Covalon Technologies Ltd.

Management’s Discussion and Analysis of Financial
Condition and Results of Operations

March 31, 2015

MANAGEMENT’S DISCUSSION & ANALYSIS
For the six months ended March 31, 2015

May 28, 2015

The following discussion of Covalon Technologies Ltd.’s (“Covalon” or the “Company”) financial condition and results of operations should be read in conjunction with our audited consolidated financial statements for the year ended September 30, 2014 and with our unaudited condensed consolidated interim financial statements, with related notes, for the six month period ended March 31, 2015. Additional information on Covalon Technologies Ltd. can be obtained on SEDAR at www.sedar.com, as well as the Company’s website at www.covalon.com. Unless otherwise indicated, all references to the terms “we”, “us”, “our”, “Covalon” and “Company” refer to Covalon Technologies Ltd. and its subsidiaries.

In this MD&A, financial information for the six month periods March 31, 2015 and 2014 is based on the unaudited condensed consolidated interim financial statements of the Company, which were prepared in accordance with International Financial Reporting Standards (“IFRS”), and are presented in Canadian dollars unless otherwise specified. In accordance with its terms of reference, the Audit Committee of the Company’s Board of Directors reviews the contents of the MD&A and recommends its approval to the Board of Directors. The Board of Directors approved this MD&A on May 28, 2015. Disclosure contained in this document is current to that date, unless otherwise noted.

Management's Responsibility for Financial Reporting

The Consolidated Financial Statements and MD&A have been prepared by management, who, when necessary, have made informed judgments and estimates of the outcome of events and transactions with due consideration given to materiality. Management acknowledges its responsibility for the fairness, integrity, and objectivity of all information provided in the consolidated financial statements and in the MD&A thereof. As a means of fulfilling its responsibility, management relies on the Company's system of internal controls. This system has been established to ensure, within reasonable limits, that assets are safeguarded, transactions are properly recorded and are executed with management's authorization, and that the accounting records provide a solid foundation from which to prepare the Consolidated Financial Statements and the MD&A. The Board of Directors carries out its responsibility for the consolidated financial statements principally through its Audit Committee. This committee meets periodically, reviews the scope of the external audit, the adequacy of the systems of internal control and the appropriateness of financial reporting, and then makes its recommendations to the Board of Directors. Based on those recommendations, the Board approves the Consolidated Financial Statements and the MD&A.

Non-IFRS Financial Measures

In this MD&A, we refer to terms that are not specifically defined under IFRS. These non-IFRS measures may not be comparable to similar measures presented by other companies.

Forward-looking Statements

This MD&A contains forward-looking statements which reflect the Company's current expectations regarding future events. The forward-looking statements are often, but not always, identified by the use of words such as "seek", "anticipate", "plan", "estimate", "expect", "intend" and statements that an event or result "may", "will", "should", "could", or "might" occur or be achieved and other similar expressions. These forward-looking statements involve risk and uncertainties, including the difficulty in predicting product approvals, acceptance of and demands for new products, the impact of the products and pricing strategies of competitors, delays in developing and launching new products, the regulatory environment, fluctuations in operating results, and other risks, any of which could cause results, performance, or achievements to differ materially from the results discussed or implied in the forward-looking statements. Many risks are inherent in the industry; others are more specific to the Company. Investors should consult the "Risks & Uncertainties" section of this MD&A as well as the Company's ongoing quarterly filings for additional information on risks and uncertainties relating to these forward-looking statements. Investors should not place undue reliance on any forward-looking statements. Management assumes no obligation to update or alter any forward-looking statements whether as a result of new information, further events, or otherwise.

Nature of Our Business

Covalon Technologies Ltd. is a researcher, developer, manufacturer, and marketer of patent-protected medical products that improve patient outcomes and save lives in the areas of advanced wound care and infection management. Our offices and laboratories are located in Mississauga, Ontario, Canada.

Covalon leverages its patented medical technology platforms and expertise in two ways; (i) we develop products that we sell under Covalon's name; and (ii) we develop and commercialize medical products for other medical companies under development and license contracts.

The majority of Covalon-branded products are sold through independent distributors to various health care providers such as hospitals, wound care centers, burn centers, extended/alternate care facilities, acute care facilities, home health care agencies, and physicians' offices. Our products require regulatory clearances and are sold on a prescription basis in the United States, Canada, and a number of international countries.

We also license our technologies and products to large medical device companies as well as work with niche start-ups to create novel technology to advance their product offerings in various medical device markets. Covalon has worked with over twenty medical companies including leaders in vascular access devices, I.V. infusion, orthopedics, device and patient care distributors, wound care product companies, specialty medical device manufacturers and major contract manufacturers.

Covalon currently has three proprietary platform technologies that have the potential to be developed into dozens of medical devices: (i) Collagen matrix; (ii) Antimicrobial silicone adhesive; and (iii) Medical coating technology. These platform technologies are protected by patents, patent applications and patents pending, patented and proprietary manufacturing processes, trade secrets, brands, trademarks, and trade names.

Our Products

We have obtained regulatory clearance on approximately 17 medical devices, many of which are derived from our platform technologies and include the following products:

ColActive and **ColActive Plus**: Collagen Matrix Dressings. The ColActive family of products is based on our patented collagen matrix and is used to treat chronic and infected wounds including diabetic ulcers (including diabetic foot ulcers), pressure ulcers, venous ulcers (including venous leg ulcers), donor and graft sites, traumatic wounds healing by secondary intention, dehisced surgical wounds, and first and second degree burns. These dressings begin from a collagen base, which is generally biocompatible with the human body, and enable the release of beneficial materials, such as antimicrobials, into the wound site and/or enhance the removal of undesirable materials, such as wound exudate from the wound. Covalon's patented manufacturing process for ColActive has certain clinical advantages over other dressings, such as open binding sites for destructive enzymes, effective antimicrobial activity, and exudate management properties that help chronic wounds heal.

IV Clear: Antimicrobial Clear Silicone Adhesive Dressings with Chlorhexidine and Silver. IV Clear is intended to cover and protect insertion sites and to secure intravenous devices to skin, including IV catheters, central venous lines, peripherally inserted central catheters (PICCs), hemodialysis catheters, other intravascular catheters, and percutaneous devices. IV Clear is the only antimicrobial clear silicone vascular access dressing that combines silver and chlorhexidine to provide broad-spectrum antimicrobial activity for 7 days. IV Clear meets the current FDA "greater than 4 log reduction" standard for an antimicrobial claim against bacteria, and yeast, most commonly associated with healthcare acquired infections. The soft silicone adhesive provides greater patient comfort, does not macerate or damage the skin, and was shown to be up to 10 times less painful upon removal when compared to acrylic adhesives.

SurgiClear: Antimicrobial Clear Silicone Adhesive Dressings with Chlorhexidine and Silver. Covalon developed SurgiClear based on the same technology as IV Clear to address the shortcomings of other surgical site cover dressings in the market. SurgiClear is intended to cover and protect wound sites against external contamination, including post-operative, debrided or partial thickness wounds such as skin graft donor sites, abrasions lacerations, skin tears, and first and second degree burns. SurgiClear can be used to cover and protect wound closure devices (i.e. sutures, staples, clips), orthopedic pins, fixtures and wires, as well as drains. SurgiClear may also be used to cover and secure primary dressings. SurgiClear inhibits microbial colonization and suppresses microbial regrowth under the dressing. SurgiClear is gentle on the skin for maximum patient comfort. Its removal will not tear or damage fragile skin, and the novel adhesive film provides excellent tissue contact and infection management. The use of silicone materials on wounds is known to help reduce excessive scarring during the healing process.

SilverCoat: Antimicrobial Silicone Foley Catheters: Covalon's SilverCoat urinary Foley catheter is coated with Covalon's patented antimicrobial silver polymer coating which is lubricious and elutes silver from the surface to kill bacteria and yeast over a seven day period. SilverCoat Foley's are used via prescription in hospitals, extended care facilities, acute care facilities, and home health care situations to catheterize patients for extended periods of time. Among urinary tract infections (UTI) acquired in the hospital, approximately 75% are associated with a urinary catheter, which is a tube inserted into the bladder through the urethra to drain urine. Between 15-25% of hospitalized patients receive urinary catheters during their hospital stay. The most important risk factor for developing a catheter-associated UTI (CAUTI) is prolonged use of the urinary catheter, according to the United States Center for Disease Control.

Our Services

We engage our service customers by developing novel medical devices for clients, as well as licensing our technology and products to medical companies on a global basis. Some medical companies and distributors license our technologies for incorporating into their own product offerings, which they sell to healthcare providers under their own brand names. Referred to by the industry as an OEM sales model (original equipment manufacturer), this approach assigns the major cost of selling to our customers, who are able to penetrate the market with a large sales force in geographical locations where Covalon does not have staff or offices. Our revenue streams are typically generated from product sales, services, technology licensing fees, and royalties from the sale or commercialization of products.

Analysis of Operating and Financial Results

Covalon continues to transition from a research lab to a successful market focused technology business with a broad platform of patented technologies and products. The Company distributes products under the Covalon brand name as well as utilizing an OEM business model to realize value in the marketplace.

The Company has set up distribution relationships with a number of companies in North America, the Middle East, Asia, and is in the process of expanding into other important global markets. The Company's attendance at selected medical products trade shows has led to increased awareness of the Covalon brand and end user interest in its products.

Covalon continues to also utilize an OEM revenue model based on selling our technologies to large medical companies. OEM models do not produce consistent revenues on a quarterly basis. Consequently, any one quarter's results are not particularly indicative of the Company's prospects. Most OEM sales models involve a long sales cycle – from initial discussion, product evaluation, regulatory filings, contract negotiation, performance of services, and then to market roll-out. This process generally takes twelve to eighteen months although there are exceptions for both shorter and longer times for the completion of a project. The start and finish of projects is dependent on many factors, many of which are outside the control of Covalon.

On November 4, 2013, Covalon licensed its antimicrobial silicone adhesive technology to Molnlycke Heath Care ("Molnlycke"). Under the license agreement, Covalon granted Molnlycke the exclusive rights to exploit Covalon's patent-pending antimicrobial silicone adhesive technology in the field of single-use surgical, wound care, and vascular access medical dressings. Covalon received $3.5 million USD in upfront fees and receives additional ongoing minimum royalties, milestone payments, and other fees. Covalon retained the rights to exploit the antimicrobial silicone adhesive technology in other fields and commercialize new life-saving products in its development pipeline while continuing to distribute its other products. The parties simultaneously signed a supply and distribution agreement under which Covalon provides to Molnlycke its United States Food and Drug Administration cleared products, SurgiClear™ and IV Clear™, for distribution under the Molnlycke brand.

Financial Highlights for the three months ended March 31, 2015

- Total revenue for the three months ended March 31, 2015 was $2,180,276, compared to $2,041,591 for the same period of the prior year.
- Revenue from advanced wound care product sales for the three month period ended March 31, 2015 increased to $1,742,672 compared to $1,400,065 for the same period last year. This increase is largely attributable to the sale of advanced wound care products to a new distribution partner in the Middle East.
- Revenue from specialized medical device coatings for the three month period ended March 31, 2015 was $312,519 compared to $462,000 for the same period of the prior year.
- During the quarter, the Company began selling antimicrobial urinary catheters under the Covalon brand name SilverCoat. Revenue from specialized medical device coatings fluctuates from quarter to quarter depending on the timing of milestone payments and deliverables derived from the sale of catheter coating equipment, design specifications, quality control system documentation, related development projects, and the sale of coated medical devices.
- Licensing fees for the three months ended March 31, 2015 were $125,085 compared to $179,526 for the three months ended March 31, 2014.
- Gross margin on product sales and services (excluding licensing fees) for the quarter ended March 31, 2015 increased to 65% compared to 53% for the same period of the prior year. The increase in margin is attributable to higher margins on the sale of wound care products and device coating technology.
- Operating expenses for the three months ended March 31, 2015 increased $223,173 or 24% to $1,159,320 compared to $936,147 for the prior year. During the quarter the Company incurred approximately $145,000 in additional legal fees related to patent applications for new products and litigation. During the quarter the Company also incurred additional costs related to the opening of a second facility in Mississauga, Ontario to allow for expanded commercialization of new advanced wound care, and specialized medical device products.
- Net income for the three months ended March 31, 2015 was $264,340 or $0.03 per share compared to $431,211 or $0.05 for the three months ended March 31, 2014.

Financial Highlights for the six months ended March 31, 2015

- Total revenue for the six months ended March 31, 2015 was $3,516,961, compared to $6,563,792 for the same period of the prior year. Revenue and profitability for the first six months of last year included an initial payment of US$3,500,000 by Mölnlycke Health Care AB related to the licensing of two of Covalon's products, IV Clear and SurgiClear, which was announced on November 4, 2013.
- Revenue from advanced wound care product sales for the six month period ended March 31, 2015 increased 18% to $2,509,763 compared to $2,133,655 for the same period last year. This increase reflects the Company's continued penetration into new and existing markets in North America and worldwide.
- Revenue from specialized medical device coatings for the six month period ended March 31, 2015 was $767,126 compared to $462,000 for the same period of the prior year. Consistent with the Company's transition to a royalty-based model of outsourced production of medical coating devices,

Covalon provides designs and equipment to enable third party manufactures to produce specialized coating products that meet Covalon's stringent quality standards.

- Licensing fees for the six months ended March 31, 2015 were $240,072 compared to $3,968,137 for the six months ended March 31, 2014. Results for the prior year reflect revenues related to licensing of the Company's IV Clear and SurgiClear products to Molnlycke under the license agreement announced November 4, 2013.
- Gross margin on product sales and services (excluding licensing fees) for the six month period ended March 31, 2015 increased to 64% compared to 60% for the same period of the prior year.
- Operating expenses for the six months ended March 31, 2015 increased $292,424 or 15% to $2,221,983 compared to $1,929,558 for the prior year. Improved financial resources have allowed the company to add additional operational staff, recommence compensation the Company's board of directors, and funding the development of new products.
- Net income for the six months ended March 31, 2015 was $34,636 or $0.00 per share compared to net income of $3,551,630 or $0.38 per share for the six months ended March 31, 2014.

Consolidated Statement of Comprehensive Loss

	Three months ended March 31, 2015	**2014**	**Six months ended March 31, 2015**	**2014**
Revenue				
Product and Services				
Advanced wound care	**$1,742,672**	$1,400,065	**$2,509,763**	$2,133,655
Specialized medical device coatings	**312,519**	462,000	**767,126**	462,000
Licensing and royalty fees	**125,085**	**179,526**	**240,072**	3,968,137
Total Revenue	**2,180,276**	**2,041,591**	**3,516,961**	6,563,792
Cost of sales	**715,942**	657,304	**1,190,690**	1,042,293
Gross Profit	**1,464,334**	1,384,287	**2,326,271**	5,521,499
Operating Expenses				
Operations	**150,114**	152,954	**319,280**	279,316
Research and development activities	**125,622**	108,748	**295,209**	224,720
Sales and marketing	**222,406**	247,410	**454,986**	438,352
General and administrative	**661,178**	427,034	**1,152,508**	987,170
	1,159,320	936,146	**2,221,983**	1,929,558
Earnings before undernoted	**305,014**	448,141	**104,288**	3,591,941
Interest (expense)	**(40,674)**	(16,930)	**(69,925)**	(40,311)
Net earnings (loss) and comprehensive income (loss) for the period	**$264,340**	$431,211	**$34,363**	$3,551,630
Basic (loss) earnings per share (Note 22)	**$ 0.03**	$ 0.05	**$ 0.00**	$ 0.38
Diluted earnings (loss) per share (Note 22)	**$ 0.01**	$ 0.02	**$ 0.00**	$ 0.19

Product and Service Revenue, Licensing and Gross Profit

Total product and service revenue, excluding licensing fees increased $681,234 or 26% to $3,276,889 for the six months ended March 31, 2015 compared to $2,595,655 for the same period last year. Increased sales of wound care products accounted for $376,108 of the increase and the remaining $305,126 was related to revenue derived from specialized device coatings products and services. Licensing revenue was $240,072 for the six months ended March 31, 2015 compared to $3,968,137 for the same period last year. Licensing revenue for the prior year was mainly attributable to the licensing of the Company’s IV Clear and SurgiClear products to Molnlycke under the license agreement announced November 4, 2013.

Product and services revenue is comprised of: (i) Advanced wound care product sales, which include ColActive Plus, IV Clear, SurgiClear and other wound care products sold under Covalon brands or sold by third parties under private label brands; and (ii) Specialized medical device coatings, which include coating services revenue and royalties, equipment sales, development services contract fees, and consulting services fees.

Quarter-to-quarter revenue continues to be inherently unpredictable due to our OEM business model. Revenue fluctuates from quarter to quarter depending on the composition of contractual arrangements entered into in each quarter, the timing of product shipments, and completion of services in any period.

The Company utilizes an outsourced manufacturing model for the production of both the wound care products and specialized medical device coated products. This allows the Company to control operating expenses, maintain margins and focus internal resources on high margin advanced wound care product development and sales.

Gross margin on product sales and services, which does not include licensing fees, fluctuates as a result of the mix of products sold in any given quarter, or year, by product type and geography. Gross margin was 64% for the six months ended March 31, 2015 compared to 60% in the prior year. Gross margin is highly influenced by: product mix between advanced wound care and specialized medical device coatings; the mix of silicone-based wound dressings and collagen dressings sold in the periods; the amount of royalties recognized in the period; and the amount of funded coating services included in revenue and costs.

The Company disclosed two product segments in its consolidated financial statements: Advanced Wound Care and Specialized Medical Device Coatings. These segments have been identified based on the underlying technology of the product.

Interest Expense

Net interest expense was $69,925 for the six months ended March 31, 2015 compared to $40,311 for the same period of the previous year. Net interest expense includes interest earned on investments, and interest expense associated with the face value of convertible debentures and the accretion of interest on convertible debentures to bring the interest expense up to an estimated fair market value. All investments are made in accordance with the Company’s Audit Committee investment guidelines of investing cash of the Company in low-risk interest-bearing instruments.

Operating Expenses

(Canadian $)	Three months ended March 31, 2015	2014	Six months ended March 31, 2015	2014
Operations				
Wages, benefits and consulting fees	**$ 133,995**	$ 132,747	**$ 293,458**	$ 231,069
Depreciation and amortization	**1,772**	2,215	**3,223**	4,430
Other	**14,347**	17,993	**22,599**	43,818
	150,114	152,955	**319,280**	279,317
Research and development activities				
Wages, benefits and consulting fees	**105,392**	97,458	**257,338**	198,733
Depreciation and amortization	**4,927**	6,159	**9,854**	12,318
Other	**15,303**	5,131	**28,017**	13,669
	125,622	108,748	**295,209**	224,720
Sales and marketing				
Wages, benefits and consulting fees	**111,171**	157,067	**227,694**	284,687
Travel	**35,348**	40,462	**63,839**	75,870
Other	**75,887**	49,881	**163,453**	77,795
	222,406	247,410	**454,986**	438,352
General and administrative				
Wages, benefits and consulting fees	**302,328**	240,204	**584,679**	654,566
Directors compensation	**36,228**	36,000	**72,228**	44,000
Professional fees	**165,416**	39,530	**257,338**	87,898
Facility	**70,867**	39,936	**135,965**	79,872
Depreciation and amortization	**13,967**	26,567	**26,777**	53,134
Other	**72,371**	44,796	**75,521**	67,700
	661,178	427,033	**1,152,508**	987,170
Total Operating Expenses	**$1,159,320**	$ 936,146	**$ 2,221,983**	$ 1,929,559

Operating expenses for the six months ended March 31, 2014 increased $292,424 or 15% to $2,221,983 compared to $1,929,559 for the same period last year.

Operating expenses for the three months ended March 31, 2014 increased $223,174 or 24% to $1,159,320 compared to $936,146 for the prior year. During the quarter the Company incurred approximately $145,000 in additional legal fees related to patent applications for new products and litigation, and legal defense. During the quarter the Company also incurred additional costs related to the openeding of a second facility in Mississauga, Ontario to allow for expanded production commercialization of its new advanced wound care, and specialized medical speciality device coatings products.

Related Party Transactions

The following is a summary of the Company's related party transactions related to key management compensation for the three and six month periods ended March 31, 2015 and 2014:

	Three months ended March 31,		Six months ended March 31,	
	2015	2014	**2015**	2014
Salary, benefits, management and directors fees	**$161,044**	$146,681	**$322,087**	$423,362
Share-based payments	**10,970**	27,379	**49,998**	54,758
	$172,014	$174,060	**$372,086**	$478,120

Critical Accounting Estimates and Judgements

The preparation of financial statements requires that management makes estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the Consolidated Financial Statements, and the reported amounts of revenue and expenses during the reporting periods. Actual results could differ from estimates and such differences would be material.

ESTIMATES

The effect of a change in an accounting estimate is recognized prospectively by including it in comprehensive income in the period of the change, if the change affects that period only, or in the period of the change and future periods if the change affects both.

i) Share-based Payment Transactions

The Company measures the cost of equity-settled transactions with directors, officers, and employees by reference to the fair value of the equity instruments at the date at which they are granted. Estimating fair value for share-based payment transactions requires determining the most appropriate valuation model, which is dependent on the terms and conditions of the grant. This estimate also requires determining the most appropriate inputs to the valuation model including the expected life of the share option, volatility and dividend yield, and making assumptions about them. The assumptions and models used for estimating fair value for share-based payment transactions are disclosed in Note 15 of the Consolidated Financial Statements.

ii) Intangible Assets

The values calculated for intangible assets involve significant estimates and assumptions, including those with respect to future cash flows, discount rates, and asset lives. These significant estimates and judgments could impact the Company's future results if the current estimates of future performance and fair value change. Variance from management's estimates could affect the amount of amortization expense on intangible assets in future periods.

iii) **Impairment of non-financial assets**

The Company reviews the carrying value of non-financial assets for potential impairment when events, or changes in circumstances, indicate that the carrying amount may not be recoverable. The impairment test is carried out by comparing the carrying amount of the asset against the value computed using the discounted cash flow method. This calculation which requires numerous assumptions to estimate future cash flows. The recoverable amount is impacted significantly by the discount rate selected to be used in the discounted cash flow model, as well as the quantum and timing of expected future cash flows, and the growth rate used for the extrapolation.

iv) **Income taxes**

The Company recognizes deferred tax assets, related tax-loss carryforwards and other deductible temporary differences where it is probable that sufficient future taxable income can be generated in order to fully utilize such losses and deductions. This requires significant estimates and assumptions regarding future earnings, and the ability to implement certain tax planning opportunities in order to assess the likelihood of utilizing such losses and deductions.

Uncertainties exist with respect to the interpretation of complex tax regulations and the amount, as well as timing, of future taxable income. Given the cross border business relationships, differences arising between the actual results and the assumptions made, or future changes in such assumptions, could necessitate future adjustments to taxable income and deductions already recorded. The Company established provisions, based on reasonable estimates, for possible consequences of audits by the tax authorities of the restive countries in which it operates. The amount of such provisions is based on various factors, such as experience of previous tax audits and differing interpretations of tax regulations by the taxable entity and the responsible tax authority. Such differences of interpretation may arise on a wide variety of issues depending on the conditions prevailing in the respective Company domicile.

JUDGMENTS

Information about critical judgments in applying accounting policies that have the most significant risk of causing material adjustment to the carrying amounts of assets and liabilities recognized in the consolidated financial statements within the next financial year are discussed below:

i) **Foreign Currency translation:**

The determination of functional currency for each of the Company's entities requires considerable judgment. The functional currency is determined based on the currency of the primary economic environment in which that entity operates. As the Company generates and expends cash in both the US and Canadian currencies, management considers several factors including: the currency in which it receives its various revenue streams and the magnitude of each; the currency in which it purchases materials and pays its employees; and the geographic environment influencing each of its consolidated entities and products.

ii) **Provisions**

A provision is a liability of uncertain timing or amount. Provisions are recognized when the Company has a present obligation (legal or constructive) as a result of a past event, it is probable that the Company will be required to settle the obligation, and a reliable estimate can be made of the amount of the obligation. A legal obligation can arise through a contract, legislation, or other operation of law. A constructive obligation arises from an entity's actions; whereby, through an established pattern of past practice, published policies, or a sufficiently specific current statement the entity has indicated it will accept certain responsibilities and has thus created a valid expectation that it will discharge those responsibilities. The amount recognized as a provision is the best estimate, at each period end, of the expenditures required to settle the present obligation considering the risks and uncertainties associated with the obligation. Judgment is necessary to determine the likelihood that pending litigation (or other claims) will succeed, or that a liability will arise and estimate the amount.

Summary of Quarterly Results and Financial Position

The quarterly financial information presented below represents eight quarters of operating results and financial position:

(in Canadian $)	2015 Second Quarter	2015 First Quarter	2014 Fourth Quarter	2014 Third Quarter	2014 Second Quarter	2014 First Quarter	2013 Fourth Quarter	2013 Third Quarter
Revenue (1)	$2,139,602	$1,336,685	$1,226,233	$1,270,058	$2,024,661	$4,498,820	$1,547,398	$1,482,132
Operating income (loss) before amortization	327,871	(137,796)	(861,770)	(151,710)	528,677	3,224,298	346,228	323,742
Net income (loss)	264,340	(229,820)	(909,704)	(240,156)	431,211	3,120,419	121,300	238,837
Net income (loss) per share (2)	0.03	(0.02)	(0.10)	(0.03)	0.05	0.34	0.01	0.03
Cash and cash equivalents	3,108,945	3,609,666	3,574,836	4,154,773	4,201,068	4,718,049	633,103	439,366
Net working capital	4,480,990	3,773,325	4,024,504	4,663,313	4,818,051	4,319,614	1,069,858	261,121
Current Ratio	3.8	3.2	3.9	3.4	3.3	2.9	1.6	1.1

(1) Includes product and services, licensing revenue, and net interest income (expense).

(2) Reflects 1 for 10 share consolidation which occurred in July 2013.

Revenue of the Company continues to be inherently unpredictable due to our business model and fluctuates from quarter to quarter depending on both the composition of contractual arrangements entered into in each quarter and the timing of completed coating and development services milestone in any period.

Liquidity & Capital Resources

(Canadian $)	**March 31, 2015**	September 30, 2014
Cash and cash equivalents	**3,108,945**	3,574,836
Short-term investments	**544,465**	541,000
Total assets	**8,533,205**	7,961,393
Deferred revenue	**783,431**	996,246

On March 31, 2015 cash, cash equivalents, restricted cash, and short-term investments amounted to $3,688,608 as compared to $4,268,345 as at September 30, 2014. During the six months ended March 31, 2015 the Company had negative cash flow of $465,891, due mainly to cash consumed by funding net working capital.

Revenue and profitability for the first six months of last year included an initial payment of US$3,500,000 by Mölnlycke Health Care AB related to the licensing of two of Covalon's products, IV Clear and SurgiClear, which was announced on November 4, 2013.

Cash flows from customer contracts will continue to be unpredictable quarter-to-quarter due to the timing of receipt of upfront payments under new contracts and the timing of royalty payments.

Cash and cash equivalents with less than three months to maturity totaled $3,653,410 at March 31, 2015. At March 31, 2015, the Company had and additional $35,198 assigned as collateral to secure the Company's credit cards. These funds are expected to be restricted for more than one year and are not included in cash and cash equivalents.

Total assets at March 31, 2015 were $8,533,205 compared to $7,961,393 at September 30, 2014. Cash, cash equivalents and short-term investments comprised 43% of total assets at March 31, 2015. The Company's accounts receivable and inventories are liquid, with collection periods and turnover ratios in the 60 to 180 day range. The balance of our assets is comprised of property, plant and equipment, and the Company's intangible assets; these have low liquidity but represent much of the intellectual property assets that are used to generate Covalon's revenue streams.

Deferred revenue decreased by $212,815 to $783,431 at March 31, 2015 compared to $996,246 at September 30, 2014.

Share Capital and Reserves

The Company is authorized to issue an unlimited number of common shares with no par value. All shares are fully paid.

During the year ended September 30, 2014 the Company raised $30,000 for 30,000 shares issued under a warrant agreement. No shares were issued during the six month period ended March 31, 2015.

The Company has an incentive Stock Option Plan ("the Plan") under which non-transferable options to purchase common shares of the Company may be granted to directors, officers, employees, or service providers of the Company. The terms of the Plan provide that the Directors have the right to grant options to acquire common shares of the Company at not less than the closing market price of the shares on the day preceding the grant at terms of up to five years. No amounts are paid or payable by the recipient on receipt of the option, and the options granted are not dependent on any performance-based criteria. Unless the board of directors decides otherwise options granted under the plan will vest as follows: 33% of the options vest in one year, with a further 33% vesting in each of the subsequent two years on the anniversary of the initial grant date.

On June 13, 2014 the Company granted 102,500 options at an exercise price of $2.00 with a weighted average fair market value of the options calculated at $1.89 per option.

On March 26, 2015 the Company granted 150,500 options at an exercise price of $1.40 with a weighted average fair market value of the options calculated at $1.29 per option.

Total expense arising from share-based payment transactions recognized during the three month period ended March 31, 2015 was $38,320 compared to $29,633 for the same period last year.

Total expense arising from share-based payment transactions recognized during the six month period ended March 31, 2015 was $75,973 compared to $61,324 for the same period last year.

Sources and Uses of Cash

	Six months ended March 31,	
(Canadian $)	**2015**	2014
Cash flows from operating activities	**(534,849)**	**3,572,277**
Cash flows from investing activities	**(110,730)**	**(55,515)**
Cash flows from financing activities	**113,846**	**-**

Operating Activities

Cash used in operating activities for the six month period ended March 31, 2015 was $534,849 compared cash generated of $3,572,277 for the same period last year. The six month period ended March 31, 2014 included cash collected from the licensing transaction with Molnlycke. Non-cash working capital used $720,461 of cash during the six month period ended March 31, 2015 compared to $218,510 for the six month period ended March 31, 2014. At March 31, 2015 accounts receivable had increased $722,771 over September 30, 2014 due mainly to large value shipments made prior to quarter end, but not yet collected.

Investing Activities

Investing activities comprise expenditures on general office furniture, lab equipment, and expenditures on intangible assets relate to filing and maintaining patents and trademarks.

Financing Activities

During the six month period ended March 31, 2015 the Company's bank released $117,311 held to secure financing facilities.

Off-Balance Sheet Arrangements

The Company does not have any off-balance sheet arrangements.

Financial Instruments

Unless otherwise noted it is Management's opinion that the Company is not exposed to significant interest or credit risks arising from financial instruments. The Company is exposed to currency risk arising from fluctuations in foreign exchange rates and the degree of volatility in those rates. The Company does not use derivative instruments to reduce its exposure to foreign currency risk.

Short-term investments consist of Guaranteed Investment Certificates (immediately redeemable) and the carrying value approximates fair market value.

All of the Company's cash is maintained by two of the major financial institutions located in Canada.

The Company has not entered into any futures, forward contracts, or other derivative instruments as at the date of this MD&A.

Risks and Uncertainties
An investment in the securities of the Company is speculative due to the proposed nature of the Company's business and the fact that Covalon Technologies Ltd. has only this past fiscal year achieved an annual profit. Consequently, an investment in the Company is subject to certain risks and investors should not invest in securities of the Company unless they can afford to lose their entire investment. In addition to the factors disclosed elsewhere in this MD&A, investors should consider the following risk factors in assessing the investment merits of such securities.

Medical Device and Biotechnology companies in the early revenue stage are subject to a number of risks and uncertainties that are inherent to the development of any new technology. General business risks include, among other things: uncertainty in product development and related clinical trials, the regulatory environment including delays or denial of approval to market products, the impact of technological change and competing technologies, the ability to protect and enforce its patent portfolio and intellectual property assets, the availability of capital to finance continued and new product development, the ability to secure strategic collaborators and its reliance on these collaborators for the development, regulatory approval, testing; manufacturing; commercialization and/or distribution of its products, and, the risk of product liability claims. In addition, market prices for securities of biotechnology companies are generally volatile and may or may not move in a manner consistent with the progress being made by a company.

Without limiting the foregoing, the following risks are discussed in more detail:

Covalon achieved net income in 2014, but has a history of net losses and may not maintain profitability in future periods.

Covalon achieved annual profitability of $2,401,769 for the year ended September 30, 2014; and, period profitability of $34,363 for the six months ended March 31, 2015. There is no guarantee that Covalon will be able to consistently achieve profitability in the future. Covalon has never paid a dividend on its common shares and does not expect to do so in the foreseeable future. Covalon's business and prospects must be considered in light of the risks, expenses, and difficulties frequently encountered by companies in new and rapidly evolving markets such as healthcare.

Covalon cannot predict if sustained profitability will ever be achieved and, if it is, whether or not it will be sustainable on a quarterly or an annual basis. Even if Covalon is not able to successfully further commercialize its products, Covalon believes that it has sufficient capital to fund its business and operations through at least fiscal 2015. However, Covalon may need to raise additional capital in the future. Additional financing may not be available, and even if available, may not be available on acceptable terms.

Any failure to obtain or protect intellectual property could adversely affect Covalon.

Covalon's success depends, in part, on its ability to obtain patents, or licenses to patents, maintain trade secret protection, and enforce its rights against others. Covalon has filed and is actively pursuing patent applications in Canada, the United States, and other jurisdictions. Covalon may not be able to obtain patent protection for key elements of its technology.
There can be no assurance that:

- patent applications will result in the issuance of patents;
- additional proprietary products developed will be suitably protected from infringement;
- patents issued will provide adequate protection or any competitive advantages;

- patents will not be successfully challenged by any third parties; and,
- patents of others will not impede Covalon's ability to commercialize its technology.

Covalon may need to obtain licenses for the development of its products. Licenses may not be available on satisfactory terms or at all. If available, these licenses may obligate Covalon to exercise diligence in bringing its technology to market and may obligate Covalon to make minimum guarantees or milestone payments. These guarantees and milestone payments may be costly and could seriously harm Covalon's business. Covalon may also be obligated to make royalty payments on the sales, if any, of products resulting from licensed technology, and may be responsible for the costs of filing and prosecuting patent applications. These costs could affect Covalon's results of operations and decrease its earnings.

Covalon's intellectual property includes trade secrets and know-how that may not be protected by patents. There can be no assurance that Covalon will be able to protect its trade secrets. To help protect its rights, Covalon requires employees, consultants, advisors, and collaborators to enter into confidentiality agreements. These agreements may not adequately protect Covalon's trade secrets, know-how, or other proprietary information in the event of any unauthorized use or disclosure.

Covalon's development programs, and products subject it to the risk of product liability claims, for which Covalon may not be able to obtain adequate insurance coverage.

Human therapeutic products and medical devices involve the risk of product liability claims and associated adverse publicity. Covalon's principal risks relate to the sales of its products and currently their use in clinical trials. Claims may be made by consumers, healthcare providers, third party strategic collaborators, or others selling Covalon's products. There can be no assurance that Covalon will be able to obtain or maintain sufficient and affordable insurance coverage for any of these claims. Without sufficient coverage any claim, any threat of such a claim, or any product withdrawal could seriously harm Covalon's business.

Covalon may incur substantial costs as a result of litigation or other proceedings relating to patent and other intellectual property rights.

Covalon's future success and competitive position depends, in part, on its ability to obtain and maintain certain proprietary intellectual property rights used in its principal products. Any such success may be achieved in part by prosecuting claims against others who Covalon believes are infringing its rights, and by defending claims of intellectual property infringement brought by its competitors and others. Covalon's involvement in intellectual property litigation could result in significant expenses adversely affecting the development of product candidates, sales of the challenged products, or sales of intellectual property. The litigation would also divert the efforts of Covalon's technical and management personnel whether or not such litigation is resolved in Covalon's favour. Some of Covalon's competitors may be able to sustain the costs of complex patent litigation more effectively than Covalon can because they have substantially greater resources. Uncertainties resulting from the initiation, and continuation, of any litigation could affect Covalon's ability to continue its operations.

In the event of an adverse outcome as a defendant in any such litigation, Covalon may, among other things, be required to:

- pay substantial damages;
- cease the development, manufacture, use, or sale of product candidates or products that infringe upon the intellectual property of others;

- expend significant resources to design around a patent, to develop, or acquire non-infringing intellectual property;
- discontinue processes incorporating infringing technology; and,
- obtain licenses to the infringed intellectual property.

If third-parties file patent applications, or are issued patents claiming technology also claimed by Covalon in pending applications, Covalon may be required to participate in interference proceedings with the United States Patent and Trademark Office (or other proceedings outside the United States). The proceedings may include oppositions to determine priority of invention, or patentability which could result in substantial cost to Covalon even if the eventual outcome were favourable.

Covalon or its clients are frequently required to receive regulatory approval for each of Covalon's product candidates before they can be sold commercially in North America, or internationally, which can take significant time and be very costly.

The development, manufacture, and sale of both medical devices and human therapeutic products in Canada, the United States, and internationally is governed by a variety of statutes and regulations.

These laws require, among other things:

- approval of manufacturing facilities and practices;
- adequate and well-controlled research and testing of products in pre-clinical and clinical trials;
- review and approval of submissions containing manufacturing, pre-clinical and/or clinical data in order to obtain marketing approval based on establishing the safety and efficacy of the product for each use sought including adherence to good manufacturing practices during production and storage; and,
- control of marketing activities, including advertising and labelling.

Some product candidates currently under development by Covalon will require significant development, pre-clinical and clinical testing, pre-market review and approval, and investment of significant funds prior to their commercialization. The process of completing clinical testing and obtaining such approvals (if required) is likely to take many years and require the expenditure of substantial resources. Covalon does not know whether any clinical studies will be successful, if regulatory approvals will be received, or if regulatory approvals will be obtained in a timely manner. Despite the time and resources expended by Covalon regulatory approval is never guaranteed.

Even if some of Covalon's products and manufacturing facilities receive regulatory approval those products and facilities may still face subsequent regulatory difficulties.

If Covalon receives regulatory approval to sell any of its products, regulatory agencies will limit the approval to certain diseases, conditions, or categories of patients who can use them. In addition, regulatory agencies subject a marketed product, its manufacturer, and the manufacturer's facilities to ongoing regulatory requirements. Regulatory agencies may also require expensive post-approval studies. Any adverse effects associated with Covalon's products must also be reported to regulatory authorities. If new data are developed, previously unknown adverse experiences with a product occur, deficiencies in Covalon's manufacturing and laboratory facilities are discovered, or Covalon fails to comply with applicable post-market regulatory requirements a regulatory agency may impose restrictions on that product or on Covalon. These may include the requirement to withdraw the product from the market; close the facility; suspend manufacturing; change the product's labels; or, pay substantial fines.

Covalon's success is partly dependent on its partners' success and the relationship with partners is governed by contracts.

Covalon is reliant on partners to execute certain key business processes. If its partners do not perform to Covalon's expectations, Covalon may be unable to enforce a change due to contractual terms. This may significantly impact Covalon's ability to generate revenues and profits.
Examples of such issues Include:

- Manufacturing may be prioritized other than as Covalon's customers desires;
- Production quality measures may not be achieved;
- Sales expectations are not achieved; and,
- New products are not launched expeditiously.

If Covalon fails to hire and retain key management, scientific, and technical personnel it may be unable to successfully implement its business plan.

Covalon is highly dependent on its senior management and its scientific and technical personnel for their domain knowledge and technical expertise. The competition for qualified personnel in the healthcare field is intense and Covalon relies heavily on its ability to attract and retain qualified managerial, scientific, and technical personnel. Covalon's ability to manage growth effectively will require continued implementation and improvement of its management systems and the ability to recruit and train new employees. Covalon may not be able to successfully attract and retain skilled and experienced personnel which could harm its ability to develop product candidates and generate revenues.

International Financial Reporting Standards
Standards, Amendments and Interpretations Not Yet Effective

Certain pronouncements were issued by the IASB or the IFRS Interpretations Committee that are mandatory for accounting periods beginning after October 1, 2013 or later periods. None of these are expected to have a significant effect on the consolidated financial statements except for the following standards and interpretations that have been issued but are not yet effective:

IFRS 9 Financial Instruments

IFRS 9 Financial Instruments is part of the IASB's wider project to replace IAS 39 Financial Instruments: Recognition and Measurement. IFRS 9 retains but simplifies the mixed measurement model and establishes two primary measurement categories for financial assets: amortized cost and fair value. The basis of classification depends on the entity's business model and the contractual cash flow characteristics of the financial asset. The standard is effective for annual periods beginning on or after January 1, 2018. The Company is in the process of evaluating the impact of the new standard.

IFRS 15 Revenue From Contracts with Customers

IFRS 15, Revenue From Contracts with Customers establish the principles that an entity shall apply to report useful information to users of financial statements about the nature, amount, timing, and uncertainty of revenue and cash flows arising from a contract with a customer. The standard is effective for annual periods beginning on or after January 1, 2017. Covalon has not yet assessed the impact of adopting this standard.

There are no other IFRSs or IFRIC interpretations that are not yet effective that would be expected to have a material impact on the Company.

Disclosure Controls and Procedures and Internal Controls over Financial Reporting

Effective as of December 15, 2008, the Ontario Securities Commission approved the revised *National Instruments 52-109, Certification of Disclosure in Issuers' Annual and Interim Filings* ("NI 52-109"). The revised NI 52-109 extends the exemption for venture issuers from certifications relating to the establishment and maintenance of disclosure controls and procedures ("DC&P) and internal controls over financial reporting ("ICFR"), as defined in NI 52-109. Additional risks to the quality, reliability, transparency, and timeliness of the Company's interim and annual filings may result from the inherent limitations on management's ability to design and implement on a cost effective basis DC&P and ICFR. The Company recognizes the importance of DC&P and ICFR, and will endeavour to have sufficient controls in place to ensure financial statements are materially correct and sufficiently disclosed.

The Company continues to formalize procedures and control measures that are already in place and to introduce new ones to ensure good evaluation and control practices. As of September 30, 2014, the Company's management evaluated the effectiveness of the design and operation of its disclosure controls and procedures as defined under the rules. The evaluation was performed under the supervision, and with the participation, of the Chief Executive Officer (CEO) and Chief Financial Officer (CFO). Based on the evaluation of the DC&P, the CEO and the CFO have concluded that, subject to the fact that an evaluation of controls can provide only reasonable, not absolute, assurance that all control issues and instances of fraud or error, if any, within the Company have been detected, the Company's DC&P are effective in providing reasonable assurance that material information relating to the Company is made known to management. Changes and new controls are evaluated and implemented as required to provide greater business control.

The design of ICFR within the Company is management's responsibility to provide reasonable assurance that the reliability of financial reporting and that the preparation of financial statements for external purposes follow Canadian generally accepted accounting principles.