



INVENTRONICS LIMITED

2022 ANNUAL FINANCIAL REPORT

MANAGEMENT DISCUSSION & ANALYSIS

For the year ended December 31, 2022

2022 Annual and Fourth Quarter Financial Report – December 31, 2022

Management Discussion and Analysis

This Management Discussion and Analysis (“MD&A”) is dated March 30, 2023 and was prepared based on information available to Inventronics Limited (referred to herein as “Inventronics” or the “Corporation”) as of this date to help readers interpret Inventronics’ financial results for the three and twelve month periods ended December 31, 2022. This MD&A should be read in conjunction with the Corporation’s 2022 audited annual financial statements which consist of the Corporation’s Statement of Financial Position, Statement of Comprehensive Income, Statement of Cash Flows, Statement of Changes in Equity, Notes to the Financial Statements and the Auditors’ Report thereon (collectively referred to as the “Financial Statements”). The Financial Statements and other information relating to the Corporation are available under Inventronics’ profile on the SEDAR website at www.sedar.com. The financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board, and all dollar amounts within this report are expressed in Canadian dollars unless otherwise stated.

Forward-looking information advisory

Certain statements contained in this report, including this MD&A, contain forward-looking information that represents the Corporation’s internal projections, expectations, estimates or beliefs concerning, among other things, the Corporation’s expectations, perceptions and/or beliefs with respect to: economic conditions and the related impact on the Corporation’s customers and/or demand for the Corporation’s products; longer production runs positively influencing certain operating efficiencies; its working capital position and its sufficiency to support the Corporation’s operations; its future revenue expectations; the manner in which the Corporation will utilize its property, plant and equipment and the useful lives and residual value of that property, plant and equipment; and its forecast financial results. All statements other than statements of historical fact may be forward-looking statements. In some cases, forward-looking statements can be identified by terminology such as “may”, “will”, “should”, “expects”, “projects”, “plans”, “anticipates”, and similar expressions. Forward-looking statements are not guarantees of future performance and involve risks and uncertainties, which could cause actual results to differ materially from those anticipated in these forward-looking statements. These risks and uncertainties include but are not limited to: general economic conditions; foreign currency fluctuations; actions by government authorities; competitor activity; indebtedness of the Corporation; availability of future financing; customer concentration risks; changes in the price of raw materials; interest rates; and changes in the communications, power and cable industries. The forward-looking information contained in this report reflects several material factors and expectations and assumptions of Inventronics including, without limitation: that Inventronics will continue to conduct its operations in a manner consistent with past operations; the general continuance of current industry conditions; the continuance of existing (and in certain circumstances, the implementation of proposed) tax and regulatory regimes; and the continued availability of adequate debt financing and cash flow from operations to fund its operations. Although management of the Corporation believes such statements are reasonable, undue reliance should not be placed on forward-looking information as the Corporation can give no assurance that such assumptions will prove to be correct. The forward-looking information has been included herein to provide shareholders with a more complete outlook on the Corporation’s future business and operations and this information may not be appropriate for other purposes. The Corporation does not undertake to update the forward-looking information contained herein except as required by applicable laws.

1. Corporation Overview

Founded in 1970 in Brandon, Manitoba, Canada, Inventronics designs and manufactures protective enclosures for use in utility-type infrastructures. The Corporation’s products are typically found in telecommunication networks, cable television networks, electric power distribution networks, oil and gas installations, and other industries where they are utilized in both outdoor and indoor applications to house and protect passive and/or active electrical and electronic components. Although the Corporation’s products have been primarily placed in service throughout North America, it is not uncommon to find Inventronics’ enclosures in other international infrastructures as well. A significant portion of Inventronics’ revenues are generated from the sale of Inventronics-branded standard products which are sold directly to utilities, original equipment manufacturers and/or through distributors. Additionally, for customers with specialty requirements, the Corporation designs and manufactures products that have been custom designed to suit the customer’s particular needs. This can range from the modification of an existing Inventronics cabinet to the conceptualization and manufacture of a completely new enclosure.

Inventronics operates from its ISO 9001:2015 certified facility located in Brandon, Manitoba where product design, manufacturing, corporate administration and sales functions are performed. The Corporation’s production employees are organized under the United Steelworkers Union. The Corporation is incorporated in the Province of Alberta, Canada, has no subsidiaries, and its shares are publicly traded on the TSX Venture Exchange under the symbol IVX.

2. Selected Annual Financial Information

Selected Annual Financial Information

(in thousands of dollars, except per share amounts)

For the years ended December 31

	2022	2021	2020
Revenue	14,245	9,985	5,640
EBITDA ¹	3,327	1,665	930
Net earnings	2,093	1,890	684
Total assets	6,027	5,228	3,742
Long-term debt, excluding current portion	1,989	2,049	2,079
Basic earnings per share	43.4¢	41.0¢	15.5¢

Note 1. See "Non-IFRS Measures" below.

3. Summary of Financial Results

Revenue in 2022 increased substantially to \$14,245,000 as compared to \$9,985,000 in 2021, which is a 43% increase year over year. The upgrading of communications infrastructure to support the demand for increased internet bandwidth is continuing to drive this surge in enclosure sales and is challenging the industry's supply capacity. The speed of this infrastructure buildout has been enhanced by government programs in both Canada and the United States. The pace of the buildout is expected to moderate following the conclusion of the government programs. The Corporation's customer base has expanded in the United States to nearly 50% of revenue. Net earnings also rose in the 2022 fiscal year to \$2,093,000 as compared to \$1,890,000 in 2021, but the earnings improvement is masked by the one-time deferred tax recovery of \$511,000 recorded in 2021. Working capital rose sufficiently in 2022 to enable the payment of a special dividend in the amount of \$1,694,000 in the fourth quarter, leaving a closing balance of \$2,394,000 compared to \$1,527,000 in the prior year.

Selected Quarterly Financial Information

(in thousands of dollars, except percentage and per share amounts)

	2022				2021			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Revenue	2,739	3,450	4,269	3,787	1,951	3,374	2,837	1,823
Cost of sales as a percentage of Revenue	77%	72%	67%	69%	81%	78%	72%	76%
EBITDA ¹	533	841	1,204	749	272	646	504	243
Net earnings	252	536	803	501	303	967	440	181
Basic earnings per share	5.2¢	11.1¢	16.7¢	10.4¢	6.6¢	20.8¢	9.8¢	4.0¢

Note 1. See "Non-IFRS Measures" below.

4. Results of Operations

Revenue

Revenue for the year ended December 31, 2022 of \$14,245,000 was \$4,260,000, or 43%, more than the \$9,985,000 achieved in 2021. Fourth quarter revenue of \$2,739,000 was \$788,000, or 40%, higher than the \$1,951,000 reported for the same quarter of 2021. It is typical for the Corporation to experience seasonal high revenue through the second and third quarter and for the first and fourth quarters to be lower due to reduced construction activity. In 2022, the first quarter revenue was abnormally high due to certain customers building their inventories earlier than normal and this level of activity is expected to moderate in 2023.

The strength in revenue for 2022 was driven by the continuing build-out of communications infrastructure in Canada and the USA in support of the demand for bandwidth to address the growth in video streaming, online gaming and remote work connectivity. These investments are forecast to continue for several years in both countries to improve communication services throughout the more remote regions. The sales team is monitoring the government programs designed to support this build-out and all customer accounts to remain positioned to respond if enclosure demand expectations change.

Cost of Sales

Cost of sales for the year ended December 31, 2022 was \$10,125,000 (71% of revenue) compared to \$7,689,000 (77% of revenue) in 2021. The 2022 fourth quarter total was \$2,115,000 (77% of revenue) compared to \$1,588,000 (81% of revenue) for the same period of 2021. These results demonstrate the effects of increased production volumes on the distribution of fixed costs. Overall, material costs remained stable through 2022, which helped to preserve margins. Longer production runs continue to positively influence certain operating efficiencies.

Selling and Administration Expense

Selling and administration expense for the 2022 fiscal year was \$1,078,000 compared to \$771,000 in 2021. These expenses for the fourth quarter of 2022 were \$186,000 compared to \$129,000 for the same period of 2021. The increase in these expenses was primarily attributable to the increase in volumes and the recognition of non-cash stock-based compensation.

Interest

Interest expense for the three and twelve month periods ended December 31, 2022 of \$26,000 and \$114,000, respectively, were lower than the \$59,000 and \$156,000 reported for the comparative periods of 2021. In the fourth quarter of 2021, one-time financing costs incurred a number of years ago were chosen to be written off and this increased the interest expense totals in both periods by \$21,000. The remaining reduction in interest costs in 2022 were a result of lower interest rates negotiated with the Corporation's lenders.

Net Earnings

For the year ended December 31, 2022, the Corporation reported net earnings of \$2,093,000, or 43.4 cents per share, compared to net earnings of \$1,890,000, or 41.0 cents per share, for 2021. The fourth quarter net earnings of \$252,000, or 5.2 cents per share, was slightly lower than the net earnings of \$303,000, or 6.6 cents per share, reported for the fourth quarter of 2021. This improved profitability for the year was a result of the increased revenue, although it is important to note that the 2021 net earnings were increased by the one-time recognition of \$511,000 in deferred tax recovery. The operational improvement is more accurately represented by the 2022 pre-tax earnings of \$2,928,000 as compared to the 2021 result of \$1,369,000, an increase of \$1,559,000.

5. Income Taxes

For the year ended December 31, 2022, the Corporation's income tax expense was \$835,000 as compared to an income tax recovery of \$521,000 in 2021. The \$1,457,000 of non-capital losses carried over from 2021 will all be used to reduce the cash tax payable for 2022.

6. Liquidity and Capital Resources

Cash Flow from Operations

The following table details the cash flow from operations for both the 2022 fourth quarter and the fiscal year as compared to the same periods in 2021.

Cash Flow from Operations				
<i>(in thousands of dollars)</i>				
For the periods ended December 31	Three months		Twelve months	
	2022	2021	2022	2021
Net earnings	252	303	2,093	1,890
Add: Interest on long-term debt ¹	26	37	112	129
Add: Depreciation	35	39	134	138
Add: Deferred income tax	4	(122)	515	(511)
Add: Other items not involving cash	61	21	151	24
Cash flow from Operations	378	278	3,005	1,670

Note 1. Interest on long-term debt considered a component of financing and therefore added back to net earnings to determine cash flow from operations.

Working Capital Position

As at December 31, 2022, the Corporation reported a working capital balance of \$2,394,000, which represented an increase of \$867,000 over the prior year value of \$1,527,000. This working capital position is net of the special dividend paid in the fourth quarter totalling \$1,694,000. The year end working capital ratio of 3.16:1 is sufficient to support the projected operating requirements of the business.

Working Capital Position

(in thousands of dollars, except ratio calculation)

At the end of	2022				2021			
	Q4	Q3	Q2	Q1	Q4	Q3	Q2	Q1
Current assets	3,536	5,085	4,513	4,182	2,419	3,478	2,886	2,801
Current liabilities	1,142	2,885	1,229	2,037	892	2,134	1,201	1,565
Working capital	2,394	2,200	3,284	2,145	1,527	1,344	1,685	1,236
Working capital ratio	3.10 :1	1.76 :1	3.67 :1	2.05 :1	2.71 :1	1.63 :1	2.40 :1	1.79 :1

Working Capital Liquidity

Working capital liquidity for operating purposes has generally been provided through positive cash flow from operations and the Corporation's operating credit facility. The Corporation's unmarginated operating credit facility limit is \$1,200,000. The credit facility is secured against trade accounts receivable and inventories (see "Borrowing Arrangements and Covenants" below).

7. Share Capital

An unlimited number of common shares are authorized for issue. The following table summarizes the authorized, issued and outstanding common shares of the Corporation.

Share Capital				
<i>(dollar amounts in thousands)</i>				
As at	December 31, 2022		December 31, 2021	
	Shares	Amount	Shares	Amount
Outstanding, beginning of the period	4,805,145	\$ 1,191	4,405,145	\$ 2,276
Reduction of stated capital	-	-	-	(1,153)
Options exercised	33,000	75	400,000	68
Authorized, issued and outstanding common shares	4,838,145	\$ 1,266	4,805,145	\$ 1,191

Reduction of stated capital

At the Corporation's annual general meeting held on August 18, 2021, shareholder approval was received to reduce the stated capital of the Corporation by \$1,153,000. The purpose of reducing the stated capital of the Common Shares is to increase the difference between the realizable value of the Corporation's assets and the aggregate of the Corporation's liabilities and the stated capital of the Common Shares, thereby providing the Corporation with additional financial flexibility.

Stock option plan

Inventronics maintains a stock option plan providing the Corporation the ability to grant options to employees and directors to purchase one common share of the Corporation per option. In the twelve months ended December 31, 2022, there were 450,000 options granted to senior management and directors at an exercise price of \$1.65 per share and vesting over the next two years. In the third quarter of 2022, 33,000 options were exercised leaving 417,000 options outstanding at year end (2021 – Nil). The exercised options contributed to share capital \$55,000 plus \$20,000 of reclassified contributed surplus in relation to the option expense previously recognized. Subsequent to year end, an additional 33,000 options were exercised at an exercise price of \$1.65 per share and no additional options were granted to employees or directors of the Corporation.

Stock Options Outstanding

For the years ended December 31	2022	2021
Opening balance	-	400,000
Options granted	450,000	-
Options exercised	(33,000)	(400,000)
Ending balance	417,000	-

The following table summarizes the issued and outstanding common shares of the Corporation along with stock options convertible into common shares.

Diluted Common Shares Outstanding				
As at	December 31, 2022		December 31, 2021	
	Number of shares	Weighted average number of shares	Number of shares	Weighted average number of shares
Issued and outstanding common shares	4,838,145	4,817,565	4,805,145	4,614,486
Stock options outstanding ⁽¹⁾	417,000	150,261	-	-
Diluted common shares outstanding	5,255,145	4,967,826	4,805,145	4,614,486

Note 1: For the purposes of calculating the diluted weighted average number of shares outstanding, only those options which are considered "in the money" (strike price below the Corporation's annual average common share price) are considered.

Dividend

In the third quarter of 2022, the Corporation's Board of Directors ("Board") declared a special dividend of \$0.35 per share payable on November 4, 2022 in the amount of \$1,694,000 (2021 - \$0.20 per share payable on November 3, 2021 in the amount of \$961,000). The Corporation has no set policy for dividends but the board and management consider dividends from time to time based on cash balances, working capital, and capital asset requirements.

8. Borrowing Arrangements and Covenants

Operating credit

The Corporation maintains a demand operating credit facility in the form of an overdraft lending account, which provides an authorized limit of \$1,200,000 and an interest rate of prime plus 0.90% (2021 – prime plus 1.75%). At December 31, 2022, an amount of \$1,200,000 under this facility was available, of which \$Nil was drawn (2021 - \$850,000 available and \$Nil drawn). The demand operating credit facility is unmarginated although the lender does retain a general security agreement over the Corporation's accounts receivable and inventory balances. New in 2022, the Corporation arranged a Master Equipment Lease Line in the amount of \$3,000,000, to be used when necessary to finance equipment additions. This Lease Line was undrawn at December 31, 2022. The Corporation is in compliance with all obligations pertaining to its credit facilities.

Long-term debt

The Corporation has a long-term lending agreement in the form of a fixed rate mortgage maturing in 2043; bearing interest at 5.25% (2021 – 5.75%); repayable monthly in blended principal and interest installments of \$14,000; secured by a mortgage on the Corporation's production facility and land in Brandon, Manitoba, which was valued at \$4,400,000 by a professional appraiser in July 2022. The facility is also secured by a general security agreement providing a security interest in all of the Corporation's present and after acquired personal property but accepting a subordinate position to all existing registered charges. Although containing general performance conditions, the loan agreement does not contain any financial covenants that must be periodically tested. The Corporation is in compliance with all obligations pertaining to this agreement.

9. Foreign Currency Exposure

Foreign currency risk pertains to the number and value of transactions denominated in US dollars. The Corporation did not engage in any derivative hedging activities during the years ended December 31, 2022 and 2021 other than a natural hedge that occurs by carrying US dollar denominated cash, receivable and payable balances simultaneously.

10. Collective Bargaining Agreement

The Corporation's production labour force is organized under a collective bargaining agreement ("CBA") with the United Steel Workers. A new 5-year CBA was ratified on March 15, 2022 with an expiry date of December 31, 2026.

11. Related Party Transactions

The four-person senior management team are members of Inventronics' Board of Directors ("Board") and receive no compensation for their service as Board members. The Corporation pays fixed and variable compensation to its senior management team for their employment services. For the three and twelve months ended December 31, 2022, the Corporation expensed \$137,000 (2021 - \$117,000) and \$1,109,000 (2021 - \$892,000), respectively, related to those compensation arrangements. In addition, the senior management team was granted 400,000 stock options in 2022 that were valued at \$220 using the Black Scholes model (see Note 11 Share Capital). For the year ended December 31, 2022, the Corporation expensed \$134,000 (2021 - \$Nil) related to those options.

12. Governance

The Corporation's Board is comprised of the four members of the Corporation's senior management team and two independent members. The Corporation's Chief Executive Officer and the two independent members comprise the Corporation's Audit Committee.

13. Non-IFRS Measures

EBITDA

Earnings before interest, tax, depreciation and amortization ("EBITDA") is not a recognized measure under IFRS. However, management believes that EBITDA is a useful supplementary measure to net earnings, as it provides investors with an indication of cash earnings prior to debt service, capital expenditure, income tax and non-cash items. Readers are cautioned, however, that EBITDA should not be construed as an alternative to net earnings determined in accordance with IFRS as an indicator of the Corporation's performance or to cash flows from operating, investing and financing activities as a measure of liquidity or cash flows. The Corporation's method of calculating EBITDA may differ from the methods by which other companies calculate EBITDA and, accordingly, the EBITDA used herein may not be comparable to measures used by other companies.

Reconciliation of EBITDA to Net Earnings

(in thousands of dollars)

<i>For the periods ended December 31</i>	Three months		Twelve months	
	2022	2021	2022	2021
EBITDA	533	272	3,327	1,665
Less: Depreciation	35	39	134	138
Less: Option expense	61	-	151	2
Less: Interest expense	26	58	114	156
Less: Income tax	159	(128)	835	(521)
Net earnings	252	303	2,093	1,890

14. Outlook

In addition to other sections of this MD&A, this section contains forward-looking information and actual outcomes may differ materially from those expressed or implied therein. Please see the forward-looking information advisory included in the opening section of this MD&A.

The Corporation is a part of the supply chain to the construction and maintenance of communications infrastructures in North America which are essential in supporting the video streaming, online gaming, and remote work environment that has been established. The continuing digitization of the economy and the rapid expansion of the metaverse are expected to play a significant part in the demand for the Corporation's products for the foreseeable future. The key risks in this uncertain environment are changes in government support programs and regulation, employee availability, customer spending patterns and supply chain challenges. These risks are being addressed and mitigated to the extent possible but are largely beyond the Corporation's control. The Corporation's balance sheet continued to strengthen through 2022 and this is expected to provide a cushion to any potential future variability in demand.

Inventronics' sales growth in 2022 was driven by the ongoing construction of broadband infrastructure and particularly the laying of fibre optic lines into the large rural and smaller centre regions of North America. This build-out is a direct response to the strong demand for bandwidth from consumers who want access to video streaming, gaming, and work from home capability. Activity levels have reached a new threshold based on the Corporation's increased customer base and exposure to the US market. With the continuation of the buildout, ongoing government programs, and the absence of a recession, management believes this level of revenue to be sustainable.