEMENT**

At the Annual and Special Meeting of Shareholders held on February 5, 2019, Derek H. Burney, Louis De Jong, Dan Shmitt, Evan Chen and Yongxing Zhu were elected directors of the Company. Additionally, Derek H. Burney was appointed Chairman of the Board of Directors.

Also on February 5, 2019, Steve Wang was appointed as Chief Executive Officer of the Company, replacing Evan Chen who had stepped down as CEO of the Company. In addition, the Company announced that Todd Zhang, Chief Financial Officer of the Company, had also stepped down. Gerald Leahy assumed the position of Interim CFO along with his current duties as Corporate Treasurer, a position Mr. Leahy has held at the Company since 2012.

## **CAPITAL RESOURCES**

Enableness finances its operations through the issuance of common shares and debt. The Company may also receive cash proceeds on the issue of additional common shares on the exercise of options and warrants depending in part on the market price for its shares.

The Company periodically evaluates the opportunity to raise additional funds through either the public or private placement of equity capital to strengthen its financial position and to provide sufficient cash reserves to protect itself from the effects of the volatile economic conditions that are difficult to predict.

See the Liquidity and Subsequent Events sections above for details on financings completed during the six months ended December 31, 2018 and for loans obtained subsequent to the year end. The continued debt and equity funding will help to position Enableness to address the increased demand it is experiencing in its 100G/s components business and to focus on its customer needs and future growth opportunities.

Enableness is authorized to issue an unlimited number of common shares and an unlimited number of preferred shares. There are 641,927 common shares issued and outstanding as of February 28, 2019 and no preferred shares issued and outstanding. The common shares of Enableness trade on the TSX Venture Exchange under the symbol "ENA" or "ENA.V".

## **OFF-BALANCE SHEET ARRANGEMENTS AND CONTRACTUAL OBLIGATIONS**

The table below presents the Company's contractual obligations from operations.

	To Dec 31, 2019	To Dec 31, 2020	To Dec 31, 2021+	Total
	\$	\$	\$	\$
Accounts payable and accrued liabilities	4,395	-	-	4,395
Notes payable	10,611	-	-	10,611
Convertible debentures	5,590	-	-	5,590
Total	20,596	-	-	20,596

The Company is required to comply with certain obligations with respect to the loan payable to Export Development Canada which is secured against the assets of the Company (see Finance Expense section above and the references to notes payable).

The Company is exposed to currency risk as certain transactions are denominated in Canadian dollars. Management is evaluating foreign exchange risk management strategies, however, the Company has not entered into forward, swap or option contracts to manage its exposures to fluctuations in foreign exchange rates.

Enablence has not entered into any other material off-balance sheet arrangements such as guarantee contracts, contingent interests in assets transferred to unconsolidated entities, or derivative instrument obligations, or with respect to any obligations under a variable interest entity arrangement.

## TRANSACTIONS WITH RELATED PARTIES

On February 2, 2016, the Company closed a private placement with ZTE Corporation ("Strategic Investor") for 77,000 shares at a price of \$0.06 CAD per common share for proceeds of \$3,280 (\$4,620 CAD). The Strategic Investor holds approximately 14.8% (June 30, 2018 – 15.3%) of the issued and outstanding shares of the Company. As part of the financing, (i) the Strategic Investor entered into a voting agreement with certain shareholders of the Company to vote in favour of one nominee of the Strategic Investor to the Board of Directors of the Company, (ii) the Strategic Investor will have a right of participation to maintain its percentage of shareholdings in the Company in future issuances of securities by the Company, and (iii) the Company has put in place a Product Roadmap Development Committee which will make recommendations to the Board of Directors on future product development (iv) an updated version of the Business Cooperation Agreement from December 2014 was signed by the Company and the Strategic Investor.

During the six months ended December 31, 2018, the Company had sales of \$Nil to ZTE (September 30, 2017 - \$2,487). At December 31, 2018, the Company had an accounts receivable balance with ZTE of \$366 (June 30, 2018 - \$1,066) which is included in accounts and other receivables.

As at December 31, 2018, China TriComm Ltd. ("TriComm") owned 30,000 Enablence common shares of the Company. TriComm is controlled by Zhiyin Gao, a former director of the Company who resigned in September 2017.

As at December 31, 2018, Irix Holding Ltd. ("Irix"), owned 39,408 common shares of the Company. Irix is a joint venture controlled by China TriComm Ltd. (a company controlled by a former director of the Company) and Win Brand (a company whereby the CEO and CFO of the Company have ownership interests). Suzhou Irix Ltd. ("Suzhou Irix") is a company controlled by Irix. The following transactions took place between Irix, Suzhou Irix and the Company during the six months ended December 31, 2018 and the year ended June 30, 2018:

- During the three months ended December 31, 2018, Suzhou Irix provided short-term financing of \$97 to Enablence Suzhou.

- During the six months ended December 31, 2018, Suzhou Irix provided employee related services and utilities to the Company of \$61 (FY2018 – \$85). At December 31, 2018 \$109 (2018 - \$66) remains outstanding within accounts payable and accrued liabilities relating to these services.
- During the fiscal year ended June 30, 2018, Irix paid \$463 to a contract manufacturer for the delivery of finished goods to a customer of which \$463 is owing to Irix at December 31, 2018.
- At December 31, 2018 an amount of \$612 (2018 – \$552) is included in accounts payable and accrued liabilities relating to consulting services provided by Irix. Of this amount, \$60 (2018 - \$60) was incurred and recorded to consulting fee expense during the six months ended December 31, 2018, relating to services provided through Irix by Todd Zhang, the CFO of the Company. At December 31, 2018 \$392 (June 30, 2018 - \$332) remains outstanding within accounts payable and accrued liabilities relating to these consulting services.
- During the fiscal year ended June 30, 2017 USA Irix provided other consulting services and materials to Enable. As a result, at December 31, 2018 the Company has an amount of \$17k owing to USA Irix (June 30, 2018 - \$17).

In January 2016 the Company entered into a one year R&D Services Agreement (the “Service Agreement”) with Suzhou Irix Ltd. and Irix Photonics Inc. (“Irix Photonics”). Irix Photonics was created to carry out the operations of Irix and is a company controlled by the Chief Executive Officer (“CEO”) and Chief Financial Officer (“CFO”) of Enable. Pursuant to the Service Agreement, for R&D services provided by Irix Photonics for the development of a new product and assistance in ramping up its volume production, Enable is contracted to pay Irix Photonics \$150/month (“Service Fees”) over the 2016 calendar year. In addition, if certain agreed upon volume production milestones are met during the twelve month period, Irix Photonics may be eligible for the payment of a success fee (“Success Fee”). The Success Fee amounts to \$2 million less any Service Fees previously paid. The Company retains ownership of all Intellectual Property associated with the products under the agreement. Pursuant to this agreement, the Company paid Irix Photonics a total of \$1,800 of which \$900 was paid during fiscal year 2016 and \$900 was paid in fiscal year 2017. The Company signed a new services agreement with Irix Photonics for the 2017 calendar year at a monthly fee of \$130, as well as a base royalty on certain future products at 3% of net sales and additionally a potential 17.5% bonus royalty on gross margin on such products if certain targets are met. As of September 30, 2018, under the 2017 contract, the Company has paid Irix Photonics \$1,235 of monthly fees and has \$325 recorded as an accrued liability.

During the six months ended December 31, 2018, the Company received \$38 in the form of a short term bridge loan from a director of the Company.

Paradigm Capital Partners Limited (“PCPL”) is a shareholder of Enable and is a company controlled by close family members of a director of Enable. The following transactions took place with PCPL, its affiliates and individuals related to PCPL (collectively “Paradigm”), during the periods ended:

Six months ended December 31, 2018:

- The Company received \$415 in unsecured short term bridge loans from a controlling shareholder of Paradigm (also see Subsequent Events)

Year ended June 30, 2018:

- The Company received \$568 in unsecured short term bridge loans from a controlling shareholder of Paradigm accruing interest at a rate of 10% amounting to \$26.

Year ended June 30, 2017:

- A controlling shareholder of Paradigm provided short term loans to the Company of \$3,241 during the year and converted a portion of the loans to equity, exchanged a portion into convertible debentures and then was repaid the remaining balance of \$1,194 during July 2017
- Paradigm earned \$474 of commissions relating to the equity and debenture financing the Company closed during May and June 2017.

These transactions are in the normal course of operations and are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties. During the six months ended December 31, 2018 the Company did not enter into any material transactions with related parties outside of those noted elsewhere in the MD&A.

## **RISKS AND UNCERTAINTIES**

The Company operates in a dynamic, rapidly changing environment that involves risks and uncertainties, and as a result, management expectations may not be realized for a number of reasons. An investment in Enableness common shares is speculative and involves a high degree of risk and uncertainty. The Company is highly dependent on additional financing to continue operations and there is no certainty that it will be able to obtain such financing.

Any investor should also consider carefully these risks and the risks and uncertainties that are detailed in our Annual MD&A filed October 29, 2018 and available at [www.sedar.com](http://www.sedar.com).

## **CRITICAL ACCOUNTING ESTIMATES**

The Company's consolidated financial statements are prepared in accordance with IFRS recognition and measurement principles that often require Management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts presented and disclosed in the consolidated financial statements. Management reviews these estimates and assumptions on an ongoing basis based on historical experience, changes in business conditions and other relevant factors as it believes to be reasonable under the circumstances. Changes in facts and circumstances may result in revised estimates, and actual results could differ from those estimates. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

### Estimates

#### *Useful lives of depreciable assets*

The useful lives of depreciable assets have been determined based on management's estimated utility of the assets. Uncertainties in these estimates relate to technological obsolescence and wear and damage of assets.

#### *Inventories*

Inventories are initially recognized at cost, and subsequently at the lower of cost and net realizable value. Management estimates the net realizable value of inventories, considering the most reliable evidence available at each reporting date. The future realization of these inventories

may be affected by future technology or other market driven changes that may reduce future selling prices. Management assesses inventory periodically and uses a provision to provide for estimated obsolescence and cost-price erosion.

#### *Stock-based compensation*

The estimation of stock-based compensation requires the selection of an appropriate valuation model and consideration as to the inputs necessary for the valuation model chosen. The Company has made estimates as to the volatility of its own share price, the forfeiture rate, the probable life of share options granted and the time of exercise of those share options. The model used by the Company is the Black-Scholes valuation model.

#### *Fair value measurement*

Management uses valuation techniques to determine the fair value of financial instruments. This involves developing estimates and assumptions consistent with how market participants would price the instrument. Management bases its assumptions on observable data as far as possible but this is not always available. In that case management uses the best information available. Estimated fair values may vary from the actual prices that would be achieved in an arm's length transaction at the reporting date.

#### Judgments

##### *Recognition of deferred income tax assets*

Management continually evaluates the likelihood that its deferred tax assets could be realized. This requires management to assess whether it is probable that sufficient taxable income will exist in the future to utilize these losses within the carry-forward period. By its nature, this assessment requires significant judgment.

##### *Going concern risk assessment*

The assessment of the Company's ability to continue as a going concern and raising additional debt or equity financing or attaining sufficient revenues to achieve and sustain profitability for the ensuing year, and to fund planned research and development activities, involves significant judgment based on historical experience and other factors including expectation of future events that are believed to be reasonable under the circumstances.

##### *Impairment*

Determining if there are any facts and circumstances indicating impairment loss or reversal of impairment losses is a subjective process involving judgment and a number of estimates and interpretations in many cases. In assessing impairment, management estimates the recoverable amount of each asset or cash-generating unit based on expected future cash flows and uses an interest rate to discount them. Estimation uncertainty relates to assumptions about future operating results and the determination of a suitable discount rate.

##### *Functional currency*

An area of judgment that has a significant effect on the amounts recognized in these consolidated financial statements is the determination of functional currency. The determination of the Company and its subsidiaries' functional currency often requires significant judgment where the primary economic environment in which they operate may not be clear. This can have a significant impact on the consolidated results of the Company based on the foreign currency translation methods used.

## **CHANGES IN ACCOUNTING POLICIES**

### *New or amended IFRS standards effective July 1, 2018*



The Company has adopted the following new or amended IFRS standards for the interim and annual period beginning on July 1, 2018:

#### IFRS 15 – Revenue from Contracts with Customers

In May 2014, the IASB released IFRS 15, Revenue from contracts with customers, which supersedes IAS 11, Construction Contracts, and IAS 18, Revenue as well as other related interpretations. The core principle of IFRS 15 is that an entity should recognize revenue to depict the transfer of promised goods or services to customers in an amount that reflects the consideration to which the entity expects to be entitled in exchange for those goods or services.

The Company has adopted IFRS 15 on the effective date using a modified retrospective basis which involves not restating periods prior to the date of initial application. The application of this new standard had no impact on the reported results. The Company's accounting policy for revenue recognition under IFRS 15 is as follows:

To determine the amount and timing of revenue to be recognized, the Company follows a 5-step process:

1. Identifying the contract with the customer
2. Identifying the performance obligations
3. Determining the transaction price
4. Allocating the transaction price to the performance obligations
5. Recognizing revenue when/as performance obligations are satisfied.

IFRS 15 principally affects the timing of revenue recognition for transactions by each element in an arrangement (distinct goods or services in a bundled price or deliveries that occur at different points in time and/or over different periods of time). Revenue is recognized when the Company transfers control of the goods or services to the customer upon delivery.

Certain information and disclosures normally included in annual consolidated financial statements, prepared in accordance with IFRS 15 Revenue from contracts, were omitted where such information is not considered material to the understanding of the Company's interim financial information.

Under IFRS 15, we apply the following practical expedients:

- We do not adjust the promised amount of consideration for the effects of a significant financing component if, at contract inception, we expect the period between when we transfer the promised goods or services to a customer and when the customer pays for that good or service will be one year or less; and
- Costs of obtaining a contract that would be amortized within one year or less are immediately expensed.

#### IFRS 9 – Financial Instruments

In July 2014, the IASB completed the three-part project to replace IAS 39, Financial instruments: recognition and measurement by issuing IFRS 9, Financial instruments. IFRS 9, Financial instruments includes (a) classification and measurement of financial assets and financial liabilities, (b) a forward-looking 'expected loss' impairment model and (c) a substantially-reformed approach to hedge accounting.

The Company has adopted IFRS 9 on the effective date and determined that there was no impact on its reported results.

#### New and revised IFRS issued but not yet effective

The following is a list of standards and amendments that have been issued but are not yet effective and have not yet been adopted by the Company:

### IFRS 16

IFRS 16, issued in January 2016, introduces a single lessee accounting model that requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. The standard will supersede IAS 17 Leases, IFRIC 4 Determining Whether an Arrangement Contains a Lease, SIC-15 Operating Leases - Incentives and SIC-27 Evaluating the Substance of Transactions Involving the Legal Form of a Lease. IFRS 16 is effective for annual periods beginning on or after January 1, 2019. The Company is currently assessing the impact of this standard on its consolidated financial statements. The Company expects to apply the standard for its consolidated financial statements dated June 30, 2020.

### **FINANCIAL AND OTHER INSTRUMENTS**

Enablence's financial instruments consist of cash and cash equivalents, accounts receivable, accounts payable and accrued liabilities, convertible debentures and notes payable. Unless otherwise noted, it is the opinion of Enablence's management that Enablence is not exposed to significant interest, currency or credit risk arising from these financial instruments. The fair value of these financial instruments approximates their carrying value due to their short-term maturity or capacity of prompt liquidation.

### **ADDITIONAL INFORMATION**

Additional information related to the Company can be found on SEDAR at: [www.sedar.com](http://www.sedar.com).