

Unaudited condensed interim consolidated financial statements of

Martello Technologies Group Inc.

For the three and six months ended September 30, 2019 and
2018

Martello Technologies Group Inc.

“Notice to Reader”

The accompanying condensed unaudited interim consolidated financial statements of Martello Technologies Group Inc. for the three and six months ended September 30, 2019 and 2018 have been prepared by management and approved by the Audit Committee and the Board of Directors of the Company. These statements have not been reviewed by the Company’s external auditors.

Dated: November 19, 2019

“Erin Crowe”

Erin Crowe
Chief Financial Officer

“John Proctor”

John Proctor
Chief Executive Officer

Martello Technologies Group Inc.

For the three and six months ended September 30, 2019 and 2018

Table of contents

Condensed interim consolidated statements of loss and comprehensive loss.....	4
Condensed interim consolidated statements of financial position	5
Condensed interim consolidated statements of changes in shareholders' equity.....	6
Condensed interim consolidated statements of cash flows	7
Notes to the condensed interim consolidated financial statements	8-22

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

Martello Technologies Group Inc.

Condensed interim consolidated statements of loss and comprehensive loss
For the three and six months ended September 30, 2019 and 2018

Unaudited

(In Canadian dollars)

	Notes	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
		(3 months ended)		(6 months ended)	
Income					
Sales	5,6	\$ 3,115,919	\$ 1,964,795	\$ 6,448,072	\$ 3,901,949
Cost of goods sold		264,715	125,402	509,295	251,840
Gross margin		2,851,204	1,839,393	5,938,777	3,650,109
Expenses					
Research and development	7	1,138,733	787,067	2,310,729	1,658,900
Sales and marketing	7	1,389,320	589,733	2,709,813	1,087,613
General and administrative	7	1,394,613	1,051,711	2,583,122	1,892,827
Depreciation	2,13	80,815	20,461	161,508	40,687
Amortization		267,253	105,691	525,337	211,131
Acquisition-related costs		30,000	142,513	60,878	379,372
		4,300,734	2,697,176	8,351,387	5,270,530
Loss from operations		(1,449,530)	(857,783)	(2,412,610)	(1,620,421)
Other income/expense					
Interest income		6,908	1,282	17,734	2,722
Interest expense	2	(65,336)	-	(117,631)	(2,519)
Reverse acquisition costs		-	(390,848)	-	(774,258)
Reverse acquisition transaction costs		-	(1,040,012)	-	(1,040,012)
Accretion of long-term debt	12	(18,052)	(15,578)	(34,271)	(30,761)
Foreign exchange gain (loss)	4,17	(56,027)	8,323	(138,052)	(38,450)
Other income		1,604	10,000	1,604	17,269
Loss before income tax		(1,580,433)	(2,284,616)	(2,683,226)	(3,486,430)
Income tax recovery		83,668	134,365	296,208	162,518
Net loss		(1,496,765)	(2,150,251)	(2,387,018)	(3,323,912)
Other comprehensive income (loss) that may be reclassified to net income (loss):					
Cumulative translation adjustment		(276,481)	-	(357,660)	-
Total comprehensive loss		(1,773,246)	(2,150,251)	(2,744,678)	(3,323,912)
Weighted average shares outstanding					
Basic	8	192,638,535	166,468,438	191,938,051	145,817,875
Net loss per share					
Basic and diluted	8	\$ (0.01)	\$ (0.01)	\$ (0.01)	\$ (0.02)

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

Martello Technologies Group Inc.

Condensed interim consolidated statements of financial position

As at September 30, 2019 and March 31, 2019

Unaudited

(In Canadian dollars)

	Notes	September 30, 2019	March 31, 2019
Assets			
Current assets			
Cash	9	\$ 9,007,386	\$ 6,649,302
Trade and other accounts receivable	10	2,855,999	3,367,694
Investment tax credits and grants receivable	7	659,796	887,949
Prepaid expenses		426,997	505,338
Inventories		180,693	233,575
Total current assets		13,130,871	11,643,858
Goodwill		9,798,835	10,068,099
Intangible assets		6,644,104	7,336,936
Equipment and leasehold improvements		466,844	474,040
Right-of-use assets	2,13	472,491	-
Total assets		30,513,145	29,522,933
Liabilities			
Current liabilities			
Accounts payable and accrued liabilities	11	2,293,267	2,259,170
Foreign exchange forward contract liability	4	47,668	5,713
Current portion of deferred revenue	5	3,124,273	3,386,512
Current portion of leasehold incentives		-	29,085
Current portion of long-term debt	12	1,156,944	1,033,775
Current portion of lease obligation	2	172,411	-
Total current liabilities		6,794,563	6,714,255
Deferred revenue	5	1,294,253	1,457,432
Leasehold incentives		-	30,506
Long-term debt	12	1,822,604	2,386,295
Lease obligation	2	345,420	-
Deferred tax liability		318,288	620,229
Total liabilities		10,575,128	11,208,717
Shareholders' equity			
Share capital	14	31,711,912	27,443,488
Contributed surplus	14	2,537,957	2,419,902
Warrants	14	19,500	37,500
Accumulated other comprehensive income (loss)		(304,869)	52,791
Deficit		(14,026,483)	(11,639,465)
Total shareholders' equity		19,938,017	18,314,216
Total liabilities and equity		30,513,145	29,522,933

Approved by the Board on November 19, 2019 and signed on its behalf by:

Original signed “Colley Clarke” Director

Original signed “Michael Michalyshyn” Director

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

Martello Technologies Group Inc.

Condensed interim consolidated statements of changes in shareholders' equity for the three and six months ended September 30, 2019 and 2018

(In Canadian Dollars)

	Notes	Shares outstanding #	Share capital \$	Warrants \$	Contributed surplus \$	Accumulated other comprehensive loss \$	Deficit \$	Total shareholders' equity \$
Balance at April 1, 2018		110,463,366	11,144,814	37,500	1,874,953	-	(6,227,665)	6,829,602
Net loss and comprehensive loss for the period		-	-	-	-	-	(1,173,662)	(1,173,662)
Issuance of common stock	14	50,568,738	7,540,453	-	-	-	-	7,540,453
Exercise of stock options	14	98,666	14,800	-	(4,008)	-	-	10,792
Share-based compensation	14	-	-	-	151,081	-	-	151,081
Balance as at June 30, 2018		161,130,770	18,700,067	37,500	2,022,026	-	(7,401,327)	13,358,266
Net loss and comprehensive loss for the period		-	-	-	-	-	(2,150,251)	(2,150,251)
Issuance of common stock	14	4,666,666	700,000	-	-	-	-	700,000
Shares issued for reverse acquisition	14	6,086,540	912,981	-	-	-	-	912,981
Exercise of stock options	14	612,502	477,765	-	(410,390)	-	-	67,375
Share-based compensation	14	-	-	-	245,820	-	-	245,820
Balance as at September 30, 2018		172,496,478	20,790,813	37,500	1,857,456	-	(9,551,578)	13,134,191
Balance as at April 1, 2019		191,237,568	27,443,488	37,500	2,419,902	52,791	(11,639,465)	18,314,216
Net loss for the period		-	-	-	-	-	(890,253)	(890,253)
Other comprehensive loss		-	-	-	-	(81,179)	-	(81,179)
Total comprehensive loss for the period		-	-	-	-	(81,179)	(890,253)	(971,432)
Share-based compensation	14	-	-	-	95,011	-	-	95,011
Balance as at June 30, 2019		191,237,568	27,443,488	37,500	2,514,913	(28,388)	(12,529,718)	17,437,795
Net loss for the period		-	-	-	-	-	(1,496,765)	(1,496,765)
Other comprehensive loss		-	-	-	-	(276,481)	-	(276,481)
Total comprehensive loss for the period		-	-	-	-	(276,481)	(1,496,765)	(1,773,246)
Issuance of common stock	14	15,333,332	4,600,000	-	-	-	-	4,600,000
Less: Transaction costs attributable to share issue		-	(570,045)	-	-	-	-	(570,045)
Exercise of warrants	14	493,715	72,309	(18,000)	-	-	-	54,309
Exercise of stock options	14	901,331	166,160	-	(62,961)	-	-	103,199
Share-based compensation	14	-	-	-	86,005	-	-	86,005
Balance as at September 30, 2019		207,965,946	31,711,912	19,500	2,537,957	(304,869)	(14,026,483)	19,938,017

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

Martello Technologies Group Inc.

Condensed interim consolidated statements of cash flows

For the six months ended September 30, 2019 and 2018

(in Canadian Dollars)

	Note	September 30, 2019	September 30, 2018
Operating activities			
Loss before income tax		(2,683,226)	\$ (3,486,430)
Items not affecting cash:			
Depreciation	2,13	161,508	40,687
Amortization of leasehold incentives		(11,288)	(17,251)
Amortization of intangible assets		525,337	211,131
Reverse acquisition transaction costs		-	1,040,012
Loss on disposal of computer equipment		-	1,716
Accretion of long-term debt		34,271	30,761
Stock-based compensation	7,14	181,016	396,901
Lease interest paid	2	12,726	-
Unrealised foreign exchange gain		(24,018)	-
Income tax refund		7,814	-
Net change in operating components of working capital	15	647,193	(614,899)
Total cash flows used in operations		(1,148,667)	(2,397,372)
Investing activities			
Cash acquired on reverse acquisition		-	636,942
Additions to equipment and leasehold improvements		(72,098)	(55,880)
Total net cash flows provided by (used in) investing activities		(72,098)	581,062
Financing activities			
Proceeds from issuance of common shares	14	4,029,955	7,540,453
Proceeds from exercise of stock options	14	103,199	78,167
Proceeds from exercise of warrants	14	54,309	-
Proceeds from line of credit		-	25,000
Proceeds of long-term debt		12,000	-
Repayment of long-term debt	12	(486,793)	(103,003)
Repayment of lease obligations	2	(99,095)	-
Total cash flows provided by financing activities		3,613,575	7,540,617
Net change in cash and restricted cash		2,392,810	5,724,307
Cash and restricted cash, beginning of period		6,649,302	2,141,432
Effects of currency translation on cash and cash equivalents		(34,726)	-
Cash and restricted cash, end of period		9,007,386	7,865,739
Cash and restricted cash consists of the following:			
Cash and cash held in trust		8,980,027	7,665,918
Restricted cash		27,359	199,821
Total cash and restricted cash		9,007,386	7,865,739

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

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

1. Corporate information

Martello Technologies Group Inc., formerly Newcastle Energy Corp. (the "Corporation") develops products and solutions that optimize the performance of real-time applications on cloud and enterprise networks, while giving IT teams and service providers control and visibility of their entire IT infrastructure from a single platform. The Corporation's common shares are traded on the TSX Venture Exchange ("TSXV") under the trading symbol MTLO.

2. Basis of preparation and accounting policies

The condensed interim consolidated financial statements have been prepared under the going concern assumption and using the historical cost basis, except for foreign exchange forward contracts which are measured at fair market value.

These condensed interim consolidated financial statements have been prepared in accordance with International Accounting Standard (IAS) 34, *Interim Financial Reporting*, and should be read in conjunction with the Corporation's most recent annual audited consolidated financial statements, which are for the year ended March 31, 2019.

Significant accounting policies

The significant accounting policies used in preparing these condensed interim consolidated financial statements are the same as those disclosed in the Corporation's 2019 annual consolidated financial statements, except for the effect of adoption of IFRS 16 on April 1, 2019. The new IFRS 16 accounting policies and the effect of adoption of IFRS 16 are described below. The previous accounting policy for leases is disclosed in note 2.2(l) to the Corporation's 2019 annual consolidated financial statements.

(a) *New accounting policies*

i. Leases

At inception of a contract, the Corporation assesses whether a contract is, or contains, a lease based on whether the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration. The Corporation recognizes a right-of-use asset and a lease liability at the lease commencement date.

The right-of-use asset is initially measured at an amount equal to the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any initial direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, less any lease incentives received. The right-of-use asset is subsequently measured at cost net of accumulated depreciation. Depreciation is calculated on a straight-line basis over the shorter of the lease term or useful economic life of the asset. The lease term includes periods covered by an option to extend if the Corporation is reasonably certain to exercise that option.

The lease liability is initially measured at the present value of the unpaid lease payments as at the commencement date, discounted using the Corporation's incremental borrowing rate unless the interest rate implicit in the lease is known. The Corporation's incremental borrowing rate for a lease is the rate that the Corporation would pay to borrow an amount necessary to obtain an asset of a similar value to the right-of-use asset on a collateralized basis over a similar term.

The lease liability is subsequently measured at amortized cost using the effective interest method. It is remeasured if there is a change in future lease payments arising from a change in an index or rate; there is a change in the Corporation's estimate of the amount expected to be payable under a residual value guarantee; or the Corporation changes its assessment of whether it will exercise a purchase, extension or termination option. On remeasurement, a corresponding adjustment is made to the carrying amount of the right-of-use asset, or directly in profit or loss if the carrying amount of the right-of-use asset has been reduced to zero.

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

Basis of preparation and accounting policies (continued)

(a) New accounting policies

i. Leases

The Corporation has elected to apply the practical expedient not to recognize right-of-use assets and lease liabilities for short-term leases that have a lease term of 12 months or less and leases of low-value assets. The lease payments associated with these leases are recognized as an expense on a straight-line basis over the lease term.

Effect of adoption of IFRS 16

In January 2016, the IASB issued IFRS 16, which replaces IAS 17, Leases (“IAS 17”), 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 sets out the principles for the recognition, measurement, presentation and disclosure of leases and require lessees to account for all leases under a single on-balance sheet model similar to the accounting for finance leases under IAS 17, and report their effects. The standard provides a single lessee accounting model, requiring lessees to recognize assets and liabilities for all major leases. The Corporation adopted “Leases” IFRS 16 with effect from April 1, 2019 using the modified retrospective approach and accordingly did not restate comparative information for the prior periods presented.

On initial application, the Corporation elected to record right-of-use assets based on the corresponding lease liability adjusted for any prepaid or accrued lease payments that existed at the date of transition. The Corporation elected to apply the following additional practical expedients on initial application: to exclude initial direct costs in the measurement of the right-of-use assets in existence at April 1, 2019; apply hindsight in assessing certain lease extension options; and exclude from the application of the standard any leases for which the lease term ends within 12 months of the date of initial application as short-term leases.

The Corporation applied the definition of a lease and the requirements of IFRS 16 to its leases of real estate in Ottawa and Amsterdam based on the contracts that were in effect on April 1, 2019.

Right-of-use assets of \$566,692 and corresponding lease liabilities of \$613,113 were recorded as of April 1, 2019, with no net impact on retained earnings and were calculated as follows:

Right-of-use asset:	\$
Balance at March 31, 2019	-
Adoption of IFRS 16 on April 1, 2019	613,113
Less unamortized leasehold incentives	<u>(46,421)</u>
Balance at April 1, 2019	566,692
Depreciation for the period	(85,327)
Foreign exchange translation	<u>(8,874)</u>
Balance at September 30, 2019	<u>472,491</u>
Lease liability:	\$
Balance at March 31, 2019	-
Adoption of IFRS 16 on April 1, 2019	<u>613,113</u>
Balance at April 1, 2019	613,113
Interest expense	12,726
Payments	(99,095)
Foreign exchange translation	<u>(8,913)</u>
Balance at September 30, 2019	<u>517,831</u>

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

Basis of preparation and accounting policies (continued)

(a) New accounting policies

i. Leases

For the three and six months ended September 30, 2019, the Corporation recognized \$42,469 and \$85,327, respectively, as depreciation on right-of-use assets, and \$7,417 and \$12,726, respectively, as interest expense on the lease liability. No other lease contracts were entered into during the three and six months ended September 30, 2019 to which the standard applies.

In applying the practical expedient for short-term leases, the Corporation has excluded rent payments of \$60,763 from the right-of-use asset and lease liability calculations.

When measuring lease liabilities, the Corporation discounted lease payments using its incremental borrowing rate at April 1, 2019 of 5.4%.

The Corporation has applied judgment in the process of applying IFRS 16 and determining the appropriate lease term on a lease by lease basis, which has a significant effect on the measurement of the lease liability and right-of-use assets recognized. Management considers many factors including any events that create an economic incentive to exercise a renewal option including expected future performance and past business practice. The Corporation has also exercised judgment in determining the incremental borrowing rate based on the term, security, the lessee entity's economic environment, credit rating, level of indebtedness and asset specific adjustments.

The following table reconciles the Corporation's operating lease obligations at March 31, 2019, as previously disclosed in note 25 to the Corporation's 2019 annual consolidated financial statements, to the lease liability recognized on initial application of IFRS 16 at April 1, 2019:

	Total
	\$
Operating lease commitment as at March 31, 2019	1,221,630
Recognition exemption of low value leases	(35,683)
Recognition exemption of leases with terms less than 1 year	(106,335)
<u>Lease operating costs not included in the measurement of lease obligations</u>	<u>(433,443)</u>
Operating lease commitments (undiscounted)	646,169
Discounted using the incremental borrowing rate and recognised as at April 1, 2019	613,113

ii. Uncertainty over income tax treatment

In June 2017, the International Accounting Standards Board (IASB) issued IFRIC Interpretation 23 - *Uncertainty over Income Tax Treatments* (the "Interpretation") to address the accounting for income taxes when treatments involve uncertainty that affects the application of IAS 12, Income Taxes ("IAS 12"). The Interpretation does not apply to taxes or levies outside the scope of IAS 12, nor does it specifically include requirements relating to interest and penalties associated with uncertain tax treatments. The Interpretation specifically addresses the following:

- Whether an entity considers uncertain tax treatments separately;
- The assumptions an entity makes about the examination of tax treatments by taxation authorities;
- How an entity determines taxable profit (tax loss), tax bases, unused tax losses, unused tax credits and tax rates; and
- How an entity considers changes in facts and circumstances.

The Interpretation is effective for annual reporting periods beginning on or after January 1, 2019. The Interpretation had no impact on the condensed interim consolidated financial statements; therefore, the Corporation was able to implement the Interpretation retrospectively without any adjustment.

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

Basis of preparation and accounting policies (continued)

(b) Cash

Cash presented on the condensed interim consolidated statements of financial position includes cash held in trust of \$4,178,949 at September 30, 2019 (\$nil – March 31, 2019). This amount represents the cash raised through a public offering on September 27, 2019 and held in a trust account at September 30, 2019. These funds were released to the Corporation subsequent to September 30, 2019.

Comparative figures

Certain comparative figures have been reclassified to conform to the current year's presentation. Balances affected include General and administrative expenses and Research and development costs.

3. Significant judgments and estimates

The preparation of the Corporation's condensed interim consolidated financial statements requires management to make judgments, estimates, and assumptions that affect the reported amounts of revenues, expenses, assets, and liabilities, and the disclosure of contingent liabilities, at each reporting date. The outcome of these uncertainties about these assumptions and estimates could result in outcomes that require a material adjustment to the carrying amount of the asset or liability affected in future periods.

The judgments, estimates and assumptions applied in the preparation of these condensed interim consolidated financial statements are the same as those disclosed in note 3 to the 2019 annual consolidated financial statements.

4. Fair value measurement

The carrying amounts of the Corporation's cash, cash equivalents, restricted cash, trade and other receivables, investment tax credits and grants receivable, accounts payable and accrued liabilities approximate their fair values due to the short-term nature of these instruments. The line of credit is a demand instrument at a variable rate and therefore the carrying amount approximates fair value. The market interest rates that would apply to the Corporation's long-term debt is not significantly different from the effective interest rates used to amortize these debts. Therefore, the carrying amounts are comparable to fair values.

Long-term debt is measured using observable interest rates at initial recognition and is categorized within Level 2 of the fair value hierarchy. The fair value of foreign exchange forward contracts, which were entered into on July 4, 2019, represented a net liability of \$47,668 at September 30, 2019. The foreign exchange contracts at March 31, 2019 were matured in June 2019. The fair value is estimated using a market approach with forward exchange rates observable at the end of the reporting period and contract forward rates as inputs and is categorized within Level 2 of the fair value hierarchy. The hierarchy is described in note 21 of the March 31, 2019 annual financial statements.

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

5. Revenue

The geographic location of revenues, based on the location of its customers, is as follows:

	Three months ended		Six months ended	
	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
	\$	\$	\$	\$
Revenue for the period ended				
Canada	1,382,412	1,030,399	2,862,103	2,096,343
United States	748,981	545,058	1,491,108	1,015,406
Europe	652,624	99,449	1,393,016	280,091
Asia	120,120	142,796	291,244	278,190
Latin America	29,970	48,280	67,471	95,369
Australia	93,905	93,761	174,027	115,043
Other	87,907	5,052	169,103	21,507
Total revenue	3,115,919	1,964,795	6,448,072	3,901,949

The Corporation's revenue can be analyzed by type and by basis of their recognition, as follows for the three and six-month periods ended:

	Three months ended		Six months ended	
	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
	\$	\$	\$	\$
Revenue recognized at a point in time				
Hardware	42,976	120,823	150,534	241,777
Perpetual licenses	70,633	219,654	305,602	449,077
Training and professional services	130,979	21,925	250,564	69,744
Revenue recognized over time				
Subscription licenses	2,250,583	1,335,053	4,457,935	2,618,964
Maintenance and support	620,748	267,340	1,283,437	522,387
Total revenue	3,115,919	1,964,795	6,448,072	3,901,949

At each reporting date, there are no unfulfilled performance obligations extending beyond a year for which the Corporation has not collected funds or deposits.

Deferred revenue is comprised of the following:

	September 30, 2019	March 31, 2019
	\$	\$
Current portion of deferred revenue		
Subscription licenses	1,607,748	1,475,782
Maintenance and support	1,516,525	1,910,730
Non-current portion of deferred revenue		
Subscription licenses	530,310	530,569
Maintenance and support	763,943	926,863
Total deferred revenue	4,418,526	4,843,944

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

Revenue (continued)

Non-current assets by geographic area are as follows:

	September 30, 2019	March 31, 2019
	\$	\$
Canada	5,103,343	5,082,436
Netherlands	12,267,116	12,782,378
Other	11,815	14,261
Total	17,382,274	17,879,075

6. Operating segment information

The Corporation has assessed that it operates in three operating segments, those being unified communications performance analytics, SDWAN and link balancing technology, and IT operations analytics. These segments engage in business activities from which they earn revenues from subscription and perpetual software licenses, hardware, maintenance and support, and training and professional services.

For the three months ended September 30, 2019	Unified communications performance analytics	IT operations analytics	SDWAN and link balancing technology	Total
	\$	\$	\$	\$
Revenue recognized at a point in time				
Hardware	11,081	-	31,895	42,976
Perpetual licenses	25,296	-	45,337	70,633
Training and professional services	490	43,356	87,133	130,979
Revenue recognized over time				
Subscription licenses	1,740,867	509,716	-	2,250,583
Maintenance and support	19,772	344,123	256,853	620,748
Total revenue	1,797,506	897,195	421,218	3,115,919

For the three months ended September 30, 2018	Unified communications performance analytics	IT operations analytics	SDWAN and link balancing technology	Total
	\$	\$	\$	\$
Revenue recognized at a point in time				
Hardware	1,318	-	119,505	120,823
Perpetual licenses	5,046	-	214,608	219,654
Training and professional services	-	-	21,925	21,925
Revenue recognized over time				
Subscription licenses	1,335,053	-	-	1,335,053
Maintenance and support	-	-	267,340	267,340
Total revenue	1,341,417	-	623,378	1,964,795

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

Operating segment information (continued)

For the six months ended September 30, 2019	Unified communications performance analytics \$	IT operations analytics \$	SDWAN and link balancing technology \$	Total \$
Revenue recognized at a point in time				
Hardware	15,821	-	134,713	150,534
Perpetual licenses	33,017	75,883	196,702	305,602
Training and professional services	23,385	117,776	109,403	250,564
Revenue recognized over time				
Subscription licenses	3,504,225	946,203	7,507	4,457,935
Maintenance and support	38,154	709,240	536,043	1,283,437
Total revenue	3,614,602	1,849,102	984,368	6,448,072

For the six months ended September 30, 2018	Unified communications performance analytics \$	IT operations analytics \$	SDWAN and link balancing technology \$	Total \$
Revenue recognized at a point in time				
Hardware	13,182	-	228,595	241,777
Perpetual licenses	25,159	-	423,918	449,077
Training and professional services	3,325	-	66,419	69,744
Revenue recognized over time				
Subscription licenses	2,618,964	-	-	2,618,964
Maintenance and support	-	-	522,387	522,387
Total revenue	2,660,630	-	1,241,319	3,901,949

7. Additional disclosures related to the statements of loss and comprehensive loss

- i. Research and development expense for the three and six months ended September 30, 2019 is net of investment tax credits recognized of \$87,002 and \$200,139, respectively (three and six months ended September 30, 2018 - \$210,946 and \$506,946, respectively) and investment grants recognized of \$293,563 and \$636,278, respectively (three and six months ended September 30, 2018 - \$nil).

The Corporation has investment tax credits receivable of \$260,063 (March 31, 2019 - \$261,511) which are earned as a result of qualifying Scientific Research and Experimental Development expenditures, and investment grants receivable of \$399,733 as at September 30, 2019 (March 31, 2019 - \$626,438), which are earned as a result of expenditures permitted under the grant agreement. The investment tax credits and grants are recognized when the expenditures are made and their realization is reasonably assured.

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

Additional disclosures related to the statements of loss and comprehensive loss (continued)

ii. Employee benefits and share-based payments consist of the following amounts:

	Three months ended		Six months ended	
	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
	\$	\$	\$	\$
Research and development				
Short-term employee benefits	1,347,805	863,307	2,760,753	1,909,473
Share-based payments	30,853	50,427	63,873	103,269
Sales and marketing				
Short-term employee benefits	1,109,510	324,209	2,097,216	595,020
Share-based payments	13,141	19,238	31,623	39,463
General and administrative				
Short-term employee benefits	521,872	265,465	1,002,908	591,201
Share-based payments	42,011	176,155	85,520	254,169
Total staff related expense	3,065,192	1,698,801	6,041,893	3,492,595

Research and development employee costs above are presented prior to any government grants and investment tax credits.

8. Loss per share

	(3 months period)		(6 months period)	
	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
	#	#	#	#
Weighted average number of ordinary shares for basic EPS:	192,638,535	166,468,438	191,938,051	145,817,875
Effects of dilution from:				
Share options	17,688,445	6,003,964	18,057,375	5,421,621
Warrants	816,984	1,028,576	922,780	1,028,576
Weighted average number of ordinary shares adjusted for the effect of dilution:	211,143,964	173,500,978	210,918,206	152,268,072

9. Cash

	September 30, 2019	March 31, 2019
	\$	\$
Cash	4,801,078	6,620,950
Cash held in trust	4,178,949	-
Restricted cash	27,359	28,352
Total	9,007,386	6,649,302

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

10. Trade and other accounts receivable

The movements in the allowance for doubtful accounts is as follows:

Movements in the allowance for doubtful accounts	September 30, 2019	March 31, 2019
	\$	\$
Balance, beginning of period	18,784	28,784
Trade receivables written off	-	(10,000)
Additional allowance recognized	10,465	-
Balance at the end of the period	29,249	18,784

The aging analysis of trade receivables is as follows:

	Total	Neither past due nor impaired	Past due but not impaired			
			< 30 days	30-60 days	60-90 days	over 90 days
		\$	\$	\$	\$	\$
September 30, 2019	2,855,999	992,770	745,193	266,669	698,484	152,883
March 31, 2019	3,367,694	2,422,723	405,623	272,633	129,207	137,508

11. Accounts payable and accrued liabilities

	September 30, 2019	March 31, 2019
	\$	\$
Trade payables	334,572	486,938
Accrued key management compensation	191,954	246,545
Accrued professional fees	486,410	520,228
Salaries, benefits, and vacation payable	857,977	626,264
Taxes payable	248,259	177,587
Other payables	174,095	201,608
Total	2,293,267	2,259,170

12. Long-term debt

	Effective interest	September 30, 2019	March 31, 2019
		\$	\$
FedDev loan; advanced to support the commercialization of the Corporation's activities; non-interest bearing, unsecured and repayable in increasing monthly payments between January 2018 and December 2023	10%	619,459	595,216
Canada Economic Development Agency (CEDA), non-interest bearing, unsecured and repayable in 60 equal monthly payments commencing in February 2021	16%	71,337	55,308
Royal Bank of Canada, interest at 5.40%, secured by a general security agreement on the property of Martello Corp, as well as secured guarantees from Elfiq Inc. and Martello Technologies Inc., Savision B.V. and its subsidiaries, and the Corporation itself, and repayable over 36 months commencing in February 2019.	7.06%	2,288,752	2,769,546
Total long-term debt		2,979,548	3,420,070
Amounts due within one year		(1,156,944)	(1,033,775)
Long-term debt		1,822,604	2,386,295

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

13. Right-of-use assets

	\$
Balance, April 1, 2019	566,692
Foreign exchange translation	(8,874)
Depreciation for the period	(85,327)
Balance at September 30, 2019	472,491

During the period, the Corporation adopted IFRS 16, Leases which resulted in a right-of-use asset being recognized as described in note 2.

14. Equity instruments

i. Common shares

The Corporation is authorized to issue an unlimited number of common shares with no par value.

The holders of the common shares are entitled to receive non-cumulative dividends, as may be determined by the Board of Directors.

On September 27, 2019, the Corporation completed an overnight marketed equity offering of 15,333,332 common shares for gross proceeds of \$4,600,000. The offering price was \$0.30 per share. Transaction costs of \$570,045 were incurred in connection with the offering.

ii. Warrants

The Corporation has outstanding 534,861 warrants. Each warrant entitles the holder to purchase one common share for an exercise price of \$0.11. All the warrants are exercisable as at September 30, 2019. The warrants expire on the earlier of:

- (a) The date that is 24 months from an initial public offering or public listing of the Corporation;
- (b) A voluntary or involuntary liquidation, dissolution, or winding-up of the Corporation;
- (c) The amalgamation or merger of the Corporation; or
- (d) A sale of substantially all of the assets or outstanding shares of the Corporation.

iii. Share-based payments

The Corporation has a stock option plan (the "Plan") open to certain members of management, employees and consultants. Unless otherwise determined by the Board of Directors, options issued under the Plan vest over a three-year period and have expiry dates which are 5 years from issuance. The maximum number of common shares reserved for issuance of options that may be granted under the Plan is 10% of the total outstanding common shares of the Corporation, calculated on a fully-diluted basis.

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

Equity instruments (continued)

iii. Share-based payments

The following table summarizes the continuity of options issued under the Plan:

	Option exercise price	Total
	\$	#
Balance outstanding at March 31, 2019	0.11-0.13	18,519,667
Granted	0.375	90,000
Exercised	0.11-0.13	(901,331)
Forfeited	0.13-0.375	(232,000)
Balance outstanding at September 30, 2019		17,476,336

Options exercisable:

At September 30, 2019	0.11-0.13	10,467,483
At March 31, 2019	0.11-0.13	9,198,168

Grant date	Option exercise price \$	Number exercisable #	Remaining life Years
September 17, 2015	0.110	2,656,000	.97
December 3, 2015	0.110	2,688,000	1.18
January 14, 2016	0.110	171,500	1.29
July 14, 2016	0.110	40,000	1.79
October 25, 2016	0.110	53,333	2.07
January 19, 2017	0.110	42,666	2.31
April 17, 2017	0.110	53,333	2.55
July 17, 2017	0.110	53,333	2.80
December 18, 2017	0.130	1,456,000	3.22
January 10, 2018	0.130	415,997	3.28
April 3, 2018	0.130	2,837,321	3.51
January 18, 2019	0.335	-	-
February 28, 2019	0.380	-	-
September 3, 2019	0.375	-	-
Weighted average	0.142		2.15
Total		10,467,483	

At September 30, 2019, the fair value of share-based compensation to be recognized as an expense in future periods totaled \$366,257 (March 31, 2019 – \$581,023). Share-based compensation expense for the period is disclosed in note 7.

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

Equity instruments (continued)

iii. Share-based payments

In determining the amount of share-based compensation, the Corporation uses the Black-Scholes option pricing model to establish the fair value of options granted. 90,000 options were granted in the three and six months ended September 30, 2019. The fair value of options granted in the six months ended September 30, 2019 was established by applying the following assumptions:

	September 30, 2019
Stock price valuation	\$0.375
Exercise price	\$0.375
Risk-free interest rate	1.23%
Expected life in years	3.5
Expected dividend yield	0%
Volatility	82.09%
Fair value of options issued in the periods	\$0.21

Volatility was determined by using the historical volatility of the stock of comparable companies over a 3.5-year period. The expected life in years represents the period of time that options granted are expected to be outstanding. The risk-free rate is based on zero-coupon Canada government bonds with a remaining term equal to the expected life of the options.

15. Supplementary cash flow information

The net change in the operating components of working capital is as follows:

		September 30, 2019	September 30, 2018
		\$	\$
Net change in operating components of working capital:			
Trade and other accounts receivable	10	497,033	(565,157)
Investment tax credits and grants receivable	7	228,153	(88,661)
Prepaid expenses		72,404	(281,185)
Inventories		52,882	(63,766)
Accounts payable and accrued liabilities	11	66,581	401,318
Foreign exchange forward contract liability	4	41,955	14,790
Deferred revenue	5	(311,815)	(32,238)
Total		647,193	(614,899)

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

16. Related party transactions and balances

During the period the Corporation entered into the following transactions with related parties in the normal course of operations.

- i. The Corporation leases office premises from Wesley Clover International Corporation (“Wesley Clover”). Included in the condensed interim consolidated statement of financial position are \$237,805 of right-of-use assets (March 31, 2018 - \$nil) and \$280,268 of lease obligations (March 31, 2018 - \$nil), relating to the Corporation’s lease with Wesley Clover. Operating expenses under the related party lease have the minimum annual payments disclosed in note 19. For the three and six months ended September 30, 2019, the Corporation incurred \$23,415 and \$55,242 in rent expense (three and six months ended September 30, 2018 - \$43,448 and \$86,062, respectively) and \$24,600 and \$49,200 in depreciation expense (three and six months ended September 30, 2018 - \$nil). Included in accounts payable and accrued liabilities at September 30, 2019 is an account payable of \$1,158 (March 31, 2019 – \$44,626) to Wesley Clover.
- ii. Included in accounts payable and accrued liabilities are balances as at September 30, 2019 totaling \$191,954 (March 31, 2019 - \$246,545) due to key management personnel for compensation and earned vacation pay.
- iii. The remuneration of directors and key management personnel during the three-month period ended was as follows:

	Three months ended		Six months ended	
	September 30, 2019	September 30, 2018	September 30, 2019	September 30, 2018
	\$	\$	\$	\$
Salaries, wages and bonuses	428,356	341,314	854,660	715,591
Other employee benefits	10,711	6,989	16,839	9,187
Share-based compensation	34,554	98,972	69,239	177,322
Total	473,621	447,275	940,738	902,100

17. Financial risk management objectives and policies

There have been no significant changes to the nature and magnitude of risk exposures and to management's objectives and processes for managing them since the prior period.

Credit risk

Trade receivables at September 30, 2019 are presented net of an allowance for doubtful accounts of \$29,249 (March 31, 2019 - \$18,784). The Corporation’s largest customer, which is included in UC performance analytics segment reporting, accounted for revenue of \$1,697,090 and \$3,425,625 or approximately 54% and 53% of total revenue, for the three and six months ended September 30, 2019 (three and six months ended September 30, 2018 - \$1,270,731 and \$2,503,410 or 65% and 64%, respectively). At September 30, 2019 the account receivable from this customer totaled \$1,914,189 (March 31, 2019 - \$1,875,338). The Corporation maintains strict credit policies and limits in respect to counterparties.

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

Financial risk management objectives and policies (continued)

Liquidity risk

The following table summarizes the maturities of financial instruments, including interest payments, as at September 30, 2019:

	2020	2021	2022	2023 and after	Total
	\$	\$	\$	\$	\$
Accounts payable and accrued liabilities	2,293,267	-	-	-	2,293,267
Lease obligation	85,044	177,118	186,915	68,754	517,831
Long-term debt	547,732	1,225,930	1,093,041	265,800	3,132,502
Total	2,926,043	1,403,048	1,279,956	334,554	5,943,600

Foreign currency risk

For the three and six months ended September 30, 2019, 97% of revenue were in foreign currencies (September 30, 2018 – 93% of revenue). For the three and six months ended September 30, 2019, 30% and 34% of expenses were in foreign currencies, respectively.

The exposure to changes in foreign currency exchange rates is not materially different from the exposure at March 31, 2019.

18. Capital management

Management defines capital as total shareholders' equity. The Board of Directors has not established capital benchmarks or other targets. There have been no changes in the Corporation's approach to capital management during the six months ended September 30, 2019. The Corporation will continually assess the adequacy of its capital structure and capacity and make adjustments within the context of the Corporation's strategy, economic conditions, and the risk characteristics of the business.

19. Commitments

The Corporation entered into a 5-year lease for office premises in Kanata, Ontario, Canada commencing March 1, 2017 extending through to February 29, 2022. During the three months ended December 31, 2018 the lease was amended to increase the leased space, effective January 1, 2019. The lease is with a related party, as described in note 15 *Related party transactions and balances*. The Corporation is also committed to a 3-year lease for office premises in Montreal, Quebec commencing November 1, 2016 and extending through to October 31, 2019. In addition, the Corporation is committed to a 5-year lease for office premises in Amsterdam, Netherlands commencing February 1, 2018 and extending through to January 31, 2023.

Future minimum lease payments in each fiscal year are as follows:

Fiscal year ended	Martello Corp.	Elfiq Inc.	Savision B.V.	Total
	\$	\$	\$	\$
2020	123,703	15,191	54,018	192,912
2021	247,406	-	101,347	348,753
2022	226,789	-	91,983	318,772
2023	-	-	76,653	76,653
Total	597,898	15,191	324,001	937,090

Martello Technologies Group Inc.

Notes to condensed interim consolidated financial statements

For the three and six months ended September 30, 2019 and 2018

(in Canadian Dollars)

20. Events after the reporting period

Short-term investments

Subsequent to September 30, 2019 the Corporation invested \$4,000,000 into a Guaranteed Investment Certificate.