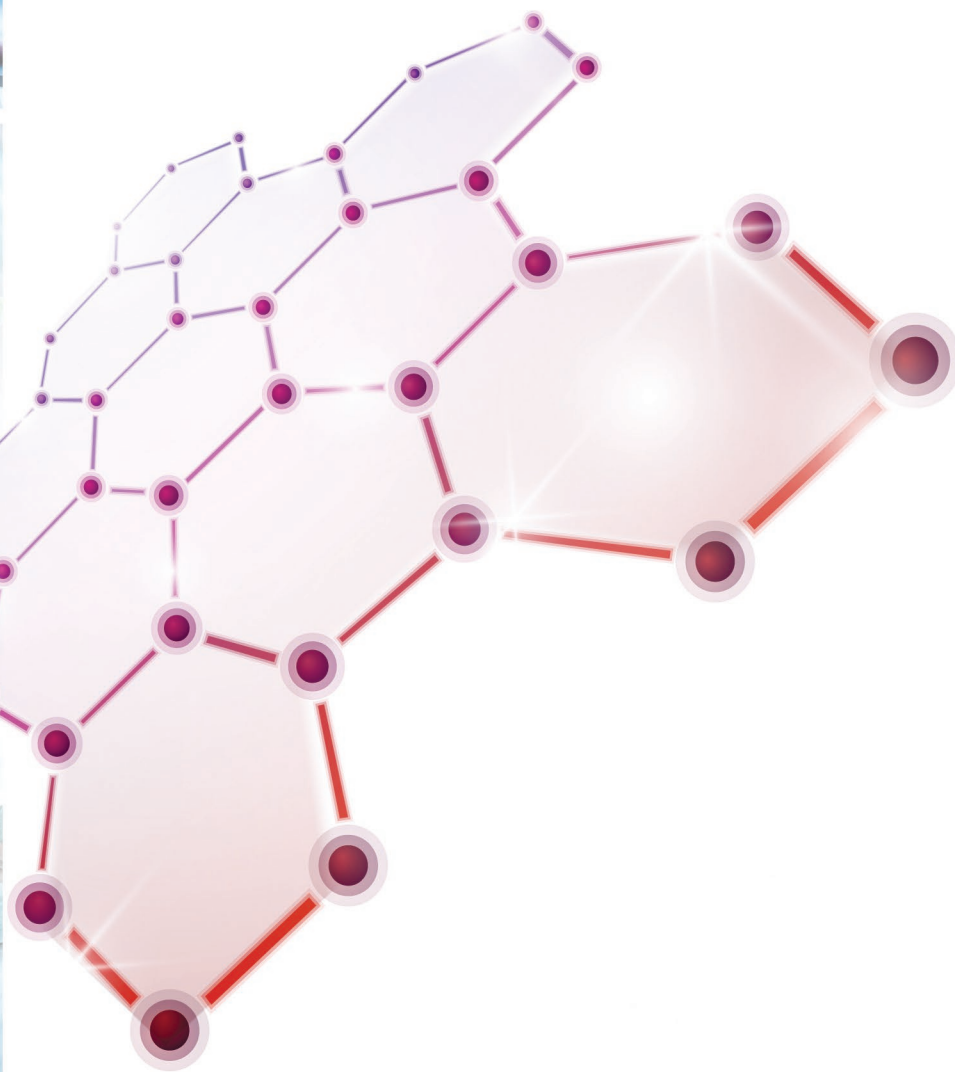


MICROBIX BIOSYSTEMS INC.



FIRST INTERIM REPORT

For the three months
ended December 31, 2017



MESSAGE TO SHAREHOLDERS

The first quarter of fiscal 2018 (Q1) has provided evidence of Microbix' growth potential: Sales were a new record for a first quarter, 48% above the first quarter of 2017 and 171% above those of 2016.

Record Q1 revenues of nearly \$2.9 million were driven by increased demand for Microbix' antigen products. However, Q1 did not benefit materially from ongoing changes to production methods, product mix and capacity. Accordingly, Microbix still incurred a net loss of \$0.1 million for Q1.

Multiple endeavors are now underway to optimize both sales and net earnings. In Q1, this included securing \$3.1 million of net new funding needed to enable growth plans. We are grateful to shareholders old and new for their support.

With the needed funding in place, we are taking steps to increase the capacity of our plant and boost our bioreactor capabilities. That work should permit us to fulfill growing antigen demand from the diagnostics industry and thereby achieve both higher sales and higher margins. To be clear, we are in business to achieve profits, not losses!

In November, we announced plans to double the power supply to our plant and to increase our bioreactor capacity by 500%. I am pleased to report that the power upgrade has been completed, which most specifically enables increased antigen purification capacity. Additionally, the majority of the new bioreactor capacity is now operational, with the balance to become available toward the end of March. With that completed, we can reallocate our people and equipment to optimize productivity and profitability. We look forward to reporting on such progress over the coming several quarters.

Broadly-speaking, we are targeting sustained double-digit growth in sales, along with material enhancement of gross margin. Starting from the near-to-breakeven results of Q1, it is management's goal to achieve significant profitability in fiscal 2019 and to demonstrate continuing progress toward that goal over the balance of fiscal 2018.

In considering our progress, I urge you to visit our company website at www.microbix.com. Our team has been working to update it in order to more readily showcase and explain Microbix' business. Additionally, the website now provides for on-line ordering of our products, a feature not important to large and well-established customers, but that may help introduce new customers to our products.

Having discussed developments in our core antigens business, let's review our development projects:

1. In Q1, we helped secure the future of our quality assessment products business by clearing-up a legal dispute and, early in Q2, announced our plans for 48 new products. Quality products now comprise 10% of sales at favorable margins and we intend to keep growing this complimentary line of business.

2. For Kinlytic, we will shortly be commencing a comprehensive outreach program to secure a funding and development partner. This work follows the successful consultation with FDA in 2017 and subsequent detailed project costing based on 3rd party quotations. Our goal is now to secure a partnership agreement over the balance of 2018.

3. For LumiSort, Microbix is proceeding cautiously given the litigious environment in the livestock sex-selection market. We continue to develop our IP portfolio for this asset, with the concurrent goal of securing a partner to complete development of its livestock applications. In so doing, we intend to retain rights to potential human health applications.

For the balance of fiscal 2018, we are pursuing continuing growth in sales of our antigen and quality products and positive net earnings. Successful partnering of Kinlytic or LumiSort would add to such value creation and are also goals. We therefore remain very optimistic about Microbix' prospects.

Personally and on behalf of our team, I thank you for your continuing support and wish you all the best.

CAMERON L. GROOME
CHIEF EXECUTIVE OFFICER AND PRESIDENT

**MANAGEMENT'S DISCUSSION AND ANALYSIS
OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS
FOR THE THREE MONTHS ENDED DECEMBER 31, 2017 AND 2016**

Canadian Funds

The Company's Management's Discussion and Analysis ("MD&A") should be read in conjunction with the unaudited Consolidated Interim Financial Statements and notes for the quarter ended December 31, 2017 and should also be read in conjunction with the audited Consolidated Financial Statements, notes and MD&A for the year ended September 30, 2017, prepared in accordance with International Financial Reporting Standards ("IFRS") and filed on SEDAR. Additional information relating to the Company, including its Annual Information Form ("AIF"), can be found on SEDAR at www.sedar.com. Reference to "we", "us", "our", or the "Company" means Microbix Biosystems Inc. unless otherwise stated. All amounts are presented in Canadian dollars unless otherwise stated. Statements contained herein, which are not historical facts, are forward looking statements that are subject to certain risks and uncertainties that could cause actual results to differ materially from those set forth or implied. These forward-looking statements involve risks and uncertainties, including the difficulty in predicting product approvals, acceptance of and demand for new products, the impact of the products and pricing strategies of competitors, delays in developing and launching new products, regulatory enforcement, changes in operating results and other risks, some or any of which could make the results differ materially from those discussed or implied in the forward-looking statements. The Company disclaims any intent or obligation to update these forward-looking statements.

The Management Discussion and Analysis is dated February 12, 2018.

COMPANY OVERVIEW

Microbix Biosystems Inc. (Microbix or the Company) (TSX: MBX) develops biological products and technologies. The Company has viral and bacterial products (Virology) business including the manufacturing and sale of cell culture-based biological products, including one of the world's most expansive sources of infectious disease antigens targeted at the diagnostics market. The Company owns Kinlytic® Urokinase, an FDA regulated human thrombolytic drug, and is developing LumiSort™, a technology platform for ultra-rapid and efficient sorting of somatic cells that can be used to enrich cell populations of interest.

Revenue from the Virology business is expected to continue growing for the foreseeable future with this growth recently accelerating as certain public health tests are being adopted in the Asia Pacific region. The Virology business provides free cash flow to cover operating and debt service costs, and funding for business initiatives that leverage this expertise and are related to this field.

The Company owns and operates a Virology manufacturing facility at 265 Watline Avenue in Mississauga, Ontario. The facility has an infectious diseases biological license from the Canadian Food Inspection Agency. The Company's administrative offices are located at 211 Watline Avenue, Mississauga, Ontario.

FINANCIAL OVERVIEW**Quarter Ending December 31, 2017**

Total revenue was \$2,885,567, a 48% increase over last year's first quarter revenue of \$1,952,502. Included was Virology product revenue of \$2,802,585, 49% higher than last year's first quarter, due to strong growth into International markets and increased sales to our key customers. Revenue from royalties were \$82,982 (2016 - \$65,678).

Gross margin increased by \$504,458 or 62%, due to increased revenues as outlined above and a change in the product mix.

Operating expenses decreased by \$2,767,887 compared to the first quarter last year. This was primarily due to one-time costs incurred in the first quarter of last year related to (1) a non-cash adjustment of \$2,582,526 to

Quarter Ending December 31, 2017 (Continued)

restructure the Company's convertible debentures as part of our debt refinancing initiative that was necessary in order to implement an enhanced revolving credit facility for the Company, and (2) the settlement of a dispute with the buyer of the Company's WFI business in 2012 in the amount of \$258,540.

As a result, the Company experienced a net loss for the period of \$94,128 (2016 – net loss of \$3,216,472).

Cash used in operations in this quarter was \$1,434,085 compared to cash provided by operations of \$309,542 in Q1 2017, as a result of significantly reducing our outstanding accounts payables and accrued liabilities during the quarter. Cash used in investing activities was \$495,446 (2016 - \$205,741), reflecting our investment in bioreactor equipment to expand our manufacturing capacity. Net cash generated from financing activities was \$1,926,459 (2016 – used in \$107,536). During the quarter the company raised \$3,137,283 (net of issue costs) in a private placement. These funds were used primarily to pay down our bank debt, reduce our accounts payable obligations and invest in capital equipment and working capital to support our growth. Net cash flow was \$3,071 negative in this quarter (2016 - \$3,735 negative).

CHANGES IN FINANCIAL POSITION

| | As at Dec. 31, 2017 | As at Dec. 31, 2016 |
|---|------------------------|------------------------|
| Total Revenue | \$2,885,567 | \$1,952,502 |
| Gross Margin | 1,318,987 | 814,529 |
| S,G&A Expenses | 951,441 | 919,888 |
| R&D Expense | 252,283 | 201,150 |
| Financial Expenses | 209,390 | 218,897 |
| Net Operating Income (Loss) (Before Debt Restructuring and Settlement Costs) | (94,128) | (525,406) |
| Cash Provided (Used) by Operating Activities | (1,434,085) | 309,542 |
| Cash | 51,389 | 1,680 |
| Accounts receivable | 1,575,827 | 1,081,314 |
| Total current assets | 6,511,696 | 5,042,192 |
| Total assets | 27,434,188 | 24,883,685 |
| Total current liabilities | 4,092,867 | 5,036,001 |
| Total liabilities | 8,997,537 | 9,603,189 |
| Total shareholders' equity | 18,436,651 | 15,280,496 |
| Current ratio | 1.59 | 1.00 |
| Debt to equity ratio | 0.49 | 0.63 |

SELECTED QUARTERLY FINANCIAL INFORMATION

| | Mar-31-16 | Jun-30-16 | Sep-30-16 | Dec-31-16 | Mar-31-17 | Jun-30-17 | Sep-30-17 | Dec-31-17 |
|--|------------------|------------------|------------------|--------------------|------------------|------------------|--------------------|------------------|
| | \$ | \$ | \$ | \$ | \$ | \$ | \$ | \$ |
| Sales | 2,729,779 | 2,253,373 | 3,470,580 | 1,952,502 | 2,646,649 | 2,773,365 | 2,813,282 | 2,885,567 |
| Net Operating Income (Loss) | 161,979 | (141,082) | 555,930 | (3,366,472) | 107,649 | 38,646 | (1,009,911) | (94,128) |
| Net Operating Income (Loss), before Debt restructuring and settlement costs | 161,979 | (141,082) | 555,930 | (525,406) | 107,649 | (164,104) | (917,673) | (94,128) |

OUTLOOK**Canadian Funds**

Microbix' business is producing high quality viral and bacterial antigens for use in the diagnostic testing industry and is the result of nearly three decades of experience in the field. As a result of Microbix' expertise and manufacturing capabilities, its products have received widespread and longstanding customer acceptance, with continuing growth in demand. More recently, growth in customers' demand for its products has been accelerating – as a number of diagnostics for infectious diseases important to public health are beginning to be adopted in the Asia-Pacific region.

Microbix is reinvesting in its business to help ensure that it can meet the growth in demand that large new markets are expected to provide. Such work includes upgrading its manufacturing technologies, processes, capacity and allocation of capacity, along with developing and launching new diagnostics-oriented products.

Based on the order projections of customers, management expects sales of viral and bacterial antigens will continue to grow for the foreseeable future. Accordingly, the Company is increasing its production – by way of expanding the capacity to make antigen using bioreactors, reallocating its conventional (roller-bottle) antigen production space and improving in-process controls and downstream production methods. It is intended that these steps increase the revenue potential of current production facilities while also improving margins. As a result of these efforts, management expects to grow sales and improve profitability.

Since securing private placement funding in support of its plans in October, Microbix has quickly put those funds to work. In accordance with the plans announced in November, the power supply to its manufacturing plant has been doubled and equipment purchased to increase its bioreactor production by 500%. In conjunction with other upgrades, such changes will help Microbix to expand production, improve its production methods, optimize its mix of products and maximize gross margins.

However, implementing such changes takes time. Specifically, while both sales and gross margins improved in Q1, neither are anywhere near to fully-optimized. It will require the completion of ongoing site renovations and the full installation, qualification and operation of new equipment and processes for Microbix to fully realize the financial benefits of its plans. That realization is expected to be ongoing through fiscal 2018, with improvements likely to be progressively apparent over the next several quarters. Management is looking forward to updating you about this progress.

Happily, progress has not been limited solely to antigen production and sales – there have also been developments with Microbix' quality assessment product line and its development projects.

Quality assessment products refer to an emerging product line that involves the development and sale of products that assist diagnostics industry participants with meeting quality objectives or requirements. Such products are inactivated (i.e., non-infectious) samples of intact pathogens that can be used to assess such matters as whether testing equipment is working properly or being operated correctly. While some such quality products are currently being sold by Microbix, many more are in development and sales are expected to accelerate as required validations of such new products are completed. Such work is ongoing, as evidenced by Microbix' announcement of its plans for the addition of 48 new quality assessment products, made shortly after quarter-end (January 2018).

The regulatory requirements of these quality assessment products are dependent on their intended usages and Microbix plans to upgrade its production quality systems to meet the highest such requirements – to enable it to realize the full scope of such opportunities. At present, such quality assessment products comprise approximately 10% of annual sales, with that proportion expected to increase.

Microbix also continues to advance its two sizeable and pre-revenue development projects – Kinlytic® urokinase (Kinlytic) and LumiSort™ cell-sorting technology (LumiSort). While large-scale spending on these projects has been halted, management has not been inactive. Work is proceeding on unlocking the value of these assets by partnering them to advance each toward full commercialization.

For Kinlytic, Microbix is completing its plans for re-launching Kinlytic into the United States (U.S.) market. Those plans are guided by its successful 2017 consultation with the U.S. Food and Drug Administration (FDA) and have the objective of approval for sale into the U.S. market three years after project funding. Firm third-party quotations have been gathered from qualified contractors for all relevant stages of the re-launch process in order to provide a stronger basis for project partnering discussions. Financial modeling of project economics based on those quotations has been completed

OUTLOOK (Continued)**Canadian Funds**

and suggests the re-launch of Kinlytic should be very rewarding to project participants. Microbix plans to conduct an intense outreach process beginning in Q2, with the objective of securing a partner to fully-fund the Kinlytic project as soon as possible thereafter. Such an alliance should result in near and longer term financial benefits to Microbix.

For LumiSort, Microbix continues to navigate a contentious market dynamic in the livestock genetics industry – where the incumbent sex-selection provider and its largest customer are in litigation. Partnering discussions are ongoing for this asset, but Microbix is being appropriately cautious in light of this environment. Our actions continue to be focused upon ensuring national-level issuances of Microbix' latest cell-sorting patent and on staying fully-apprised of market developments. For fiscal 2018, Microbix is continuing to pursue commercialization options in the field of livestock sex-selection and also intends to explore the potential human health applications of its cell-sorting innovations.

To summarize, management believes the outlook for the antigens and quality business is positive and that increased sales, margins and profits are likely from them over the coming quarters. In turn, Microbix is working to realize value from its Kinlytic and LumiSort development projects via successful partnering.

LIQUIDITY, CASH FLOWS AND CAPITAL RESOURCES

The consolidated financial statements have been prepared in accordance with the International Financial Reporting Standards ("IFRS") on a going concern basis, which presumes the Company will continue operating for the foreseeable future and will be able to realize a return on its assets and discharge its liabilities and commitments in the normal course of business.

The Company has incurred historical losses resulting in an accumulated deficit of \$27,170,965 as at December 31, 2017. Management continuously monitors the financial position of the Company with respect to working capital needs, as well as long-term capital requirements compared to the annual operating budget. Variances are highlighted and actions are taken to ensure the Company is appropriately capitalized.

Future Liquidity and Capital Needs

The Company primarily funds new product development activities and capital expenditures from profits earned by its business and, periodically from additional equity and/or debt.

Over the course of fiscal 2018, cash flow is expected to improve due to: 1) continued growth in antigen and quality product sales, 2) improvements in product pricing and other sales terms, 3) commencement of sales of higher margin product from the Company's bioreactor production process, and 4) other business development and financial initiatives. Management expects these developments will significantly improve the overall liquidity position, as the Company's plans come to full fruition.

The \$3.1 million of net proceeds from Microbix' October private placement have been deployed to support growth plans and ongoing operations. Principal utilizations have been to purchase needed equipment, support increases in receivables and inventories, and reduce outstanding payables – including legal costs incurred to preserve quality assessment product opportunities (i.e., the Zeptomatrix dispute). Further funds were allocated to reduce bank credit utilization, which may be redrawn as needed.

Microbix will continue to monitor and manage its cash position, with the objective of anticipating and meeting all future liquidity and capital needs.

Contractual Obligations**New Distribution Agreement**

On January 12, 2017 Microbix signed a distribution agreement with Meridian Life Science, Inc.. Under the terms of the Agreement, Meridian will receive exclusive distribution rights to Microbix' branded antigen products for China, Hong Kong, Taiwan and Macau. Additionally, Microbix will also provide bulk-finished product to Meridian to be sold under Meridian-label to customers in the Asia-Pacific region. Both companies will explore additional collaboration opportunities in the future.

The relationship will enable Microbix to leverage its expanding manufacturing capacity and Meridian's substantial commercial presence to better serve the region's diagnostic customers. Overall, the distribution collaboration has significantly expanded the business relationship between the two companies, and serves as a platform for the continued growth and expansion of their respective products and services.

Expanded Customer Agreement

On August 8, 2017 Microbix announced the execution of an expanded customer supply agreement. Under the agreement, Microbix will supply an existing long-term customer with an increasing quantity of viral antigen products over the next five years, with the parties having the option to extend that term. Sales from the agreement are expected to total \$25 million, with approximately \$10 million to be incremental business. The agreement is with a major global diagnostics company with growing sales of infectious disease tests that require more antigen supply. The parties' obligations under the agreement are those customary for the supply and purchase of biological materials and its renewal and expansion provides Microbix with a secure base of business and underpins its decision to increase its production by expanding bioreactor capacity and other measures.

Settlement of Disputes

On December 30, 2016 Microbix reached a final settlement with Irvine Scientific Inc. over a dispute related to the sale of the Company's Water-for-Injection business to Irvine in December 2012. Microbix has agreed to pay Irvine (U.S.) \$192,500 in three installments as follows –

| | | |
|-------------------|--------|----------|
| December 30, 2016 | (U.S.) | \$64,167 |
| March 31, 2017 | (U.S.) | \$64,167 |
| June 30, 2017 | (U.S.) | \$64,166 |

As of June 30, 2017, all financial obligations relating to this settlement have been completed.

On October 11, 2017 Microbix announced the court approval of a legal dispute settlement with Zeptometrix Corporation, with the latter party's claims of patent infringement being withdrawn. The withdrawal of the lawsuit was 'with prejudice', following a settlement agreement between the parties that was to Microbix' satisfaction.

Outstanding Share Capital

Share capital issued and outstanding as at February 12, 2018 was \$33,964,663 for 96,770,890 common shares versus \$31,299,416 for 84,704,257 common shares at September 30, 2017.

Historical spending patterns are no indication of future expenditures. Investment in the new products and technologies is at the discretion of management. The Company is not aware of any material trends related to its business that have not been discussed in this Management Discussion and Analysis dated February 12, 2018.

RISKS AND UNCERTAINTIES

The Company is exposed to business risks, both known and unknown, which may or may not affect its operations. Management works continuously to mitigate unacceptable risk, while still allowing the business to grow and prosper. These risk factors include the following:

A significant portion of Virology Product sales are dependent on key clients, open borders, international transportation systems, and access to raw materials.

A significant share of the Company's Virology products sales are sold to a few key customers globally. These products contributed a significant share of the revenue in 2017. The loss of a key customer, or restrictions on export, import, or international transportation of its products, raw materials or insufficient marketing resources, could materially impact revenue and profitability.

Environmental, safety and other regulatory

Microbix' research and manufacturing operations involves potentially hazardous materials. The Company takes extensive precautions to appropriately manage these materials as regulated by the applicable environmental and safety authorities. Changes in environmental and safety legislation may limit the Company's activities or increase costs. An environmental accident could adversely impact its operations. Microbix' diagnostic products are not regulated by governments in Canada or other jurisdictions. Commercialization of certain products requires approval of regulatory agencies such as the FDA, in which case Microbix will not receive revenue until regulatory approval is obtained.

Re-Launch of Kinlytic® urokinase

Microbix' goal is to re-launch this biologic clot-buster drug into the United States market. The Company has consulted with the United States Food and Drug Administration about the viability of its re-launch plans and secured quotations for major project tasks from third-party service providers to independently validate budgets and timelines. Outreach will shortly be undertaken to secure project funding from development partners on the basis of the resulting re-launch plans. There is no assurance the Company will be successful in this endeavour.

Commercialization of LumiSort™ technology

Microbix has developed a proprietary cell-sorting technology that has a global patent estate and successfully completed a prototype instrument that confirms its key patent claims. The Company is currently working to secure a partner from within the animal genetics industry to fund the next stage of development – to build a commercial semen-sexing instrument and conduct field trials. There is no assurance the Company will be successful in this endeavour.

Quality Assessment Products in development

The Company has multiple quality assessment products under development, with the goal of building its sales of this category of product. There is no assurance that these development activities will result in the completion of new commercial products. If the Company is unable to develop and commercialize products, it will be unable to recover its related product development investments.

Product commercialization requires strategic relationships

To commercialize large market products in development, Microbix may need to establish strategic partnerships, joint ventures or licensing relationships with pharmaceutical, biotechnology or animal genetics companies. It is possible the Company may be unable to negotiate mutually acceptable terms.

Operating and capital requirements

Microbix earns a profit on the sale of its Virology Products, which is a major source of funding for its research and development activities. The Company believes that cash generated from operations is sufficient to meet normal operating and capital requirements. However, the Company may need to raise additional funds, from time to time for several reasons including, to advance its current research and development programs, to support various collaboration initiatives with third parties, to underwrite the cost of filing, prosecuting and enforcing patents and other intellectual property rights, to invest in acquisitions, new technologies and new market developments. Additional financing may not be available, and even if available, may not be offered on acceptable terms.

Future success may depend on successfully commercializing new products or technologies

In the nearer term, Microbix must maintain and grow its existing product sales. To survive and prosper over the longer term, Microbix may need to commercialize new products or technologies. Such work is inherently uncertain and there is no guarantee that Microbix will be successful with its efforts.

Failure to obtain and protect intellectual property could adversely affect business

Microbix' future success depends, in part, on its ability to obtain patents, or licenses to patents, maintain trade secret protection and enforce its rights against others. The Company's intellectual property includes trade secrets and know-how that may not be protected by patents. There is no assurance that the Company will be able to protect its trade secrets. To help protect its intellectual property, the Company requires employees, consultants, advisors and collaborators to enter into confidentiality agreements. However, these agreements may not adequately protect trade secrets, know-how or other proprietary information in the event of any unauthorized use or disclosure. Protection of intellectual property may also entail prosecuting claims against others who the Company believes are infringing its rights. Involvement in intellectual property litigation could result in significant costs, adversely affecting the development of products or sales of the challenged product, or intellectual property, and divert the efforts of its scientific and management personnel, whether or not such litigation is resolved in the Company's favour.

Microbix will continue to face significant competition

Competition from life sciences companies, and academic and research institutions is significant. Many competitors have substantially greater resources and general capabilities in the areas of scientific and product development, legal review, manufacturing, sales and marketing, and financial support than Microbix. While the Company continues to expand its technological, commercial, legal and financial capabilities in order to remain competitive, Microbix' competitors may also be making significant investments in all of these areas, which could make it more difficult for Microbix to commercialize its products and technologies.

The primary risks affecting the Company are summarized below and have not changed during the fiscal year. The list does not cover all risks, nor is there an assurance that the strategy of management to mitigate the risks is sufficient to eliminate the risk.

Credit risk:

The Company's customers are primarily large multi-national companies with very high quality credit ratings. Given this track record, management perceives the credit risk to be low. Typically the outstanding accounts receivable balance is relatively concentrated with a few large customers representing the majority of the value. At December 31, 2017, five customers accounted for 82% (2016 – five customers accounted for 74%) of the outstanding balance. The Company has had minimal bad debts over the past several years and accordingly management has recorded an allowance of \$10,000 (2016 - \$10,000).

Currency risk:

The Company is exposed to currency risk given its global customer base. Over 90% of its revenue is denominated in either U.S. dollars or Euros. The Company does not use financial instruments to hedge this currency risk. At December 31, 2017, the significant balances, quoted in Canadian dollars, held in foreign currencies are:

| | US dollars | | Euros | |
|--|------------|------------|----------|-----------|
| | 2017 | 2016 | 2017 | 2016 |
| Cash | \$ 49,835 | \$ 7,448 | \$ - | \$ 85 |
| Accounts receivable | 717,516 | 423,030 | 400,854 | 229,658 |
| Accounts payable and accrued liabilities | \$ 297,820 | \$ 369,592 | \$ 1,505 | \$ 21,587 |

The impact of a 5% increase in the U.S. dollar against the Canadian dollar would result in an increase in annual U.S. dollar based revenue of about \$284,600 Cdn. The impact of a 5% increase in the Euro against the Canadian dollar would result in an increase in annual Euro based revenue of about \$201,800. Correspondingly, the impact of a 5% decrease in the U.S. dollar against the Canadian dollar would result in a loss in annual U.S. dollar based revenue of about \$284,600 Cdn. The impact of a 5% decrease in the Euro against the Canadian dollar would result in a loss in annual Euro-based revenue of about \$201,800.

Liquidity risk

Liquidity risk measures the Company's ability to meet its financial obligations when they fall due. To manage this situation, the Company projects and monitors its cash requirements to accommodate changes in liquidity needs. In addition, during fiscal 2017 the Company announced that it has arranged a new secured revolving credit facility with The Toronto-Dominion Bank ("TD Bank") and Export Development Canada ("EDC"). The credit facility is being used to fund the Company's need for working capital to grow its existing business. Management expects this new facility will help satisfy the Company's liquidity needs and to manage the liquidity risk going forward.

Interest rate risk

Financial instruments that potentially subject the Company to interest rate risk include those assets and liabilities with a variable interest rate. Exposure to interest rate risk is primarily on the BDC debt that has a variable rate pegged to the bank rate. The rate can be fixed, if the outlook indicates interest rates will move higher. The only other variable debt the Company has is the \$1,500,000 line of credit that bears interest at the bank's prime lending rate plus 2.25%. A 1% increase in the bank rate would cost the Company approximately \$30,000 per year for BDC and about \$15,000 on the line of credit usage if it were fully used throughout the fiscal year.

Market risk

Market risk reflects changes in pricing for both Virology products and raw materials based on supply and demand criteria; also market forces can affect foreign currency exchange rates as well as interest rates which could affect the Company's financial performance or the value of its financial instruments. Microbix products are valuable components in our customers' products and cannot be easily replaced. The Company works closely with customers to ensure its products meet their specific criteria.

Fair value

The fair value of a financial instrument is approximated by the consideration that would be agreed to in an arm's length transaction between willing parties and through appropriate valuation methods, but considerable judgement is required for the Company to determine the value. The actual amount that could be realized in a current market exchange could be different than the estimated value.

The fair values of financial instruments included in current assets and current liabilities approximate their carrying values due to their short-term nature.

The fair value of the long-term debt is based on rates currently available for items with similar terms and maturities. The convertible and non-convertible debenture fair values are not readily determinable as the convertible debentures have been issued to shareholders of the Company. The fair values of financial instruments in other long-term liabilities approximate their carrying values as they are recorded at the net present values of their future cash flows, using an appropriate discount rate.

CRITICAL ACCOUNTING ESTIMATES

The preparation of these consolidated financial statements requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities, revenues and expenses. The Company's audited consolidated financial statements are prepared in accordance with International Financial Reporting Standards ("IFRS") and the reporting currency is Canadian dollars. On an on-going basis, management bases its estimates on historical and other experience and assumptions, which it believes are reasonable in the circumstances. The significant accounting policies that the Company believes are the most critical in fully understanding and evaluating the reported financial results include:

Intangible Assets

Intangible assets include technology costs, patents, trademarks and licenses. Each is recorded at cost and amortized on a straight-line basis over the term of the agreements. Intangible assets with indefinite lives are not amortized but are assessed for impairment on an annual basis.

Impairment of Long-lived Assets

The Company reviews the carrying value of non-financial assets with definite lives for potential impairment when events or changes in circumstances indicate that the carrying amount may not be recoverable. The carrying value of non-financial assets with indefinite lives, and of non-financial assets with definite lives but are not ready for use, are assessed at least annually for impairment based on the impairment test on cash-generating units (CGUs). The impairment test on CGUs is carried out by comparing the carrying amount of the CGU and its recoverable amount. The recoverable amount of a CGU is the higher of fair value less costs to sell and its value in use. This complex valuation process entails the use of methods such as the discounted cash method 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 risk-adjusted future cash flows and the growth rate used for the extrapolation.

The impairment loss is calculated as the difference between the fair value of the asset and its carrying value. Management has determined that no long-lived assets of the Company as at December 31, 2017 have met the criteria for impairment.

Non-Convertible and Convertible Debentures

Management determines the fair value of the debenture using valuation techniques. Those techniques are significantly affected by the estimated assumptions used, including discount rates, expected life and estimates of future cash flows.

Deferred income taxes

Deferred income tax assets and liabilities are recognized for the estimated income tax consequences attributable to differences between financial statement carrying amounts of assets and liabilities and their respective income tax bases. Deferred income tax assets and liabilities are measured using tax rates expected to be in effect when the temporary differences are expected to be recovered or settled. The effects of changes in income tax rates are reflected in future income tax assets and liabilities in the year that the rate changes are substantively enacted.

Share-based payments

The Company applies the fair value method of accounting for stock-based compensation for awards granted to officers, directors, employees and consultants of the Company. The fair value of the award at the time of granting is determined using the Black-Scholes option pricing model, and recognized as a compensation expense on a straight-line basis over the vesting period with an offsetting amount recorded to contributed surplus. The amount of the compensation cost recognized at any date at least equals the value of the portion of the options vested at that date. When stock options are exercised, the consideration paid by employees or directors, together with the related amount in contributed surplus, is credited to capital stock. When an employee leaves the Company, vested options must be exercised within 90 days, or the options expire. Any options that are unvested are reversed in the period that the employee leaves.

FINANCIAL INSTRUMENTS

The fair value of a financial instrument is approximated by the consideration that would be agreed to in an arm's length transaction between willing parties and through appropriate valuation methods, but considerable judgment is required for the Company to determine the value. The actual amount that could be realized in a current market exchange could be different than the estimated value.

The carrying amounts of cash and cash equivalents, accounts receivable, bank indebtedness and accounts payable and accrued liabilities approximate fair value due to the short-term maturities of these instruments. Based on available market information, the fair value of the obligation under capital lease approximates its carrying value.

The fair value of the long-term debt is based on rates currently available for items with similar terms and maturities. The fair value of the liability for each convertible debenture has been calculated and the residual is accounted for in equity. The Company does not have any off balance sheet financial instruments.

Disclosure Controls

The Chief Executive Officer and the Chief Financial Officer have evaluated the effectiveness of the Company's disclosure controls and procedures, as defined in the National Instrument 52-109 Certification of Disclosure in Issuer's Annual Filings (NI 52-109F1). As at December 31, 2017, management has concluded that the disclosure controls are effective in providing reasonable assurance that information required to be disclosed in the Company's reports is recorded, processed summarized and reported within the time periods specified in the Canadian Securities Administrator's rules and forms.

Internal Controls Over Financial Reporting

The design of internal controls over financial reporting ("ICFR") within the company is a management responsibility to provide reasonable assurance that the reliability of financial reporting and that the preparation of financial statements for external purposes is in accordance with generally accepted accounting principles of IFRS. While the CEO and CFO believe that the internal controls are adequate to provide the above information, the process to evaluate and document all policies and procedures that could impact financial reporting is continuously reviewed with consultation with the Audit Committee.

Internal Controls Over Financial Reporting (Continued)

Shareholders should be aware that Microbix is a small company without the department resources associated with larger firms. Management is using the Committee of Sponsoring Organization of the Treadway Commission ("COSO") Framework and has concluded that the Internal Control over Financial Reporting ("ICFR") as defined in NI 52-109 is effective as at the period ended December 31, 2017.

Examination by the Chief Executive Officer and the Chief Financial Officer showed that there were no changes to the internal controls over financial reporting during the period ended December 31, 2017 that have materially affected, or are reasonably thought to materially affect, the internal control over financial reporting.

ACCOUNTING PRONOUNCEMENTS ISSUED BUT NOT YET APPLIED

Certain new standards, interpretations, amendments and improvements to existing standards were issued by the International Accounting Standards Board ("IASB") or IFRS Interpretation Committee ("IFRIC") that are mandatory at certain dates or later. Management is still assessing the effects of the pronouncements on the Company. The standards impacted that may be applicable to the Company are following:

IFRS 15, Revenue from Contracts with Customers

IFRS 15, Revenue from Contracts with Customers ("IFRS 15") was issued by the IASB in May 2014. The core principle of the new standard is for companies to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services. The new standard will also result in enhanced disclosures about revenue, provide guidance for transactions that were not previously addressed comprehensively (for example, service revenue and contract modifications) and improve guidance for multiple-element arrangements. The new standard is effective for annual periods beginning on or after January 1, 2018. Earlier application is permitted. IFRS 15 supersedes the following standards: IAS 11 Construction Contracts, IAS 18 Revenue, IFRIC 13 Customer Loyalty Programmes, IFRIC 15 Agreements for the Construction of Real Estate, IFRIC 18 Transfers of Assets from Customers, and SIC-31 Revenue - Barter Transactions Involving Advertising Services.

The Company has commenced a review process to assess any impact on its current revenue recognition policies and reporting processes.

IFRS 16, Leases

On January 13, 2016, the IASB issued IFRS 16, which outlines requirements for lessees to recognize assets and liabilities for most leases. Lessees are required to recognize the lease liability for the obligations to make lease payments and a right-of-use asset for the right to use the underlying asset for the lease term. Lease liability is measured at the present value of lease payments to be made over the term of the lease. The right-of-use asset is initially measured at the amount of the lease liability and adjusted for prepayments, direct costs and incentives received.

The new standard will be effective for annual periods beginning on or after January 1, 2019. Early recognition is permitted, provided the new revenue standard, IFRS 15 Revenue from Contracts with Customers, has been applied, or is applied at the same date as IFRS 16. The Company has commenced a review process to assess any impact on its current revenue recognition policies and reporting processes.

IFRS 2, Share-based Payment (“IFRS 2”)

In June 2016, the IASB issued final amendments to IFRS 2, clarifying how to account for certain types of share-based payment transactions. The amendments, which were developed through the IFRS Interpretations Committee, provide requirements on the accounting for: (i) the effect of vesting and non-vesting conditions on the measurement of cash-settled share-based payments; (ii) share-based payment transactions with a net settlement feature for withholding tax obligations; and (iii) a modification to the terms and conditions of a share-based payment that changes the classifications of the transaction from cash-settled to equity-settled. The effective date for this standard is for reporting periods beginning on or after January 1, 2018, with earlier application permitted.

The Company has completed the review process to assess the impact and application of the aforementioned amendments and has determined it will have no impact on the Company.

IFRIC 22, Foreign Currency Transactions and Advance Consideration

In 2016, the IASB issued IFRIC Interpretation 22, Foreign Currency Transactions and Advance Consideration (“IFRIC 22”) which provides requirements about which exchange rate to use in reporting foreign currency transactions (such as revenue transactions) when payment is made or received in advance. IFRIC 22 is effective for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. On initial application, entities have the option to apply either retrospectively or prospectively. The Company is in the process of evaluating the impact of adopting these amendments on the Company’s consolidated financial statements.

Pursuant to National Instrument 51-102, Part 4, sub section 4.3(3)(a) issued by the Canadian Securities Administrators, if an audit has not performed a review of the interim financial statements, the interim financial statements must be accompanied by a notice indicating that they have not been reviewed by the auditor.

MICROBIX**CONSOLIDATED STATEMENTS OF FINANCIAL POSITION****Unaudited**

As at December 31, 2017 and September 30, 2017

| | As at December 31, 2017 | Canadian Funds As at September 30, 2017 |
|---|-------------------------------|--|
| ASSETS | | |
| CURRENT ASSETS | | |
| Cash | \$ 51,389 | \$ 54,460 |
| Accounts receivable | 1,575,827 | 1,337,488 |
| Inventory (Note 5) | 4,640,830 | 4,467,106 |
| Prepaid expenses and other assets (Note 6) | 93,856 | 152,989 |
| Investment tax credit receivable (Note 18) | 149,794 | 149,794 |
| TOTAL CURRENT ASSETS | 6,511,696 | 6,161,837 |
| LONG-TERM ASSETS | | |
| Deferred tax assets | 1,580,000 | 1,580,000 |
| Property, plant and equipment (Note 7) | 12,771,014 | 12,211,770 |
| Intangible assets (Note 8) | 6,571,478 | 6,484,004 |
| TOTAL LONG-TERM ASSETS | 20,922,492 | 20,275,774 |
| TOTAL ASSETS | \$ 27,434,188 | \$ 26,437,611 |
| LIABILITIES | | |
| CURRENT LIABILITIES | | |
| Accounts payable and accrued liabilities | \$ 1,809,680 | \$ 2,841,950 |
| Bank indebtedness | 360,000 | 1,355,000 |
| Current portion of finance lease obligation | 79,742 | 23,070 |
| Current portion of long-term debt (Note 10) | 336,480 | 536,480 |
| Current portion of debentures (Note 9) | 630,049 | 614,563 |
| Deferred revenue (Note 11) | 876,916 | 1,145,185 |
| TOTAL CURRENT LIABILITIES | 4,092,867 | 6,516,249 |
| Finance lease obligations | 314,008 | 74,327 |
| Non-convertible debenture (Note 9) | 797,153 | 802,819 |
| Convertible debentures (Note 9) | 1,276,719 | 1,268,623 |
| Long-term debt (Note 10) | 2,516,790 | 2,600,910 |
| TOTAL LONG-TERM LIABILITIES | 4,904,670 | 4,746,679 |
| TOTAL LIABILITIES | \$ 8,997,537 | \$ 11,262,928 |
| SHAREHOLDERS' EQUITY | | |
| SHARE CAPITAL (Note 12) | \$ 33,964,663 | \$ 31,299,416 |
| EQUITY COMPONENT OF | | |
| CONVERTIBLE DEBENTURES (Note 9) | 2,903,789 | 2,903,789 |
| CONTRIBUTED SURPLUS (Note 13) | 8,739,164 | 8,048,315 |
| ACCUMULATED DEFICIT | (27,170,965) | (27,076,837) |
| TOTAL SHAREHOLDERS' EQUITY | \$ 18,436,651 | \$ 15,174,683 |
| TOTAL LIABILITIES & SHAREHOLDERS' EQUITY | \$ 27,434,188 | \$ 26,437,611 |

Commitments and Contingencies (Note 26)

On behalf of the Board:

(Signed) "William J. Gastle"

 WILLIAM J. GASTLE
 DIRECTOR

(Signed) "Cameron L. Groome"

 CAMERON L. GROOME
 DIRECTOR

The accompanying notes and summary of significant accounting policies are an integral part of these consolidated financial statements.

MICROBIX

| CONSOLIDATED INTERIM STATEMENTS OF COMPREHENSIVE INCOME (LOSS) | | Unaudited |
|---|--------------------|-----------------------|
| For the Three Months Ended December 31 | | Canadian Funds |
| | 2017 | 2016 |
| SALES | | |
| Virology products and technologies | \$ 2,802,585 | \$ 1,886,824 |
| Royalties | 82,982 | 65,678 |
| TOTAL SALES | 2,885,567 | 1,952,502 |
| COST OF GOODS SOLD | | |
| Virology products and technologies (Note 17) | 1,551,141 | 1,115,610 |
| Royalties | 15,440 | 22,363 |
| TOTAL COST OF GOODS SOLD | 1,566,581 | 1,137,973 |
| GROSS MARGIN | 1,318,987 | 814,529 |
| EXPENSES | | |
| Selling and business development (Note 17) | 146,163 | 142,932 |
| General and administrative (Note 17) | 805,279 | 776,956 |
| Research and development (Note 17) | 252,283 | 201,150 |
| Financial expenses (Note 19) | 209,390 | 218,897 |
| NET COMPREHENSIVE OPERATING INCOME (LOSS) | | |
| BEFORE DEBT RESTRUCTURING AND SETTLEMENT EXPENSES | (94,128) | (525,406) |
| Debt restructuring expense (Note 9) | - | 2,582,526 |
| Settlement expense (Note 27) | - | 258,540 |
| NET COMPREHENSIVE OPERATING INCOME (LOSS) FOR THE PERIOD | (94,128) | (3,366,472) |
| INCOME TAXES | | |
| Deferred income taxes | - | (150,000) |
| Current income taxes | - | - |
| NET COMPREHENSIVE INCOME (LOSS) FOR THE PERIOD | \$ (94,128) | \$ (3,216,472) |
| NET COMPREHENSIVE LOSS PER SHARE | | |
| Basic (Note 16) | \$ (0.001) | \$ (0.038) |
| Diluted (Note 16) | \$ (0.001) | \$ (0.038) |

The accompanying notes and summary of significant accounting policies are an integral part of these consolidated financial statements.

MICROBIX**CONSOLIDATED INTERIM STATEMENTS OF CASH FLOWS****Unaudited****For the Three Months Ended December 31****Canadian Funds****2017****2016****OPERATING ACTIVITIES**

| | | |
|---|-------------|----------------|
| Net comprehensive income (loss) for the period | \$ (94,128) | \$ (3,216,472) |
| Items not affecting cash | | |
| Amortization and depreciation | 161,887 | 101,465 |
| Accretion of debentures | 36,812 | 30,293 |
| Stock options expense (Note 15) | 114,813 | 55,576 |
| Deferred revenue | (268,268) | 224,186 |
| Debt restructuring expense (Note 27) | - | 2,582,526 |
| Deferred tax asset | - | (150,000) |
| Change in non-cash working capital balances (Note 18) | (1,385,201) | 681,968 |

| | | |
|--|--------------------|----------------|
| CASH PROVIDED BY (USED IN) OPERATING ACTIVITIES | (1,434,085) | 309,542 |
|--|--------------------|----------------|

INVESTING ACTIVITIES

| | | |
|---|-----------|-----------|
| Purchase of property and equipment (Note 7) | (342,504) | (38,949) |
| Additions from internal development of intangible assets (Note 8) | (152,942) | (166,792) |

| | | |
|--|------------------|------------------|
| CASH USED IN INVESTING ACTIVITIES | (495,446) | (205,741) |
|--|------------------|------------------|

FINANCING ACTIVITIES

| | | |
|---|-----------|-----------|
| Repayments of long-term debt (Note 10) | (84,120) | (81,925) |
| Repayments of convertible and non-convertible debentures (Note 9) | (21,711) | (18,964) |
| Repayments of shareholders' loans | (200,000) | (200,000) |
| Repayments of finance lease | (13,993) | (1,647) |
| Proceeds (repayments) of credit facility (Note 10) | (995,000) | 195,000 |
| Proceeds from exercise of stock options | 104,000 | - |
| Issue of common shares, net of issue costs | 3,137,283 | - |

| | | |
|--|------------------|------------------|
| CASH PROVIDED BY (USED IN) FINANCING ACTIVITIES | 1,926,459 | (107,536) |
|--|------------------|------------------|

| | | |
|---|-------------------|-------------------|
| NET CHANGE IN CASH DURING THE PERIOD | \$ (3,071) | \$ (3,735) |
|---|-------------------|-------------------|

| | | |
|-----------------------------------|---------------|--------------|
| CASH - BEGINNING OF PERIOD | 54,460 | 5,415 |
|-----------------------------------|---------------|--------------|

| | | |
|-----------------------------|------------------|-----------------|
| CASH - END OF PERIOD | \$ 51,389 | \$ 1,680 |
|-----------------------------|------------------|-----------------|

The accompanying notes and summary of significant accounting policies are an integral part of these consolidated financial statements.

MICROBIX
CONSOLIDATED INTERIM STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY
Unaudited
As at December 31, 2017 and September 30, 2017
Canadian Funds

| | SHARE CAPITAL (Note 12) | | CONTRIBUTED SURPLUS | DEFICIT | EQUITY COMPONENT OF DEBENTURE | TOTAL SHAREHOLDERS' EQUITY |
|---|-------------------------|---------------------|------------------------|-----------------------|-------------------------------------|----------------------------------|
| | NUMBER OF SHARES | STATED CAPITAL | | | | |
| BALANCE, SEPTEMBER 30, 2016 | 84,704,257 | \$31,299,416 | \$4,937,649 | \$(23,296,749) | \$2,351,425 | \$15,291,741 |
| Stock option expense | | | 55,576 | | | 55,576 |
| Issuance of warrants pursuant to refinancing of convertible debentures | | | 245,860 | | | 245,860 |
| Conversion of a convertible debenture to a non-convertible debenture | | | 86,680 | | (86,680) | |
| Extinguishment of convertible debentures | | | 2,264,745 | | (2,264,745) | |
| Refinancing of convertible debentures | | | | | 2,903,789 | 2,903,789 |
| Net comprehensive income (loss) for the period | | | | (3,216,472) | | (3,216,472) |
| BALANCE, DECEMBER 31, 2016 | 84,704,257 | \$31,299,416 | \$7,590,510 | \$(26,513,221) | \$2,903,789 | \$15,280,494 |
| Stock option expense | | | 429,510 | | | 429,510 |
| Extinguishment of convertible debenture | | | 28,295 | | | 28,295 |
| Net comprehensive income (loss) for the period | | | | (563,616) | | (563,616) |
| BALANCE, SEPTEMBER 30, 2017 | 84,704,257 | \$31,299,416 | \$8,048,315 | \$(27,076,837) | \$2,903,789 | \$15,174,683 |
| Stock option expense | | | 114,813 | | | 114,813 |
| Share Issuance pursuant to Stock Options Exercised | 400,000 | 181,516 | (77,516) | | | 104,000 |
| Issue of Warrants pursuant to Private Placement | | | 743,905 | | | 743,905 |
| Share Issuance pursuant to Private Placement | 11,666,633 | 2,756,085 | | | | 2,756,085 |
| Share Issue Costs pursuant to Private Placement | | (272,354) | (90,353) | | | (362,707) |
| Net comprehensive income (loss) for the period | | | | (94,128) | | (94,128) |
| BALANCE, DECEMBER 31, 2017 | 96,770,890 | \$33,964,663 | \$8,739,164 | \$(27,170,965) | \$2,903,789 | \$18,436,651 |

The accompanying notes and summary of significant accounting policies are an integral part of these consolidated financial statements.

1. NATURE OF THE BUSINESS

Microbix Biosystems Inc. develops and commercializes proprietary biological and technology solutions for human health and wellbeing. Microbix manufactures a wide range of critical biological materials for the global diagnostics industry, notably antigens used in immunoassays or quality assessment and proficiency testing controls. Its fiscal 2017 revenues of \$10.2 million were largely from these product lines.

The company also applies its biological expertise to develop other innovative and proprietary technologies and products. Its development pipeline currently includes two such proprietary products: (1) Kinlytic® Urokinase for injection, a thrombolytic biologic drug used to treat blood clots, and (2) LumiSort™ cell-sorting, a technology for ultra-rapid and efficient sorting of somatic cells that can be used to enrich cell populations of interest, such as in sexing semen.

The Company operates the Virology Business in its owned manufacturing facility at 265 Watline Avenue, Mississauga, Ontario, L4Z 1P3.

2. BASIS OF PREPARATION

The Company's management prepared these consolidated financial statements in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB") applicable to the preparation of financial statements for the three months ended December 31, 2017. The Board of Directors approved these consolidated financial statements on February 12, 2018.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES**Basis of Measurement**

The consolidated financial statements have been prepared under the historical cost convention, except for the revaluation of certain financial assets and financial liabilities to fair value. For each entity, the Company determines the functional currency and items included in the financial statements of each entity are measured using the functional currency, which represents the currency of the primary economic environment in which each entity operates. The consolidated financial statements are presented in Canadian dollars.

Basis of consolidation

These consolidated financial statements include the accounts of the Company and its wholly owned subsidiary, Crucible Biotechnologies Limited, which the Company has control. Control exists when the entity is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through its power over the entity. The non-controlling interest component, if any, of the Company's subsidiaries is included in equity.

The financial statements of the Company's subsidiary is prepared for the same reporting period as the Company, using consistent accounting policies. All intra-company balances, transactions, unrealized gains and losses resulting from intra-company transactions and dividends are eliminated in full.

There has been no business activity in the subsidiary during the three months ended December 31, 2017 and 2016. All significant intercompany transactions and balances have been eliminated upon consolidation.

Use of estimates and judgments

The preparation of financial statements requires management to make estimates and judgements 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 could be material.

Key areas of managerial judgements and estimates are as follows:

- i) Property, plant and equipment:
Measurement of property, plant and equipment involves the use of estimates for determining the expected useful lives of depreciable assets. Management's judgement is also required to determine depreciation methods and an asset's residual value and whether an asset is a qualifying asset for the purposes of capitalizing borrowing costs.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**Use of estimates and judgements (Continued)**

ii) Internally generated intangible assets:

Management monitors the progress of each internal research and development project. Significant judgement is required to distinguish between the research and development phases. Development costs are recognized as an asset when the following criteria are met: (i) technical feasibility; (ii) management's intention to complete the project; (iii) the ability to use or sell; (iv) the ability to generate future economic benefits; (v) availability of technical and financial resources; (vi) ability to measure the expenditures reliably. Research costs are expensed as incurred. Management also monitors whether the recognition requirements for development assets continue to be met and whether there are any indicators that capitalized costs may be impaired. The amortization period and amortization method for intangible assets with finite useful lives are reviewed at least at the end of each reporting period.

iii) Financial assets and liabilities:

Estimates and judgements are also made in the determination of fair value of financial assets and liabilities and include assumptions and estimates regarding future interest rates, the relative creditworthiness of the Company to its counterparties, the credit risk of the Company's counterparties relative to the Company, the estimated future cash flows and discount rates.

iv) Income taxes:

The Company recognizes deferred tax assets, related tax-loss carry-forwards 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.

v) Fair value of share-based compensation:

The Company measures the cost of equity-settled transactions with employees by reference to the fair value of the equity instruments at the date on which they are granted. Estimating fair value for share-based compensation 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, dividend yield and forfeiture rates and making assumptions about them.

vi) Impairments:

The recoverable amount of intangible assets and property, plant and equipment is based on estimates and assumptions regarding the expected market outlook and cash flows from each CGU.

Revenue Recognition

Revenues from product sales are recognized when persuasive evidence of an arrangement exists, the product is shipped, received or accepted by the customer, there are no future performance obligations, the purchase price is fixed and determinable, and collectability is reasonably assured.

Revenues from licensing are recognized when the service is rendered or the deliverables are substantially complete and other revenue recognition criteria are met.

For upfront, non-refundable payments received in accordance with the execution of licensing and collaboration agreements, revenue is deferred and recognized over the performance period, the period over which the Company maintains substantive contractual obligations.

Amounts the Company expects to earn in the current year are included in the current portion of deferred revenue and amounts expected to be earned in subsequent periods are included in deferred revenue. The term over which upfront fees are recognized is revised if the period over which the Company maintains substantive contractual obligations changes.

Milestone payments are immediately recognized as licensing revenue when the condition is met, if the milestone is not a condition to future deliverables and collectability is reasonably assured. Otherwise, they are recognized over the remaining term of the agreement or the performance period.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**Cash**

Cash consists of cash on hand and deposits with banks and investments in highly liquid instruments with original maturities of three months or less. There are no cash equivalents held at December 31, 2017 or 2016.

Financial assets and liabilities

All financial instruments, including derivatives, are included on the consolidated statement of financial position and are measured either at fair market value or, in limited circumstances, at cost or amortized cost. Subsequent measurement and recognition of the changes in fair value of financial instruments depends upon their initial classifications as follows:

- Held-for-trading financial assets, measured at fair value with subsequent changes in fair value recognized in current period net income;
- Held-to-maturity assets, loans and receivables and other financial liabilities, initially measured at fair value and subsequently measured at amortized cost with changes recognized in current period net income; and
- Available-for-sale financial assets, measured at fair value with subsequent gains or losses included in other comprehensive income until the asset is removed from the consolidated statements of financial position.

The following summarizes the Company's classification and measurement of financial assets and liabilities as at December 31:

| | Classification | Measurement | 2017 | 2016 |
|--|-----------------------|----------------|--------------|--------------|
| Financial assets: | | | | |
| Cash | Held-for-trading | Fair value | \$ 51,389 | \$ 1,680 |
| Accounts receivable | Loans and receivables | Amortized cost | 1,575,827 | 1,081,314 |
| Financial liabilities: | | | | |
| Accounts payable and accrued liabilities | Other liabilities | Amortized cost | \$ 1,809,680 | \$ 1,965,191 |
| Bank Indebtedness | Other liabilities | Amortized cost | 360,000 | 720,000 |
| Deferred revenue | Other liabilities | Amortized cost | 876,916 | 907,680 |
| Finance lease obligation | Other liabilities | Amortized cost | 393,750 | 11,012 |
| Non-convertible debentures | Other liabilities | Amortized cost | 1,172,517 | 1,334,697 |
| Convertible debentures | Other liabilities | Amortized cost | 1,531,404 | 1,469,039 |
| Long-term debt | Other liabilities | Amortized cost | 2,853,270 | 3,915,570 |
| Total Financial liabilities | | | \$ 8,997,537 | \$ 9,603,189 |

Transaction costs that are directly attributable to the acquisition or issuance of financial assets or financial liabilities, other than financial assets and financial liabilities measured at fair value through profit and loss ("FVTPL"), are accounted for as part of the carrying amount of the respective asset or liability at inception. Transaction costs related to financial instruments measured at amortized cost are amortized using the effective interest rate over the anticipated life of the related instrument.

Transaction costs on financial assets and financial liabilities measured at FVTPL are expensed in the period incurred. Financial assets are derecognized when the contractual rights to the cash flows from financial assets expire or have been transferred. All derivative instruments, including embedded derivatives, are recorded in the financial statements at fair value.

Inventories

Inventory is carried at the lower of cost and market. Cost consists of direct materials, direct labour and an overhead allocation and is determined on a first-in, first-out basis. Market is defined as net realizable value, which is defined as the summation of the estimated selling price less the cost to complete less the cost to sell. Management reviews its reserve for obsolete inventory annually for finished goods and work-in-process.

Property, plant and equipment

Property and equipment are measured at cost less accumulated depreciation and impairment (if any). Cost includes the cost of material, labour and other costs directly attributable to bringing the asset to a working condition for its intended use.

Depreciation is calculated at rates which will reduce the original cost to estimated residual value over the estimated useful life of each asset. Depreciation commences once the asset is available for use.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**Property, plant and equipment (Continued)**

Depreciation is provided for at the following basis and rates:

| | |
|------------------------------------|----------------------------|
| Research and development equipment | Declining balance, 10-100% |
| Other equipment and fixtures | Declining balance, 10-30% |
| Buildings | Straight line, 50 years |

Land is not depreciated. Depreciation methods, useful lives and residual values are reviewed at each reporting date and adjusted prospectively, if appropriate.

Finance lease obligation

Leases that transfer substantially all of the benefits and risks of ownership of the asset to the Company are accounted for as finance leases. At the time a finance lease is entered into, an asset is recorded together with its related long-term obligation, reflecting the fair value of future lease payments, discounted at the appropriate interest rates. Finance lease obligations are amortized over their estimated useful lives at the same rates used for other equipment and fixtures. All other leases are classified as operating leases and expensed on a straight-line basis.

Intangible assets

Intangible assets represent technology costs, patents and trademarks, and rights and licenses. Each is recorded at cost and is amortized on a straight-line basis over the term of the agreements or over the useful life of the asset. Amortization commences when the intangible asset is available for use. Intangible assets with definite lives but not yet available for use are assessed annually for impairment.

Impairment of long-lived assets

An impairment charge is recognized for long-lived assets, including intangible assets with definite lives, when an event or change in circumstances indicates that the assets' carrying value may not be recoverable. The impairment loss is calculated as the difference between the carrying value of the asset and the recoverable amount. The recoverable amount is the higher of the fair value less costs to sell and value in use.

Management has determined that no long-lived assets of the Company as at December 31, 2017 have met the criteria for impairment.

Borrowing costs

Borrowing costs consist of interest and other costs that an entity incurs in connection with the borrowing of funds. Borrowing costs directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are capitalized as part of the cost of the asset. All other borrowing costs are expensed in the period they are incurred.

Share-based compensation

The Company applies the fair value method of accounting for share-based compensation for awards granted to officers, directors and employees of the Company. The fair value of the award at the time of granting is determined using the Black-Scholes option pricing model, and recognized as a compensation expense over the vesting period with an offsetting amount recorded to contributed surplus. Each tranche in an award is considered a separate award with its own vesting period and grant date fair value.

Share options issued to consultants of the Company are based on the fair value of the services provided. The amount of the compensation cost recognized at any date at least equals the value of the portion of the options vested at that date. When stock options are exercised, the consideration paid by employees or directors, together with the related amount in contributed surplus, is credited to share capital. When an employee leaves the Company, vested options must be exercised within 90 days, or the options expire. Any options that are unvested are reversed in the period that the employee leaves. A forfeiture rate is incorporated into the Company's assumptions. Forfeitures are estimated at the time of grant and are based on historical experience. To the extent that the actual forfeiture rate is different from the Company's estimate, share-based compensation related to these awards will be different from the Company's estimate and forfeiture rates for subsequent periods are revised.

Foreign currency translation

Foreign currency denominated revenues and expenses are translated by use of the exchange rate in effect at the end of the month in which the transaction occurs. Foreign currency denominated monetary assets and liabilities are translated at the year-end date. Exchange gains and losses arising on these transactions are included in the consolidated statements of comprehensive income for the period.

3. SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES (Continued)**Income (loss) per common share**

The Company calculates basic income per share amounts for profit or loss attributable to ordinary equity holders. Basic income per share is calculated using the weighted average number of common shares outstanding during the period. Diluted income per share is calculated in the same manner as basic income per share except for adjusting the profit or loss attributable to ordinary equity holders and the weighted average number of shares outstanding for the effects of all dilutive potential ordinary shares.

Deferred taxes

Deferred income tax assets and liabilities are recognized for the estimated income tax consequences attributable to differences between financial statement carrying amounts of assets and liabilities and their respective income tax bases. Deferred income tax assets are recognized to the extent that it is probable that future taxable income will be available against which temporary differences can be utilized. Deferred income tax assets and liabilities are measured using tax rates expected to be in effect when the temporary differences are expected to be recovered or settled. The effects of changes in income tax rates are reflected in deferred income tax assets and liabilities in the year that the rate changes are substantively enacted, with a corresponding charge to income. The amount of deferred tax assets recognized is limited to the amount that is more likely than not to be realized.

Research and development expenses

Costs associated with research and development activities are expensed during the year in which they are incurred net of tax credits earned, except where product development costs meet the criteria under IFRS for deferral and amortization.

Investment tax credits

The Company is entitled to Canadian federal and provincial investment tax credits which are earned as a percentage of eligible research and development expenditures incurred in each taxation year. Investment tax credits are accounted for as a reduction of the related expenditure for items of a current nature and a reduction of the related asset cost for items of a long-term nature. These credits are only recognized to the extent that it is probable that there will be sufficient taxable profits against which to utilize the benefits of the credits in the foreseeable future.

4. ACCOUNTING PRONOUNCEMENTS ISSUED BUT NOT YET APPLIED

Certain new standards, interpretations, amendments and improvements to existing standards were issued by the International Accounting Standards Board ("IASB") or IFRS Interpretation Committee ("IFRIC") that are mandatory at certain dates or later. Management is still assessing the effects of the pronouncements on the Company. The standards impacted that may be applicable to the Company are following:

IFRS 15, Revenue from Contracts with Customers

IFRS 15, Revenue from Contracts with Customers ("IFRS 15") was issued by the IASB in May 2014. The core principle of the new standard is for companies to recognize revenue to depict the transfer of goods or services to customers in amounts that reflect the consideration to which the company expects to be entitled in exchange for those goods or services. The new standard will also result in enhanced disclosures about revenue, provide guidance for transactions that were not previously addressed comprehensively (for example, service revenue and contract modifications) and improve guidance for multiple-element arrangements. The new standard is effective for annual periods beginning on or after January 1, 2018. Earlier application is permitted. IFRS 15 supersedes the following standards: IAS 11 Construction Contracts, IAS 18 Revenue, IFRIC 13 Customer Loyalty Programmes, IFRIC 15 Agreements for the Construction of Real Estate, IFRIC 18 Transfers of Assets from Customers, and SIC-31 Revenue - Barter Transactions Involving Advertising Services.

The Company has commenced a review process to assess any impact on its current revenue recognition policies and reporting processes.

4. ACCOUNTING PRONOUNCEMENTS ISSUED BUT NOT YET APPLIED (Continued)**IFRS 16, Leases**

On January 13, 2016, the IASB issued IFRS 16, which outlines requirements for lessees to recognize assets and liabilities for most leases. Lessees are required to recognize the lease liability for the obligations to make lease payments and a right-of-use asset for the right to use the underlying asset for the lease term. Lease liability is measured at the present value of lease payments to be made over the term of the lease. The right-of-use asset is initially measured at the amount of the lease liability and adjusted for prepayments, direct costs and incentives received.

The new standard will be effective for annual periods beginning on or after January 1, 2019. Early recognition is permitted, provided the new revenue standard, IFRS 15 Revenue from Contracts with Customers, has been applied, or is applied at the same date as IFRS 16. The Company has commenced a review process to assess any impact on its current revenue recognition policies and reporting processes.

IFRS 2, Share-based Payment ("IFRS 2")

In June 2016, the IASB issued final amendments to IFRS 2, clarifying how to account for certain types of share-based payment transactions. The amendments, which were developed through the IFRS Interpretations Committee, provide requirements on the accounting for: (i) the effect of vesting and non-vesting conditions on the measurement of cash-settled share-based payments; (ii) share-based payment transactions with a net settlement feature for withholding tax obligations; and (iii) a modification to the terms and conditions of a share-based payment that changes the classifications of the transaction from cash-settled to equity-settled. The effective date for this standard is for reporting periods beginning on or after January 1, 2018, with earlier application permitted.

The Company has completed the review process to assess the impact and application of the aforementioned amendments and has determined it will have no impact on the Company.

IFRIC 22, Foreign Currency Transactions and Advance Consideration

In 2016, the IASB issued IFRIC Interpretation 22, Foreign Currency Transactions and Advance Consideration ("IFRIC 22") which provides requirements about which exchange rate to use in reporting foreign currency transactions (such as revenue transactions) when payment is made or received in advance. IFRIC 22 is effective for annual periods beginning on or after January 1, 2018, with earlier adoption permitted. On initial application, entities have the option to apply either retrospectively or prospectively. The Company is in the process of evaluating the impact of adopting these amendments on the Company's consolidated financial statements.

5. INVENTORIES

Inventories as at December 31 consist of the following:

| | 2017 | 2016 |
|-----------------|---------------------|---------------------|
| Raw material | \$ 550,198 | \$ 389,109 |
| Work in process | 1,421,663 | 710,409 |
| Finished goods | 2,668,969 | 2,574,906 |
| | \$ 4,640,830 | \$ 3,674,424 |

During the three months ended December 31, 2017, inventories in the amount of \$1,566,581, (2016 - \$1,137,973) were recognized as an expense through cost of sales. The allowance for inventory impairment as at December 31, 2017 was \$20,000 (2016 - \$30,561).

MICROBIX**NOTES TO THE UNAUDITED CONSOLIDATED INTERIM FINANCIAL STATEMENTS** Canadian Funds

As at and for the three months ended December 31, 2017 and 2016

6. PREPAID EXPENSES AND OTHER ASSETS

Prepaid expenses and other assets as at December 31, 2017 were \$93,856 (2016 - \$62,376), consisting of insurance policy premiums, deposits for trade shows and other prepaid amounts.

7. PROPERTY, PLANT, AND EQUIPMENT

The freehold land and buildings have been pledged as security for bank loans under a mortgage (see Note 10). Property plant and equipment consists of:

| | Building | Research & development equipment | Other equipment & fixtures | Land | Total |
|--|--------------------|----------------------------------|----------------------------|------------------|---------------------|
| <u>Cost</u> | | | | | |
| Balance, Sept 30, 2017 | 4,565,379 | 6,939,732 | 4,605,040 | 800,000 | 16,910,151 |
| Additions | - | 36,564 | 616,285 | - | 652,849 |
| Disposals | - | - | - | - | - |
| Balance, Dec 31, 2017 | 4,565,379 | 6,976,296 | 5,221,325 | 800,000 | 17,563,000 |
| <u>Accumulated depreciation</u> | | | | | |
| Balance, Sept 30, 2017 | 1,247,532 | 582,968 | 2,867,881 | - | 4,698,381 |
| Disposals | - | - | - | - | - |
| Depreciation | 38,028 | 5,166 | 50,411 | - | 93,605 |
| Balance, Dec 31, 2017 | 1,285,560 | 588,134 | 2,918,292 | - | 4,791,986 |
| <u>Net book value</u> | | | | | |
| Balance, Sept 30, 2017 | 3,317,847 | 6,356,764 | 1,737,159 | 800,000 | 12,211,770 |
| Balance, Dec 31, 2017 | \$3,279,819 | \$6,388,162 | \$2,303,033 | \$800,000 | \$12,771,014 |

Included in research and development equipment is \$6,205,829 not yet available for use. Included in these amounts is directly attributable interest from borrowings to finance these asset additions of \$454,405 since inception. These assets are not yet subject to depreciation.

MICROBIX

NOTES TO THE UNAUDITED CONSOLIDATED INTERIM FINANCIAL STATEMENTS Canadian Funds As at and for the three months ended December 31, 2017 and 2016

8. INTANGIBLE ASSETS

Intangible assets are depreciated on a straight line basis at the following rates:

| | |
|--|----|
| License agreement, LumiSort™ (Note 8a) | 5% |
| Technology investments: | |
| LumiSort™ (Note 8a) | 5% |
| Kinlytic® (Note 8b) | 0% |
| Bioreactor (Note 8c) | 7% |

Intangible assets consist of:

| | Capitalized development costs | | Patents and trademarks | | Licenses | Total |
|--------------------------------------|-------------------------------|--------------------|------------------------|--------------------|------------------|--------------------|
| | LumiSort™ (a) | Bioreactor (c) | Kinlytic® (b) | LumiSort™ (a) | LumiSort™ (a) | |
| Cost | | | | | | |
| Balance, as at September 30, 2017 | 30,532 | 2,088,573 | 3,078,586 | 2,115,236 | 278,528 | 7,591,455 |
| Additions from internal developments | - | - | - | 155,756 | - | 155,756 |
| Balance, December 31, 2017 | 30,532 | 2,088,573 | 3,078,586 | 2,270,992 | 278,528 | 7,747,211 |
| Accumulated amortization | | | | | | |
| Balance at September 30, 2017 | 6,748 | 11,603 | - | 831,999 | 257,101 | 1,107,451 |
| Amortization expense | 238 | 34,809 | - | 27,879 | 5,356 | 68,282 |
| Balance, December 31, 2017 | 6,986 | 46,412 | - | 859,878 | 262,458 | 1,175,734 |
| Net book value | | | | | | |
| Balance, September 30, 2017 | 23,784 | 2,076,970 | 3,078,586 | 1,283,237 | 21,427 | 6,484,004 |
| Balance, December 31, 2017 | \$23,546 | \$2,042,161 | \$3,078,586 | \$1,411,114 | \$16,071 | \$6,571,478 |

a) Lumisort™

The Company acquired a license agreement from Sequent Biotechnologies Inc. ("Sequent"), a biotechnology company solely involved in the development and commercialization of the LumiSort™ technology under license. New intellectual property with the issue of patents has resulted from this research program. These assets are in the process of being developed and new patents are pending and under development.

The recoverable amount of the Lumisort intangible has been determined based on its fair value less cost to sell. Key assumptions include growth rates in line with industry expectations and a discount rate determined based on the Company's best estimate of a risk adjusted discount rate.

b) Kinlytic®

The Company acquired the assets and rights pertaining to development, production, and licensing of Kinlytic® from ImaRX Therapeutics, Inc. in 2008. These assets are in the process of being developed and new patents are pending and under development.

The recoverable amount of the Kinlytic® intangible has been determined based on its fair value less cost to sell. This estimate uses risk-adjusted cash flow projections based on financial budgets.

Management made these assumptions based on probabilities of technical, regulatory and clinical acceptances and financial support. Management believes that any reasonably-possible change in the key assumptions on which the recoverable amount is based would not cause the carrying amount to exceed its recoverable amount. The discount rate has been determined based on the Company's best estimate of a risk adjusted discount rate.

As at and for the three months ended December 31, 2017 and 2016
8. INTANGIBLE ASSETS (Continued)
c) Bioreactor

The Company has internally developed an improved bioreactor production process ("Bioreactor") to increase the efficiency and output of manufacturing certain virology products.

9. DEBENTURES

The Company has convertible and non-convertible debentures issued and outstanding as at December 31, 2017. The carrying values of the debt component of these debentures are as follows:

| | Non-convertible Debentures | | Total Non-convertible Debentures | Convertible Debentures | | | Total Convertible Debentures |
|---|-------------------------------|------------------|-------------------------------------|------------------------|------------------|------------------|---------------------------------|
| | (a) | (b) | | (c) | (d) | (e) | |
| Date of issue | Jan, 2014 | Apr, 2017 | | Oct, 2016 | Oct, 2016 | Oct, 2016 | |
| Face value | \$ 2,000,000 | \$ 500,000 | \$ 2,500,000 | \$ 1,500,000 | \$ 500,000 | \$ 2,500,000 | \$ 4,500,000 |
| Liability component at the date of issue | 928,373 | 268,955 | - | 461,550 | 223,050 | 780,750 | |
| Balance, September 30, 2017 | 894,955 | 275,162 | 1,170,117 | 470,692 | 247,265 | 797,931 | 1,515,888 |
| Accretion | 18,119 | 5,993 | 24,112 | 2,814 | 7,420 | 5,282 | 15,516 |
| Repayments | (21,712) | - | (21,712) | - | - | - | - |
| Balance, December 31, 2017 | 891,362 | 281,155 | 1,172,517 | 473,506 | 254,685 | 803,213 | 1,531,404 |
| Less: current portion | 94,209 | 281,155 | \$ 375,364 | - | 254,685 | - | \$ 254,685 |
| Non-current portion | 797,153 | - | \$ 797,153 | 473,506 | - | 803,213 | \$ 1,276,719 |
| Balance, December 31, 2017 | 891,362 | 281,155 | 1,172,517 | 473,506 | 254,685 | 803,213 | 1,531,404 |
| Equity component reclassified to contributed surplus upon extinguishment | - | 28,295 | \$ 28,295 | 916,971 | 111,042 | 1,236,732 | \$ 2,264,745 |
| Equity component at December 31, 2017 | - | - | - | 574,435 | 631,222 | 1,698,132 | \$ 2,903,789 |
| Loss / (gain) on date of extinguishment - Oct 2016 | - | 197,578 | \$ 197,578 | 494,575 | 361,460 | 1,528,913 | \$ 2,384,948 |
| Loss / (gain) on date of extinguishment - April 2017 | - | (202,750) | \$ (202,750) | - | - | - | \$ - |
| Conversion price per per common share | \$ - | \$ - | | \$ 0.23 | \$ 0.23 | \$ 0.23 | |
| Effective interest rate charged | 25.69% | 30.20% | | 31.07% | 30.20% | 30.85% | |
| Payment frequency | Quarterly | Quarterly | | Quarterly | Quarterly | Quarterly | |
| Maturity of financial instrument | Jan, 2029 | Apr, 2022 | | Jan, 2029 | Feb, 2022 | Sep, 2028 | |
| Stated interest rate | 9% | 12% | | 9% | 9% | 9% | |
| Terms of repayment | Principal and interest | Interest only | | Interest only | Interest only | Interest only | |
| Blended quarterly repayment | \$ 61,071 | N/A | | N/A | N/A | N/A | |

9. DEBENTURES (Continued)

As discussed in note 10, the Company arranged a new secured revolving credit facility jointly with The Toronto-Dominion Bank ("TD Bank") and Export Development Canada ("EDC"). To accommodate the additional security required by TD Bank and EDC, effective October 12, 2016, the Company negotiated amended terms with the holders of its issued and outstanding convertible debentures. The following debentures were amended: \$2,500,000 debenture (e) above, \$1,500,000 debenture (c) above, \$500,000 (b) above and \$500,000 (d) above, in exchange for reducing their security position to one of unlimited subordination to the credit facility lenders.

The \$2,500,000 debenture, (e) above, maturing in 2028 was originally convertible at \$0.65 per common share, and the \$1,500,000 debenture, (c) above, maturing in 2029 was originally convertible at \$0.35 per common share. The conversion price for both of these debentures has been amended to \$0.23 per common share, and these debentures are now subject to restricted conversion privileges of a combined total of 1 million shares per year for the next five years, with the remaining balances being eligible for conversion through the end of their expiry dates in 2028 and 2029, respectively.

The two \$500,000 debentures, (b) and (d) above, were originally convertible at \$0.90 per common share and matured on October 12, 2016 and February 15, 2017, respectively. The first \$500,000 debenture, (b) above has been modified to extend its maturity date to April 30, 2017 and was modified to become non-convertible. In addition, the stated interest rate was modified from 9% to 12% for the remaining term (see paragraph below for further details on this debenture). The second \$500,000 debenture, (d) above, has been modified to extend its maturity date to February 15, 2022, and the conversion price has been modified from \$0.90 to \$0.23 per common share. The debenture is now callable at the option of the holder at any time after February 15, 2017 for outstanding principal and accrued interest. In addition, the debenture holder of both \$500,000 debentures (b) and (d) received 1.5 million common share purchase warrants, with an exercise price of \$0.23 per common share and a term of five years.

The Company has accounted for the modifications to each of the debentures as an extinguishment with the recognition of a new instrument. Upon extinguishment of the debentures, the Company has recognized a non-cash loss of \$2,379,776 in the comprehensive consolidated statement of income (loss). The Company measured the non-cash loss based on the change in fair value of the debentures under the original and modified terms. In addition, a value of \$245,860 has been ascribed to warrants issued at the time of the grant. The value is determined using the Black-Scholes option pricing model, which is affected by the Company's share price as well as assumptions regarding a number of subjective variables.

On April 28, 2017, the Company announced it has reached an agreement with one of its debenture holders to extend the maturity date on the \$0.5 million non-convertible debenture set to mature on April 30, 2017, (b) above, to April 30, 2022. The debenture is callable at the option of the holder upon sixty days written notice to the Company. The Company has accounted for the modifications to each of the debentures as an extinguishment with the recognition of a new instrument. Upon extinguishment of the debenture, the Company has recognized a non-cash gain of \$202,750 in the consolidated statement of income and comprehensive income. In addition, as part of the amendment, the Company amended the terms of 300,000 outstanding common share purchase warrants held by the debenture holder. The terms of the warrants were modified to extend the life of the warrants from August 21, 2019 to August 21, 2022 and modify the exercise price from \$0.55 to \$0.25 per share. The modification of the debenture was accounted for as an extinguishment with recognition of a new instrument. In addition, the modification of the warrants resulted in a non-cash loss of \$28,295.

The debentures denoted as (a), (c), and (e) above are secured against the real property and the personal property of the Company including, without limiting the foregoing, a registered second mortgage on the property at 265 Watline Avenue, Mississauga, Ontario, in favour of the holder, its successors and assigns subordinate only to indebtedness to a Canadian chartered bank or similar financial institution on normal commercial terms up to their maximum principal. The debentures denoted as (b) and (d) are secured by a subordinated security agreement covering all of the Company's property and assets.

Convertible debentures contain two components: liability and equity elements. The equity element is presented in equity under the heading of "equity component of debentures". Convertible debentures are initially accounted for in accordance with their substance and are presented in the consolidated financial statements in their component parts measured at the time of issue. The debt components were valued first with the residual to shareholders' equity. The convertible debentures are convertible at the option of the holder, at any time, into fully paid and non-assessable common shares of the Company at the conversion price then in effect.

All of the debentures were issued to shareholders of the Company. A holder of a debenture has an economic interest in future earnings of the Lumisort asset and will receive a distribution equal to 10% of any future earnings that are derived from the Lumisort asset. Over the term of the convertible debentures, the debt components will be accreted to the face value of the debentures by the recording of additional interest expense using the effective interest rate, as detailed above.

MICROBIX

NOTES TO THE UNAUDITED CONSOLIDATED INTERIM FINANCIAL STATEMENTS Canadian Funds

As at and for the three months ended December 31, 2017 and 2016

10. LONG-TERM DEBT, BANK INDEBTEDNESS AND OTHER DEBT

- a) The Company has term loans with the Business Development Bank ("BDC") for a variety of purposes. The following summarizes these loans as at December 31, 2017:

| Term Loans with the Business Development Bank ("BDC") | (a) | (b) | (c) | (d) | (e) | Totals |
|---|--------------------------|--------------------------|--------------------------|--------------------------|--------------------------|--------------|
| Effective date of loan | Jun, 2008 | Oct, 2014 | Oct, 2015 | Oct, 2015 | Nov, 2015 | |
| Initial Loan Amount | \$ 3,000,000 | \$ 615,000 | \$ 50,000 | \$ 200,000 | \$ 250,000 | \$ 4,115,000 |
| Balance, September 30, 2017 | 2,268,700 | 348,500 | 28,080 | 129,870 | 162,240 | 2,937,390 |
| Loan repayments during the period | (27,780) | (30,750) | (3,120) | (9,990) | (12,480) | (84,120) |
| Balance, December 31, 2017 | \$ 2,240,920 | \$ 317,750 | \$ 24,960 | \$ 119,880 | \$ 149,760 | \$ 2,853,270 |
| Current Portion | \$ 111,120 | \$ 123,000 | \$ 12,480 | \$ 39,960 | \$ 49,920 | \$ 336,480 |
| Non-current portion | 2,129,800 | 194,750 | 12,480 | 79,920 | 99,840 | 2,516,790 |
| Payment frequency | Monthly | Monthly | Monthly | Monthly | Monthly | |
| Maturity of loan | Feb, 2038 | Jul, 2020 | Dec, 2019 | Dec, 2020 | Dec, 2020 | |
| Terms of repayment | "Principal and interest" | "Principal and interest" | "Principal and interest" | "Principal and interest" | "Principal and interest" | |

- Notes: (a) Loan for the purchase of manufacturing facility and building improvements.
(b) Loan for the purchase of equipment for our bioreactor project
(c) Loan for the purchase of building improvements.
(d) Loan for the purchase of manufacturing equipment
(e) Working Capital loan

All BDC loans have a floating interest rate based on BDC's floating base rate plus 0.5% - 1.8%. At December 31, 2017, the floating base rate was 5.8%. The loans are secured with the building and equipment.

As at December 31, 2017, the commitment for the next five fiscal years for the BDC loans is as follows:

| | |
|---------------------|--------------|
| 2018 | \$ 252,360 |
| 2019 | 336,480 |
| 2020 | 306,620 |
| 2021 | 133,590 |
| 2022 | 111,120 |
| 2023 and thereafter | \$ 1,713,100 |

10. LONG-TERM DEBT, BANK INDEBTEDNESS AND OTHER DEBT (Continued)

- b) On October 20, 2016, the Company arranged a new revolving line of credit agreement with its Canadian chartered bank. That agreement allowed the Company to draw on to a limit of \$1,000,000 bearing interest at the bank's prime lending rate plus 2.25%. This credit facility was implemented in November 2016, replacing the Company's previous credit facility of \$0.5 million. Accounts receivable and inventory were pledged as collateral for the bank credit facility.

On April 28, 2017, the Company received approval from its Chartered Bank to increase the borrowing limit on its credit facility to \$1.5 million. The newly expanded credit facility was available on May 4, 2017.

As at December 31, 2017 the Company had drawn on \$360,000 of the facility (2016 - \$720,000).

- c) On December 31, 2015 the Company issued two outstanding shareholder loans for total proceeds of \$200,000. These loans were repaid on December 31, 2016. On September 12, 2017, the Company issued two outstanding shareholder interest bearing loans for total proceeds of \$200,000. These loans were repaid on October 23, 2017.
- d) On May 3, 2017, the Company signed an agreement with Business Development Corporation for a new equipment credit facility in the amount of \$610,000. As of December 31, 2017 no funds have been withdrawn against this loan.

11. DEFERRED REVENUE

As at December 31, 2017, the Company has received payment, in the amount of \$876,916 (2016 - \$907,680), for a portion of product sales which was not yet shipped. This amount has been recognized as deferred revenue under the current liabilities in the consolidated statements of comprehensive income.

12. SHARE CAPITAL

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

On October 18, 2017 and October 26, 2017 (the "Closing Date"), the Company completed a private placement offering of an aggregate of 11,666,633 units for total gross proceeds of \$3,499,990, net proceeds of \$3,137,283 after share issuance costs of \$362,707. Each unit consists of one common share of Microbix and one half of a common share purchase warrant. Each whole warrant entitles the holder to purchase one additional common share at an exercise price of \$0.36 for three years. The financing was brokered. Cash commissions of \$226,729 were paid and an aggregate of 755,764 Broker's Warrants were issued in the private placement offering. Each Broker's Warrant entitles the holder to purchase one unit at a price of \$0.335 for a period of two years. All securities issued under the private placement will be subject to a hold period expiring four months and one day from the date of closing.

The number of issued and outstanding common shares and the stated capital of the Company as at December 31, 2017 are presented below:

| | Number of Shares | Share Capital |
|-----------------------------------|---------------------|----------------------|
| Balance, September 30, 2017 | 84,704,257 | \$ 31,299,416 |
| Issued on private placement | 11,666,633 | 2,483,731 |
| Exercise of stock options | 400,000 | 181,516 |
| Balance, December 31, 2017 | 96,770,890 | \$ 33,964,663 |

MICROBIX

NOTES TO THE UNAUDITED CONSOLIDATED INTERIM FINANCIAL STATEMENTS Canadian Funds As at and for the three months ended December 31, 2017 and 2016

13. CONTRIBUTED SURPLUS

Changes in contributed surplus up to December 31, 2017 are described as follows:

| | Amount |
|--|---------------------|
| Balance, as at September 30, 2017 | \$ 8,048,315 |
| Share Issuance pursuant to Stock Options Exercised | (77,516) |
| Issuance of Warrants pursuant to Private Placement | 743,905 |
| Share issue costs pursuant to Private Placement | (90,353) |
| Stock options expensed | 114,813 |
| Balance, as at December 31, 2017 | \$ 8,739,164 |

14. COMMON SHARE PURCHASE WARRANTS

A continuity of the Company's warrants outstanding as at December 31, 2017 and September 30, 2017 is presented in the following table:

| | Units | Weighted average exercise price |
|-----------------------------------|-------------------|---------------------------------|
| Outstanding, September 30, 2017 | 8,331,313 | \$ 0.48 |
| Issued | 6,589,081 | \$ 0.36 |
| Expired | - | - |
| Balance, December 31, 2017 | 14,920,394 | \$ 0.43 |

A summary of the Company's warrants outstanding as at December 31, 2017 and September 30, 2017 is presented in the following table:

| | December 31, 2017 | | | September 30, 2017 | | |
|---------------------------|--------------------|---------------------------------|---|--------------------|---------------------------------|---|
| | Number outstanding | Weighted average exercise price | Weighted average remaining contractual life (years) | Number outstanding | Weighted average exercise price | Weighted average remaining contractual life (years) |
| Range of exercise prices: | | | | | | |
| \$0.55 | 6,449,763 | \$ 0.55 | 1.64 | 6,531,313 | \$ 0.55 | 2.18 |
| \$0.23 to \$0.44 | 8,470,631 | 0.33 | 2.95 | 1,800,000 | 0.23 | 3.65 |
| | 14,920,394 | \$ 0.43 | 2.38 | 8,331,313 | \$ 0.48 | 2.50 |

15. STOCK OPTION PLAN

On March 5, 2013 and January 16, 2015 the shareholders of the Company approved resolutions to amend the Company's stock option plan. This amendment changed the total number of common shares available to be issued under the plan from a maximum of 10,000,000 to a maximum of 12,000,000 common shares. Under the plan, the Company has a total of 5,820,000 options issued and pending (2016 – 4,327,000).

The exercise price of each option equals no less than the market price at the date immediately preceding the date of the grant. In general, options issued under the plan vest and are exercisable in equal amounts in three steps, at the issue date and at the anniversary date in the subsequent two years. Management does not expect any stock options issued in the year and remaining unvested at the year-end to be forfeited before they vest.

The activity under the Company's stock option plan for the three months ended December 31, 2017 is as follows:

| | Units | Weighted average exercise price |
|---------------------------------------|------------------|---------------------------------|
| Outstanding, September 30, 2017 | 6,470,000 | \$ 0.39 |
| Stock options exercised | (400,000) | 0.26 |
| Stock options forfeited | (250,000) | 0.54 |
| Stock options issued | - | - |
| Balance, December 31, 2017 | 5,820,000 | \$ 0.40 |
| Exercisable, December 31, 2017 | 2,932,833 | \$ 0.46 |

The exercise price of each option equals the closing market price of the Company's capital stock on the day preceding the grant date.

The following table reflects the number of options, their weighted average price and the weighted average remaining contract life for the options grouped by price range as of December 31, 2017 and September 30, 2017:

| | December 31, 2017 | | | September 30, 2017 | | |
|---------------------------|--------------------|---------------------------------|---|--------------------|---------------------------------|---|
| | Number outstanding | Weighted average exercise price | Weighted average remaining contractual life (years) | Number outstanding | Weighted average exercise price | Weighted average remaining contractual life (years) |
| Range of exercise prices: | | | | | | |
| \$0.54 | 2,670,000 | \$ 0.54 | 2.83 | 2,920,000 | \$ 0.54 | 3.00 |
| \$0.23 to \$0.28 | 3,150,000 | \$ 0.28 | 4.68 | 3,550,000 | \$ 0.27 | 4.33 |
| | 5,820,000 | \$ 0.40 | 3.67 | 6,470,000 | \$ 0.39 | 3.73 |

The volatility of the stock for the Black-Scholes options pricing model was based on 5-year historic volatility of the Company's stock price on the Toronto Stock Exchange. Management believes that the historic stock volatility provides a fair and appropriate basis of estimate for the expected future volatility of the stock. Stock options are assumed to be exercised at the end of the option's life, as management believes the probability of an early exercise is remote. During the period, the fair value of the options vested in the year were expensed and credited to contributed surplus. During the quarter the company recorded share-based compensation expense of \$114,813 (2016 - \$55,576).

As at and for the three months ended December 31, 2017 and 2016
16. INCOME PER SHARE

Basic income per share is calculated using the weighted average number of shares outstanding. Diluted income per share reflects the dilutive effect of the exercise of stock options, warrants and convertible debt. The following table reconciles the net income and the number of shares for the basic and diluted loss per share computations:

| | As at December 31 | |
|---|-------------------|----------------|
| | 2017 | 2016 |
| Numerator for basic income per share: | | |
| Net income (loss) available to common shareholders (\$) | \$ (94,128) | \$ (3,216,472) |
| Denominator for basic income per share: | | |
| Weighted average common shares outstanding | 96,770,890 | 84,704,257 |
| Effect of dilutive securities: | | |
| Warrants | - | - |
| Stock Options | - | - |
| Convertible debentures | - | - |
| Denominator for diluted income (loss) per share | 96,770,890 | 84,704,257 |
| Net income (loss) per share: | | |
| Basic | (\$0.001) | (\$0.038) |
| Diluted | (\$0.001) | (\$0.038) |

The following represents the warrants, stock options and convertible debentures not included in the calculation of diluted EPS due to their anti-dilutive impact:

| | 2017 | 2016 |
|------------------------------------|------------|------------|
| Pursuant to warrants | 14,920,394 | 6,831,313 |
| Under stock options | 5,820,000 | 4,007,000 |
| Pursuant to convertible debentures | 19,565,217 | 21,739,130 |
| | 40,305,611 | 32,577,443 |

MICROBIX**NOTES TO THE UNAUDITED CONSOLIDATED INTERIM FINANCIAL STATEMENTS** Canadian Funds

As at and for the three months ended December 31, 2017 and 2016

17. EXPENSES BY NATURE

The Company has chosen to present its consolidated statements of comprehensive income based on the functions of the entity and include the following expenses by nature:

Depreciation and amortization

| | Three months ended Dec 31, 2017 | Three months ended Dec 31, 2016 |
|-------------------------------------|---------------------------------------|---------------------------------------|
| Included in: | | |
| Cost of goods sold | \$ 123,248 | \$ 71,606 |
| General and administrative | 238 | 248 |
| Research and development expenses | 38,401 | 29,611 |
| Total depreciation and amortization | \$ 161,887 | \$ 101,465 |

Employee costs

| | Three months ended Dec 31, 2017 | Three months ended Dec 31, 2016 |
|--|---------------------------------------|---------------------------------------|
| Short-term wages, bonuses and benefits | \$ 1,331,033 | \$ 1,126,073 |
| Share based payments | 114,813 | 55,576 |
| Total employee costs | 1,445,846 | 1,181,649 |

| | | |
|-------------------------------------|--------------|--------------|
| Included in: | | |
| Cost of goods sold | 734,578 | 594,068 |
| Research and development expenses | 187,152 | 198,441 |
| General and administrative expenses | 422,587 | 302,854 |
| Selling and business development | 101,529 | 86,286 |
| Total employee costs | \$ 1,445,846 | \$ 1,181,649 |

18. CHANGES IN NON-CASH WORKING CAPITAL

| | Three months ended Dec 31, 2017 | Three months ended Dec 31, 2016 |
|--|---------------------------------------|---------------------------------------|
| Accounts receivable | \$ (238,339) | \$ 940,558 |
| Inventory | (173,724) | (278,431) |
| Prepaid expenses and other assets | 59,133 | (6,835) |
| Investment tax credits receivable | - | (40,000) |
| Accounts payable and accrued liabilities | (1,032,270) | 66,676 |
| | \$ (1,385,201) | \$ 681,968 |

MICROBIX**NOTES TO THE UNAUDITED CONSOLIDATED INTERIM FINANCIAL STATEMENTS** Canadian Funds

As at and for the three months ended December 31, 2017 and 2016

19. FINANCIAL EXPENSES

| | 2017 | 2016 |
|----------------------------|------------|------------|
| Cash interest: | | |
| Interest on long-term debt | \$ 41,969 | \$ 41,046 |
| Interest on debentures | 121,859 | 120,000 |
| Interest other | 8,750 | 27,558 |
| Interest income | - | - |
| Non-cash interest: | | |
| Accretion on debentures | 36,812 | 30,293 |
| Financial expenses | \$ 209,390 | \$ 218,897 |

20. CAPITAL MANAGEMENT

The Company's capital management objective is to safeguard its ability to function as a going concern to maintain its Virology operations and to fund its development activities. Microbix defines its capital to include the revolving line of credit, shareholders' equity, the Business Development Bank capital loans, and the debentures. The capital at December 31, 2017 was \$24,353,842 (2016 - \$22,004,091).

To date, the Company has used cash provided by operating activities, common equity issues, debentures, bank mortgage and other financing to fund its activities. The equity is through private placements, the debentures are all controlled by private individuals known to the Company and the mortgage and other financing are with the Business Development Bank. If possible, the Company tries to optimize its liquidity needs by non-dilutive sources, including cash provided by operating activities, investment tax credits, grants and interest income. The Company has a revolving line of credit of \$1,500,000 with its Canadian chartered bank, Note 10 (b).

The Company's general policy is to not pay dividends and retain cash to keep funds available to finance the Company's growth. However, the Board of Directors may, from time to time, choose to declare a dividend in assets if warranted by circumstances. There was no change during the year in how the Company defines its capital or how it manages its capital.

21. FINANCIAL INSTRUMENTS

The Company categorizes its financial assets and liabilities measured at the fair value into one of three different levels depending on the observation of the inputs used in the measurement.

For the three months ended December 31, 2017 and 2016, the Company has carried at fair value financial instruments in Level 1. At December 31, 2017, the Company's only financial instrument measured at fair value is cash, which is considered to be a Level 1 instrument. There were no transfers between levels during the year.

The three levels are defined as follows:

- a) Level 1: Fair value is based on unadjusted quoted prices for identical assets or liabilities in active markets.
- b) Level 2: Fair value is based on inputs other than quoted prices included within Level 1 that are not observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- c) Level 3: Fair value is based on valuation techniques that require one or more significant unobservable inputs.

The following table provides the fair value measurement hierarchy of the Company's assets and liabilities.

| | Date of valuation | Quoted prices in active markets (Level 1) | Significant observable inputs (Level 2) | Significant unobservable inputs (Level 3) |
|--|-------------------|---|---|---|
|--|-------------------|---|---|---|

Assets measured at fair value:

| | | | | |
|------|-----------|-----------|---|---|
| Cash | 30-Dec-17 | \$ 51,389 | - | - |
|------|-----------|-----------|---|---|

Liabilities for which fair values are disclosed:

| | | | | |
|-------------------------------|-----------|---|--------------|--------------|
| Non-convertible debentures | 30-Dec-17 | - | - | \$ 1,172,517 |
| Convertible debentures | 30-Dec-17 | - | - | 1,531,404 |
| Long-term-debt and other debt | 30-Dec-17 | - | \$ 3,213,270 | - |

| | Date of valuation | Quoted prices in active markets (Level 1) | Significant observable inputs (Level 2) | Significant unobservable inputs (Level 3) |
|--|-------------------|---|---|---|
|--|-------------------|---|---|---|

Assets measured at fair value:

| | | | | |
|------|-----------|----------|---|---|
| Cash | 30-Dec-16 | \$ 1,680 | - | - |
|------|-----------|----------|---|---|

Liabilities for which fair values are disclosed:

| | | | | |
|-------------------------------|-----------|---|--------------|--------------|
| Non-convertible debentures | 30-Dec-16 | - | - | \$ 1,334,697 |
| Convertible debentures | 30-Dec-16 | - | - | 1,469,039 |
| Long-term-debt and other debt | 30-Dec-16 | - | \$ 3,915,570 | - |

The fair value of a financial instrument is approximated by the consideration that would be agreed to in an arm's length transaction between willing parties and through appropriate valuation methods, but considerable judgement is required for the Company to determine the value. The actual amount that could be realized in a current market exchange could be different than the estimated value.

The fair values of financial instruments included in current assets and current liabilities approximate their carrying values due to their short-term nature.

The fair value of the long-term debt is based on rates currently available for items with similar terms and maturities. The convertible and non-convertible debenture fair values are not readily determinable as the convertible debentures have been issued to shareholders of the Company. The fair values of financial instruments in other long-term liabilities approximate their carrying values as they are recorded at the net present values of their future cash flows, using an appropriate discount rate.

22. FINANCIAL RISK MANAGEMENT

The primary risks that affect the Company are set out below and the risks have not changed during the reporting periods. The list does not cover all risks to the Company, nor is there an assurance that the strategy of management to mitigate the risks is sufficient to eliminate the risk.

Risks arising from financial instruments and risk management

The Company's activities expose it to a variety of financial risks: market risk (including foreign exchange risk), credit risk and liquidity risk. The Company's overall risk management program focuses on the unpredictability of financial markets and seeks to minimize potential adverse effects on the Company's financial performance.

Risk management is the responsibility of the corporate finance function. Material risks are monitored and are regularly discussed with the Audit Committee of the Board of Directors.

Credit risk

The Company's cash and cash equivalents are held in accounts or short-term interest bearing accounts at one of the major Canadian chartered banks. Management perceives the credit risk to be low. There is a concentration of accounts receivable risk due to the few large customers comprising the Company's international customer base. In the three months ended December 31, 2017, five customers accounted for 82% (2016 - five customers accounted for 76%) of revenue. The Company has had minimal bad debts over the past several years and accordingly management has recorded an allowance of \$10,000 (2016 - \$10,000).

Trade accounts receivable are aged as follows at December 31:

| | As at Dec 31, 2017 | As at Dec 31, 2016 |
|---------------------------|-----------------------|-----------------------|
| Current | \$ 1,208,896 | \$ 673,865 |
| 0 - 30 days past due | 318,107 | 103,134 |
| 31 - 60 days past due | 37,269 | 299,398 |
| 61 days and over past due | 11,555 | 4,917 |
| | \$ 1,575,827 | \$ 1,081,314 |

Market risk and foreign currency risk

Market risk is the risk that changes in market prices, such as foreign exchange rates, will affect the Company's income or the value of its financial instruments. The Company's activities that result in exposure to fluctuations in foreign currency exchange rates consist of the sale of products and services to customers invoiced in foreign currencies and the purchase of services invoiced in foreign currencies. The Company does not use financial instruments to hedge these risks. As at December 31 the significant balances, quoted in Canadian dollars, held in foreign currencies are:

| | US dollars | | Euros | |
|--|------------|----------|---------|---------|
| | 2017 | 2016 | 2017 | 2016 |
| Cash | \$ 49,835 | \$ 7,448 | \$ - | \$ 85 |
| Accounts receivable | 717,516 | 423,030 | 400,854 | 229,658 |
| Accounts payable and accrued liabilities | 297,820 | 369,592 | 1,505 | 21,587 |

22. FINANCIAL RISK MANAGEMENT (Continued)
Market risk and foreign currency risk (Continued)

The Company's revenue and expenses by foreign currency for the quarters ended December 31, 2017 and 2016 are as follows:

| | 2017 | 2016 |
|-----------------|------|------|
| Revenue | | |
| Euros | 46% | 32% |
| U.S. dollars | 48% | 64% |
| Expenses | | |
| U.S. dollars | 8% | 8% |

The impact of a 5% increase in the U.S. dollar against the Canadian dollar would result in an increase in annual U.S. dollar based revenue of about \$284,600 Cdn. The impact of a 5% increase in the Euro against the Canadian dollar would result in an increase in annual Euro based revenue of about \$201,800. Correspondingly, the impact of a 5% decrease in the U.S. dollar against the Canadian dollar would result in a loss in annual U.S. dollar based revenue of about \$284,600 Cdn. The impact of a 5% decrease in the Euro against the Canadian dollar would result in a loss in annual Euro-based revenue of about \$201,800.

Liquidity risk

Liquidity risk is the risk that the Company will encounter difficulties in meeting its financial liability obligations as they become due. The Company has a planning and budgeting process in place to help determine the funds required to support the normal operating requirements on an ongoing basis. The Company has financed its cash requirements primarily through issuance of securities, short-term borrowings, long-term debt and debentures. The Company controls liquidity risk through management of working capital, cash flows and the availability of sourcing of financing.

Interest rate risk

Financial instruments that potentially subject the Company to cash flow interest rate risk are those assets and liabilities with a variable interest rate. Interest rate risk exposure is primarily on the BDC debt that has a variable rate that is pegged to the bank rate. The rate can be fixed at the Company's option, if the outlook for interest rates should move higher. The only other variable debt the Company has is the \$1,500,000 line of credit that bears interest at the bank's prime lending rate plus 2.25%. A 1% increase in the bank rate would cost the Company approximately \$30,000 per year for BDC and about \$15,000 on the line of credit usage if it were fully used throughout the fiscal year.

23. SEGMENTED INFORMATION

The Company operates in two industries: (i) the development, manufacturing and distribution of cell-based products and technology and, (ii) the provision of facility, technical and production personnel for contract research and development. External revenue by segment is attributed to geographic regions based on the location of customers: North America, Europe and other foreign countries. The following is an analysis of the Company's revenue and profits from continuing operations by reportable segment:

| | Segment revenue | | Segment profit (loss) | |
|------------------------------------|-----------------|--------------|-----------------------|----------------|
| | 2017 | 2016 | 2017 | 2016 |
| Virology products and technologies | \$ 2,885,567 | \$ 1,952,502 | \$ (68,978) | \$ (3,169,903) |
| Lumisort™ | - | - | (25,150) | (46,569) |
| Kinlytic® | - | - | - | - |
| Total for continuing operations | \$ 2,885,567 | \$ 1,952,502 | \$ (94,128) | \$ (3,216,472) |

Segment revenue reported above represents revenue generated from external customers. There were no inter-segment sales in the current period (2016 - \$Nil).

As at and for the three months ended December 31, 2017 and 2016

23. SEGMENTED INFORMATION (Continued)

The accounting policies of the reportable segments are the same as the Company's accounting policies described in Note 3. Segment profit represents the profit before tax earned by each segment without allocation of central administration costs and directors' salaries, share of profits of associates, gain recognised on disposal of interest in former associate, investment income, other gains and losses as well as finance costs. This is the measure reported to the chief operating decision maker for the purposes of resource allocation and assessment of segment performance.

Segmented assets and liabilities as at December 31 are as follows:

| | Segment assets | | Segment liabilities | |
|------------------------------------|----------------------|----------------------|---------------------|---------------------|
| | 2017 | 2016 | 2017 | 2016 |
| Virology Products and Technologies | \$ 13,719,965 | \$ 12,057,623 | \$ 8,637,537 | \$ 8,425,429 |
| Lumisort™ | 9,055,638 | 8,679,653 | - | 457,760 |
| Kinlytic® | 3,078,585 | 2,866,413 | - | - |
| | <u>\$ 25,854,188</u> | <u>\$ 23,603,689</u> | <u>\$ 8,637,537</u> | <u>\$ 8,883,189</u> |

All assets are allocated to reportable segments other than interests in associates and current and deferred tax assets. Assets used jointly by reportable segments are allocated on the basis of the revenues earned by individual reportable segments. All liabilities are allocated to reportable segments other than borrowings and current and deferred tax liabilities. Liabilities for which reportable segments are jointly liable are allocated in proportion to segment assets.

Segmented depreciation and amortization and additions to non-current assets as at December 31 are as follows:

| | Depreciation and amortization | | Additions to non-current assets | |
|------------------------------------|-------------------------------|-------------------|---------------------------------|-------------------|
| | 2017 | 2016 | 2017 | 2016 |
| Virology Products and Technologies | \$ 128,414 | \$ 77,573 | \$ 616,285 | \$ 38,949 |
| Lumisort™ | 33,473 | 23,892 | 192,320 | 70,908 |
| Kinlytic® | - | - | - | 95,884 |
| | <u>\$ 161,887</u> | <u>\$ 101,465</u> | <u>\$ 808,605</u> | <u>\$ 205,741</u> |

24. GEOGRAPHIC INFORMATION

The Company operates in three principal geographical areas – North America (country of domicile), Europe and in other foreign countries. The Company's revenue from continuing operations from external customers by location of customer's operations and information about its non-current assets by location of assets are detailed below.

| | Revenue from external customers | | Non-current assets | |
|-------------------------|---------------------------------|---------------------|----------------------|----------------------|
| | 2017 | 2016 | 2017 | 2016 |
| North America | \$ 1,274,135 | \$ 727,396 | \$ 20,922,492 | \$ 19,841,493 |
| Europe | 1,536,743 | 901,691 | - | - |
| Other foreign countries | 74,689 | 323,415 | - | - |
| | <u>\$ 2,885,567</u> | <u>\$ 1,952,502</u> | <u>\$ 20,922,492</u> | <u>\$ 19,841,493</u> |

As at and for the three months ended December 31, 2017 and 2016

25. RELATED PARTY TRANSACTIONS*Key management compensation*

Key management personnel are those persons having authority and responsibility for planning, directing and controlling the activities of the Company. Key management includes directors and key management executive officers. Compensation for the Company's key management personnel was as follows:

| | Three months ended Dec 31, 2017 | Three months ended Dec 31, 2016 |
|--|---------------------------------------|---------------------------------------|
| Short-term wages, bonuses and benefits | \$ 200,838 | \$ 189,920 |
| Termination benefits | - | - |
| Share-based payments | 101,005 | 36,406 |
| Total key management compensation | \$ 301,843 | \$ 226,326 |

The Company has issued and outstanding debentures with two shareholders of the Company (see note 9). On December 31, 2015 the Company had issued two shareholder loans for total proceeds of \$200,000. On December 31, 2016, the two outstanding shareholder loans were repaid. On September 12, 2017, the company issued two outstanding shareholder loans for total proceeds of \$200,000. These loans were repaid on October 23, 2017.

26. COMMITMENTS AND CONTINGENCIES*Lease commitments*

| | Amount |
|---------------------|-------------------|
| 2018 | \$ 76,588 |
| 2019 | 97,920 |
| 2020 | 91,962 |
| 2021 | 91,499 |
| 2022 | 82,649 |
| 2023 and thereafter | 7,077 |
| | <u>\$ 447,695</u> |

Payments on convertible and non-convertible debentures (Note 9)

| | Amount |
|---------------------|----------------------|
| 2018 | \$ 531,931 |
| 2019 | 709,242 |
| 2020 | 709,242 |
| 2021 | 709,242 |
| 2022 | 1,657,992 |
| 2023 and thereafter | 7,736,408 |
| | <u>\$ 12,054,057</u> |

Contingencies

The Company is not party to any legal proceedings arising out of the normal course of business.

27. SETTLEMENT OF DISPUTES AND LAWSUITS**Sale of Microbix' WFI business to Irvine Scientific**

On December 30, 2016 Microbix reached a final settlement with Irvine Scientific Inc. over an ongoing dispute related to the sale of the Company's Water-for-Injection business to Irvine Scientific that occurred in December 2012. Irvine Scientific had filed a Notice of Arbitration with the American Arbitration Association in New York as stipulated in its original agreement with Microbix. Prior to initiation of the arbitration proceeding the companies agreed on final settlement terms, namely Microbix will pay Irvine a total amount of (U.S.) \$192,500 in the following instalments:

- December 30, 2016 - (U.S.) \$64,167
- March 31, 2017 - (U.S.) \$64,167
- June 30, 2017 - (U.S.) \$64,166

All obligations under this settlement were completed at June 30, 2017.

Settlement of Zeptometrix Lawsuit

On October 5, 2016, Zeptometrix Corporation filed a statement of claim against Microbix in Canadian Federal Court, alleging infringement of its Canadian patent. During fiscal 2017 Microbix defended itself against these allegations, maintaining it did not infringe this patent. On October 11, 2017 Microbix announced the court approval of a legal dispute settlement with Zeptometrix Corporation, with the latter party's claims of patent infringement being withdrawn. The withdrawal of the lawsuit was "with prejudice", following a settlement agreement between the parties that was to Microbix' satisfaction.

DIRECTORS

Peter M. Blecher
Ontario, Canada
Staff Emergency Physician
Lakeridge Health Hospital

Mark A. Cochran
Virginia, USA
Managing Director
Johns Hopkins Medicine

Vaughn C. Embro-Pantalony ^{(1) (2)}
Ontario, Canada
Pharmaceutical Executive

William J. Gastle ⁽²⁾
Ontario, Canada
Executive Chairman
Microbix Biosystems Inc.

Cameron Groome ⁽²⁾
Ontario, Canada
Chief Executive Officer and President
Microbix Biosystems Inc.

Martin A. Marino ^{(1) (2)}
Ontario, Canada
Pharmaceutical Executive

Joseph D. Renner ^{(1) (2)}
New Jersey, USA
Pharmaceutical Executive

⁽¹⁾*Member of Audit Committee.*

⁽²⁾*Member of the Human Resources,
Compensation and Governance Committee.*

SENIOR MANAGEMENT

William J. Gastle
Executive Chairman

Cameron L. Groome
President and Chief Executive Officer

James S. Currie
Chief Financial Officer

Dr. Mark Luscher
Senior Vice-President, Scientific Affairs

Phillip Casselli
Senior Vice-President, Sales & Business Development

Kevin J. Cassidy
Vice-President, Biopharmaceuticals

Kathryn Froh
Vice-President, Diagnostics

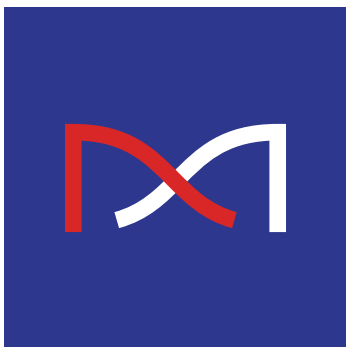
Christopher B. Lobb
General Counsel & Secretary

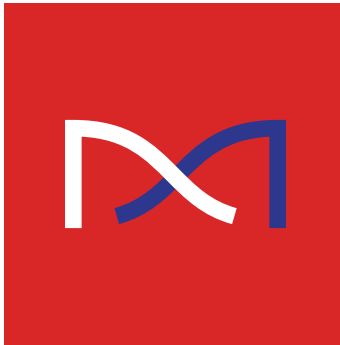
CORPORATE INFORMATION

| | |
|-------------------|--|
| Corporate Counsel | <i>Boyle & Co. LLP</i> |
| Auditors | <i>Ernst Young LLP</i> <i>Chartered Accountants</i> |
| Transfer Agent | <i>AST Trust Company Inc.</i> <i>as the Administrative Agent for</i> <i>CIBC Mellon Trust Company</i> <i>416-682-3860 1-800-387-0825</i> |
| Bankers | <i>The Toronto Dominion Bank</i> |
| Head Office | Microbix Biosystems Inc. 265 Watline Avenue, Mississauga, Ontario Canada L4Z 1P3 Tel: 905-361-8910 Fax: 905-361-8911 www.microbix.com |

NOTICE OF ANNUAL MEETING

The Annual Meeting of the Shareholders will be held at the University Club, 380 University Avenue, Toronto, Ontario on Wednesday, March 28, 2018 at 1:00 PM.





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