

Xebec Adsorption Inc.

Condensed Interim Consolidated Financial Statements

(Unaudited)

June 30, 2015

(expressed in Canadian dollars)

The Condensed Interim Consolidated Financial Statements which are included in this Report have not been subject to a review by the Company's External Auditors.

Xebec Adsorption Inc.

Condensed Interim Consolidated Statements of Financial Position (Unaudited)

(expressed in Canadian dollars)

	As at June 30, 2015 \$	As at December 31, 2014 \$
Assets		
Current assets		
Cash	390,550	1,008,421
Restricted cash, (Note 3)	73,080	221,930
Trade and other receivables	1,887,237	2,681,311
Inventories	1,153,251	1,669,350
Investment tax credits receivable	69,723	50,000
Other current assets	372,666	396,241
Total current assets	3,946,507	6,027,253
Non-current assets		
Property, plant and equipment (Note 4)	318,269	347,845
Intangible assets (Note 5)	843,001	919,297
Goodwill (Note 5)	142,616	142,616
Total non-current assets	1,303,886	1,409,758
Total assets	5,250,393	7,437,011
Liabilities		
Current liabilities		
Bank loan	430,000	136,437
Trade payables	2,774,782	3,491,897
Accrued liabilities	832,700	723,890
Deferred revenues	488,711	815,010
Current portion of long-term debt	16,677	50,475
Current portion of government royalty program obligation	103,940	762,825
Provisions	276,888	236,365
Total current liabilities	4,923,698	6,216,899
Non-current liabilities		
Government royalty program obligation	646,778	-
Government assistance	9,583	12,083
Deferred rent	98,940	85,748
Provisions	88,059	192,990
Total non-current liabilities	843,360	290,821
Total liabilities	5,767,058	6,507,720
Equity		
Share capital	19,732,623	19,732,623
Contributed surplus	2,487,440	2,460,146
Accumulated other comprehensive loss	(878,574)	(606,685)
Deficit	(22,130,358)	(20,914,588)
Total equity	(788,869)	671,496
Total liabilities and equity	5,250,393	7,437,011

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

Approved by the Board of Directors

(signed) Kurt Sorschak _____ Director

(signed) William Beckett _____ Director

Xebec Adsorption Inc.

Condensed Interim Consolidated Statements of Income (Loss)

For the three-month and six-month period ended June 30, 2015 and 2014

(Unaudited)

(expressed in Canadian dollars)

	2015 \$	2014 \$	2015 \$	2014 \$
Revenue	2,204,557	3,521,039	5,301,248	6,148,267
Cost of goods sold	<u>1,963,656</u>	<u>2,530,100</u>	<u>4,380,882</u>	<u>4,516,680</u>
Gross margin	<u>240,901</u>	<u>990,939</u>	<u>920,366</u>	<u>1,631,587</u>
Research and development expenses	(12,772)	(41,946)	(2,713)	84,372
Selling and administrative expenses	1,251,572	1,603,351	2,301,247	3,019,299
Foreign exchange (gain) loss	<u>136,640</u>	<u>122,393</u>	<u>(216,963)</u>	<u>68,160</u>
	<u>1,375,440</u>	<u>1,683,798</u>	<u>2,078,571</u>	<u>3,171,831</u>
Operating Loss	<u>(1,134,539)</u>	<u>(692,859)</u>	<u>(1,158,205)</u>	<u>(1,540,244)</u>
Finance income	(11,893)	(5,292)	(14,321)	(11,396)
Finance expense	<u>39,494</u>	<u>50,439</u>	<u>63,136</u>	<u>84,388</u>
Finance costs – net	<u>27,601</u>	<u>45,147</u>	<u>48,815</u>	<u>72,992</u>
Loss before income taxes	<u>(1,162,140)</u>	<u>(738,006)</u>	<u>(1,207,020)</u>	<u>(1,613,236)</u>
Income taxes	<u>-</u>	<u>-</u>	<u>8,750</u>	<u>-</u>
Net loss for the period	<u>(1,162,140)</u>	<u>(738,006)</u>	<u>(1,215,770)</u>	<u>(1,613,236)</u>
Loss attributable to:				
Shareholders of the Company	(1,162,140)	(737,368)	(1,215,770)	(1,577,186)
Non-controlling interest	<u>-</u>	<u>(638)</u>	<u>-</u>	<u>(36,050)</u>
	<u>(1,162,140)</u>	<u>(738,006)</u>	<u>(1,215,770)</u>	<u>(1,613,236)</u>
Loss per share				
Basic and diluted	<u>(0.03)</u>	<u>(0.02)</u>	<u>(0.03)</u>	<u>(0.04)</u>

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

Xebec Adsorption Inc.

Condensed Interim Consolidated Statements of Comprehensive Income (Loss)

For the three-month and six-month period ended June 30, 2015 and 2014

(Unaudited)

(expressed in Canadian dollars)

	2015 \$	2014 \$	2015 \$	2014 \$
Net loss for the period	(1,162,140)	(738,006)	(1,215,770)	(1,613,236)
Other comprehensive income (loss)				
Cumulative translation adjustment	<u>51,423</u>	<u>160,288</u>	<u>(257,480)</u>	<u>132,405</u>
Comprehensive loss for the period	<u>(1,110,717)</u>	<u>(577,718)</u>	<u>(1,473,250)</u>	<u>(1,480,831)</u>
Attributable to:				
Shareholders of the Company	(1,111,203)	(570,809)	(1,487,659)	(1,449,879)
Non-controlling interest	<u>486</u>	<u>(6,909)</u>	<u>14,409</u>	<u>(30,952)</u>
	<u>(1,110,717)</u>	<u>(577,718)</u>	<u>(1,473,250)</u>	<u>(1,480,831)</u>

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

Xebec Adsorption Inc.

Condensed Interim Consolidated Statements of Changes in Equity (Deficiency)

(Unaudited)

(expressed in Canadian dollars)

	Number		Amount						
	Common shares	Warrants	Share capital – Common shares and warrants \$	Contributed surplus \$	Accumulated other comprehensive income (loss) \$	Deficit \$	Equity attributable to the Company \$	Non-controlling interest \$	Total \$
Balance – January 1, 2014	39,363,867	10,091,886	19,732,623	2,388,063	(313,486)	(20,131,974)	1,675,226	283,762	1,958,988
Net loss for the period	-	-	-	-	-	(1,577,186)	(1,577,186)	(36,050)	(1,613,236)
Other comprehensive income	-	-	-	-	127,307	-	127,307	5,098	132,405
Comprehensive income (loss) for the period	-	-	-	-	127,307	(1,577,186)	(1,449,879)	(30,952)	(1,480,831)
Share-based compensation	-	-	-	19,358	-	-	19,358	-	19,358
Balance – June 30, 2014	39,363,867	10,091,886	19,732,623	2,407,421	(186,179)	(21,709,160)	244,705	252,810	497,515
Balance – January 1, 2015	39,363,867	10,091,886	19,732,623	2,460,146	(606,685)	(20,914,588)	671,496	257,795	929,291
Net loss for the period	-	-	-	-	-	(1,215,770)	(1,215,770)	-	(1,215,770)
Other comprehensive income (loss)	-	-	-	-	(271,889)	-	(271,889)	14,409	(257,480)
Comprehensive income (loss) for the period	-	-	-	-	(271,889)	(1,215,770)	(1,487,659)	14,409	(1,473,250)
Share-based compensation	-	-	-	27,294	-	-	27,294	-	27,294
Balance – June 30, 2015	39,363,867	10,091,886	19,732,623	2,487,440	(878,574)	(22,130,358)	(788,869)	272,204	(516,665)

Accumulated other comprehensive income relates solely to cumulative translation adjustments.

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

Xebec Adsorption Inc.

Condensed Interim Consolidated Statements of Cash Flows

For the three-month and six-month period ended June 30, 2015 and 2014

(Unaudited)

(expressed in Canadian dollars)

	2015	2014	2015	2014
	\$	\$	\$	\$
Cash flows from				
Operating activities				
Net loss for the period	(1,162,140)	(738,006)	(1,215,770)	(1,613,236)
Items not affecting cash				
Amortization of property, plant and equipment	27,842	22,328	56,133	42,761
Amortization of intangible assets	38,474	42,563	76,954	84,929
Gain on debt forgiveness	(22,026)	(2,621)	(190,092)	(12,624)
Government assistance	(1,250)	(1,250)	(2,500)	(2,500)
Accretion and revaluation of government royalty program obligation	(4,078)	9,077	2,353	18,615
Stock-based compensation expense	13,688	19,358	27,294	19,358
Deferred rent	6,596	6,596	13,192	13,192
	<u>(1,102,894)</u>	<u>(641,955)</u>	<u>(1,232,436)</u>	<u>(1,449,505)</u>
Changes in non-cash working capital components related to operations (note 9)	681,112	(1,267,343)	505,105	24,143
	<u>(421,782)</u>	<u>(1,909,298)</u>	<u>(727,331)</u>	<u>(1,425,362)</u>
Investing activities				
Acquisition of property, plant and equipment	(8,625)	(38,528)	(21,894)	(54,594)
Acquisition of intangible assets	-	(2,651)	-	(2,651)
	<u>(8,625)</u>	<u>(41,179)</u>	<u>(21,894)</u>	<u>242,755</u>
Financing activities				
Restricted cash	-	-	145,386	(145,386)
Increase (decrease) of bank loan	430,000	(244,367)	293,563	(244,367)
Repayment of long-term debt	(10,663)	(10,527)	(33,798)	(33,522)
Repayment of government royalty program obligation	(14,460)	(24,500)	(14,460)	(98,000)
	<u>404,877</u>	<u>(279,394)</u>	<u>390,691</u>	<u>(521,275)</u>
Effect of exchange rate changes on cash	52,568	167,268	(259,337)	138,651
Increase (decrease) in cash and cash equivalent during the period	27,038	(2,062,603)	(617,871)	(1,565,231)
Cash and cash equivalent – Beginning of period	363,512	3,332,423	1,008,421	2,835,051
Cash and cash equivalent – End of period	<u>390,550</u>	<u>1,269,820</u>	<u>390,550</u>	<u>1,269,820</u>
Additional information				
Interest paid	30,297	41,362	47,508	65,773

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

Xebec Adsorption Inc.

Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

June 30, 2015

(expressed in Canadian dollars)

1 Nature of business

a) Nature of business

Xebec Adsorption Inc. (“Xebec” or the “Company”) is a global provider which specializes in the design and manufacture of cost-effective, environmentally responsible, purification, separation, dehydration, and filtration equipment for gases and compressed air. Xebec’s main product lines are: Biogas Plants for the purification of biogas from agricultural digesters, landfill sites and waste water treatment plants, Natural Gas Dryers for NGV refuelling stations, Associated Gas Purification Systems which enable diesel displacement on drilling sites, and Hydrogen Purification Systems for fuel cell and industrial applications. The Company is incorporated and domiciled in Canada and is listed on the TSX Venture Exchange under the symbol XBC-V. The address of its registered office is 730 Industriel Boulevard, Blainville, Quebec, Canada.

b) Liquidity risk

The Company has realized an operating loss of \$1,158,205, had cash outflows from operations of \$727,331 for the period ended June 30, 2014 and finished the period with cash and cash equivalents amounting to \$390,550, working capital deficit of \$977,191 and had access to credit facilities totalling \$500,000 of which \$430,000 has been used. During the year, management undertook various initiatives and developed a plan to manage its operating and liquidity risks in light of prevailing economic conditions. Management is also currently seeking alternative financings for its operations. The Company has prepared a revised budget and forecast for 2015 for which management believes the assumptions are reasonable. Achieving budgeted results is dependent on improving the volume of revenues in Canada, United States and China, delivering on sales and contracts schedules, meeting expected overall operating margin levels and controlling general and administrative costs. Management expects to meet its budget and to have enough liquidity to fund operations to at least beyond December 31, 2015.

The Company is thus faced with uncertainties that may have an impact on future operating results and liquidity. These uncertainties include reduced spending in biogas projects reflecting the weakness of the market, fluctuations in foreign currency rates and achieving the Company’s business plan goals as mentioned in the previous paragraph, which includes the development of a new business segment. While management believes it has developed planned courses of action to mitigate operating and liquidity risks, there is no assurance that management will be able to achieve its business plan and maintain the necessary liquidity level, including accessing liquidities from China, if events or conditions develop that are not consistent with management’s expectations, key budget assumptions for 2015 and planned courses of action. Therefore, the Company may require additional external funding and there is no assurance that it would be successful. It is possible that future changes in capital markets conditions could result in such funding not being available when required or at acceptable costs. The Company is unable to predict the possible effects, if any, of such uncertainties and the potential adjustments to the carrying values of assets and liabilities that could be needed should the Company have insufficient liquidity. Such adjustments could be material.

Xebec Adsorption Inc.

Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

June 30, 2015

(expressed in Canadian dollars)

2 Basis of preparation

These condensed consolidated interim financial statements, have been prepared in accordance with International Financial Reporting Standards (“IFRS”) applicable to the preparation of interim financial statement, including IAS 34 Interim Financial Reporting. The condensed consolidated interim financial statements do not include all of the information required for annual financial statements, and should be read in conjunction with the annual consolidated financial statements for the year ended December 31, 2014, as they follow the same accounting policies and methods of application, unless otherwise indicated. These consolidated interim financial statements were approved by the Board of Directors on August 31, 2015.

3 Restricted cash

Restricted cash consist in a cash equivalent to \$73,080 retained by the liquidator of the South East Asia subsidiary. The guarantee investment certificate equivalent to \$152,827 and pledge against a loan to the China subsidiary existing at the end of the fiscal year 2014 was refunded during the first current quarter.

Xebec Adsorption Inc.

Notes to Condensed Interim Consolidated Financial Statements (Unaudited)

June 30, 2015

(expressed in Canadian dollars)

4 Property, plant and equipment

	Machinery and equipment	Office furniture and equipment	Computers	Moulds	Vehicles	Total
Cost						
Balance at December 31, 2014	484,754	143,672	232,642	163,431	35,984	1,060,483
Additions	-	333	21,561	-	-	21,894
Effect of movements in exchange rates	8,918	6,658	9,385	7,375	-	32,336
Balance at June 30, 2015	493,672	150,663	263,588	170,806	35,984	1,114,713
Accumulated amortization						
Balance at December 31, 2014	282,517	101,882	206,130	89,724	32,385	712,638
Amortization	22,830	6,954	12,729	10,021	3,599	56,133
Effect of movements in exchange rates	6,614	6,028	8,550	6,481	-	27,673
Balance at June 30, 2015	311,961	114,864	227,409	106,226	35,984	796,444
Carrying Amount						
At December 31, 2014	202,237	41,790	26,512	73,707	3,599	347,845
At June 30, 2015	181,711	35,799	36,179	64,580	-	318,269

Xebec Adsorption Inc.

Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

June 30, 2015

(expressed in Canadian dollars)

5 Intangible assets

	Customer relations \$	Other Software \$	Internally generated Development costs \$	Total intangible assets \$	Goodwill \$
Cost					
Balance at December 31, 2014	1,900,000	270,894	298,485	2,469,379	142,616
Effect of movements in exchange rates	-	8,426	-	8,426	-
Balance at June 30, 2015	1,900,000	279,320	298,485	2,477,805	142,616
Accumulated amortization					
Balance at December 31, 2014	1,266,666	254,376	29,040	1,550,082	-
Amortization of the period	39,584	7,521	29,849	76,954	-
Effect of movements in exchange rates	-	7,768	-	7,768	-
Balance at June 30, 2015	1,306,250	269,665	58,889	1,634,804	-
Carrying Amount					
At December 31, 2014	633,334	16,518	269,445	919,297	142,616
At June 30, 2015	593,750	9,655	239,596	843,001	142,616

For the six-month period ended June 30, amortization of \$76,954 (2014 - \$84,929) is included in the consolidated statement of loss: \$5,201 (2014 - \$1,536) in 'cost of goods sold' and \$71,753 (2014 - \$83,393) in 'selling and administrative expenses'.

For the three-month period ended June 30, amortization of \$38,474 (2014 - \$42,563) is included in the consolidated statement of loss: \$2,598 (2014 - \$867) in 'cost of goods sold' and \$35,876 (2014 - \$41,696) in 'selling and administrative expenses'.

Xebec Adsorption Inc.

Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

June 30, 2015

(expressed in Canadian dollars)

6 Share capital

Earnings (loss) per share

i) Basic

Basic loss per share is calculated by dividing the net income attributable to owners of the parent by the weighted average number of common shares in issue during the year.

	<u>For the three-month period ended June 30,</u>		<u>For the six-month period ended June 30,</u>	
	<u>2015</u>	<u>2014</u>	<u>2015</u>	<u>2014</u>
	<u>\$</u>	<u>\$</u>	<u>\$</u>	<u>\$</u>
Net income (loss) attributable to owners of the parent	(1,162,140)	(737,368)	(1,215,770)	(1,577,186)
Weighted average number of common shares in issue	<u>39,363,867</u>	<u>39,363,867</u>	<u>39,363,867</u>	<u>39,363,867</u>
	<u>(0.03)</u>	<u>(0.02)</u>	<u>(0.03)</u>	<u>(0.04)</u>

ii) Diluted

Diluted earnings per share is calculated by adjusting the weighted average number of common shares outstanding to assume conversion of all dilutive potential common shares. The Company has two categories of dilutive potential common shares: warrants and stock options. For both, a calculation is performed to determine the number of shares that could have been acquired at fair value (determined as the average market share price of the Company's outstanding shares for the period), based on the monetary value of the subscription rights attached to the warrants and stock options. The number of shares calculated below is compared with the number of shares that would have been issued assuming exercise of the warrants and stock options. For the periods ended June 30, 2015 and 2014, the diluted net loss per share was the same as the basic net loss per share, since the effect of assumed exercise of share options and warrants to purchase common shares was anti-dilutive.

Xebec Adsorption Inc.

Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

June 30, 2015

(expressed in Canadian dollars)

7 Expenses by nature

	For the three-month period ended June 30,		For the six-month period ended June 30,	
	2015 \$	2014 \$	2015 \$	2014 \$
Employee salaries and benefits	1,584,110	1,592,269	2,908,920	3,004,645
Material	1,023,413	1,608,737	2,465,259	2,818,007
Rent and repairs and maintenance	171,215	156,511	348,712	312,156
Travel expenses	143,591	231,310	304,190	455,015
Professional fees	98,792	131,370	276,246	269,881
Amortization	66,315	64,891	133,086	127,691
Office expense	56,591	130,321	122,473	242,115
Subcontract cost	43,795	219,763	97,522	271,489
Stock-based compensation	13,688	19,359	27,294	19,359
Commission	-	47,052	-	47,052
Other	13,718	(68,132)	(1,573)	(31,431)
	<u>3,215,228</u>	<u>4,133,451</u>	<u>6,682,129</u>	<u>7,535,979</u>

8 Finance expenses

	For the three-month period ended June 30,		For the six-month period ended June 30,	
	2015 \$	2014 \$	2015 \$	2014 \$
Interest charges	23,621	29,545	30,926	45,265
Interest and bank charges	6,638	11,657	16,490	20,157
Accretion and revaluation of government royalty program obligation	9,197	9,077	15,628	18,615
Interest on long-term debt	38	160	92	351
	<u>39,494</u>	<u>50,439</u>	<u>63,136</u>	<u>84,388</u>

Xebec Adsorption Inc.

Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

June 30, 2015

(expressed in Canadian dollars)

9 Supplemental Cash flow information

Net change in non-cash working capital balances related to operations consists of the following:

	For the three-month period ended June 30,		For the six-month period ended June 30,	
	2015 \$	2014 \$	2015 \$	2014 \$
Decrease (increase) in assets:				
Trade and other receivables	1,114,278	(200,255)	794,074	735,756
Inventories	344,706	182,090	516,099	185,449
Investment tax credits receivable	(19,723)	(105,000)	(19,723)	(17,240)
Other current assets	34,210	(180,677)	23,575	(260,123)
Increase (decrease) in liabilities:				
Trade payables	(464,029)	194,846	(527,023)	(54,729)
Accrued liabilities	(38,700)	(180,855)	108,810	(184,384)
Deferred revenues	(213,720)	(868,132)	(326,299)	(203,690)
Other operating liabilities	(75,910)	(109,360)	(64,408)	(176,896)
	<u>681,112</u>	<u>(1,267,343)</u>	<u>505,105</u>	<u>24,143</u>

10 Related party transactions

The following table presents a summary of the related party transactions during the period:

	For the three-month period ended June 30,		For the six-month period ended June 30,	
	2015 \$	2014 \$	2015 \$	2014 \$
Marketing and professional services expenses paid to companies controlled by members of the immediate family of an officer	27,610	28,745	54,590	55,345
Sales to entities controlled by a subsidiary manager	<u>205,005</u>	<u>150,404</u>	<u>843,106</u>	<u>853,043</u>

These transactions are measured at the exchange amount, which is the amount of consideration established and agreed to by the related parties.

Xebec Adsorption Inc.

Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

June 30, 2015

(expressed in Canadian dollars)

11 Segmented information

The Company has only one segment and specializes in the design and manufacture of filtration, purification, separation and dehydration equipment for gases and compressed air. The Company has four product lines and provides related engineering services.

Revenue summarized by country, as determined by location of the customers, is as follows:

	For the three-month period ended June 30,		For the six-month period ended June 30,	
	2015	2014	2015	2014
	\$	\$	\$	\$
Revenue				
United States	1,030,673	1,409,039	1,981,076	2,150,553
Canada	435,494	439,751	1,215,247	1,013,182
Singapore	204,984	150,404	842,478	853,043
China	288,908	685,999	745,525	989,020
Other	244,498	835,846	516,922	1,142,469
	<u>2,204,557</u>	<u>3,521,039</u>	<u>5,301,248</u>	<u>6,148,267</u>

Xebec Adsorption Inc.

Notes to Condensed Interim Consolidated Financial Statements

(Unaudited)

June 30, 2015

(expressed in Canadian dollars)

Revenue summarized by product line is as follows:

Product line	For the three-month period ended June 30,		For the six-month period ended June 30,	
	2015	2014	2015	2014
	\$	\$	\$	\$
Natural gas dryers	973,689	1,169,076	2,607,431	2,529,343
Compressed gas filtration	874,319	927,350	1,879,468	1,882,480
Gas purification	301,600	783,826	637,581	1,028,332
Associated Gas	-	640,787	68,850	708,112
Air dryers	54,949	-	107,918	-
	<u>2,204,557</u>	<u>3,521,039</u>	<u>5,301,248</u>	<u>6,148,267</u>

Major customers representing 10% or more of total sales include:

	For the three-month period ended June 30,		For the six-month period ended June 30,	
	2015	2014	2015	2014
	\$	\$	\$	\$
Customer A	255,369	-	843,106	-
Customer B	-	149,540	-	708,112
	<u>255,369</u>	<u>149,540</u>	<u>843,106</u>	<u>708,112</u>

The location of the Company's non-current assets by geographic region is as follows:

	June 30, 2015	December 31, 2014
	\$	\$
Non-current assets		
Canada	1,236,506	1,337,833
Asia	62,536	66,826
United States	4,844	5,099
	<u>1,303,886</u>	<u>1,409,758</u>