



First Quarterly Report  
Ending August 31, 2002

## Management's Discussion and Analysis

Management's Discussion and Analysis is intended to assist in the understanding and assessment of the trends and significant changes in the operating results and financial position of Neptune Technologies & Bioresources. Historical results are no guarantee of future performance. This analysis should be read in conjunction with the Company's consolidated financial statements and accompanying notes. The Company has a limited operating history on which to base an evaluation of its business and prospects. Its prospects must be considered in light of the risks and uncertainties involved in any new emerging market. Such risks include, but are not limited to, an evolving and unpredictable business and management of potentially high growth.

To counter these risks, the Company must, among other things: continue to develop and improve its technological platform and extraction processes, pursue the validation of its product benefits in the nutraceutical, cosmetics and biopharmaceutical fields, formulate and implement its business and marketing strategy, meet competition and attract, retain and motivate qualified personnel. There can be no guarantee that the Company will be successful in containing such risks.

## The Company

Founded in 1998, the Company is pursuing its mission of developing and exploiting innovative high-yield technological processes in the production of value-added natural products. These include oils rich in Omega-3 fatty acids, phospholipids and antioxidants, protein concentrates, amino acid concentrates and other marine and aquatic biomass extracts. It intends to market its products for innovative applications in the nutraceutical, cosmetic and biopharmaceutical fields. Krill, a cold deepwater zooplankton, is the first group of marine species actively exploited by the Company.

## Review of the three-month period ending August 31, 2002

During the fiscal year, the Company continued to establish its operational structure and proceeded with the financing indispensable to the fulfillment of its business plan.

The Company took out two loans in July 2002 to finance installation and start-up of the Sherbrooke plant. One loan, in the amount of \$ 980,000 for a seven-year term, came from *La Financière du Québec*. The interest rate for this loan is the weekly variable rate plus 1%. For the purpose of this financing, the Company issued 196,000 warrants, allowing the holder, over a two-year period, to acquire one common share of the Company at \$1.00 per warrant exercised.

The second loan, in the amount of \$ 1,000,000, in the form of a convertible term note, maturing January 31, 2003, was concluded with *Société Innovatech du Sud du Québec*. This

note is repayable before term from the proceeds of future financing. Under this financing, the Company issued 100,000 warrants, allowing the holder, for a one-year period, to subscribe for one share of the Company at \$1.00 per warrant.

This financing completes the referred investment for the installation of the equipment at our Sherbrooke plant, as the phase I of our industrial development, and permits the Company to invest more aggressively in its commercialisation.

The Company generated no revenue in the first quarter ending August 31, 2002. However, it devoted its efforts to install the equipment required for commercial operation of its extraction process at its Sherbrooke plant. It also hired and trained the personnel who will be called upon to operate the plant after its startup in early autumn 2002. Completing these steps allows the Company to move from business startup to a revenue-generating going concern.

## Operating results

During the first quarter ended August 31, 2002, the Company recorded a net loss of \$760,370 (0.049 per share) compared to \$502,744 (0.039 per share) for the quarter ended in August 31, 2001.

The operating expenses amounted to \$771,877 for the quarter ended August 31, 2002 compared to \$523,587 for the quarter ended August 31, 2001. This increase of \$248,290 is mainly due to the increase in Research & Development expenses of \$85,363, the increase of \$58,354 in marketing expenses related to the beginning of our commercial activities and the new expense of long debt interest of \$87,118. This interest charge comes from the required financing for the installation at our Sherbrooke plant.

The increase in the Research & Development expenses comes mainly from the increase in salaries and subcontracting. This increase, outlined our business plan, was required to maintain our research programs on the health benefits from our products extracted from the krill.

The administration expenses remained at the same level for the comparative periods. The administrative expenses totalled respectively \$301,638 and \$309,343 for the quarter ended August 31, 2002 and August 31, 2001.

## Balance sheets

As of August 31, 2002, the Company's total assets amounted to \$7,923,891 compared to \$6,637,504 as of May 31, 2002. This increase is mainly due to the additions of the equipment at our Sherbrooke plant.

The decrease in the working capital of the company between August 31, 2002 and May 31, 2002 is explained by the increase in the accounts payable to the amount of \$218,271 and the

convertible note of \$1,000,000, both due to the installation of the equipment and start-up of the Sherbrooke plant. At August 31, 2002 the company presented a negative working capital of \$455,307 with cash of \$625,194 compared to a working capital of \$1,722,208 and cash of \$1,844,560 at May 31, 2002.

## Financing activity

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## Outlook

Our main challenges for the year ahead consist of start-up of the Sherbrooke plant and optimization of its operation for the production of Neptune Krill Oil NKO™ and its by-products. At the same time, we must market our products to generate revenue. This will enable us to break even on our operating activities and fund research programs to develop applications for our products and components. The target markets for these products are the nutraceutical, cosmetic and biopharmaceutical sectors and the emerging field of nutrigenomics.

The nutraceutical, cosmetic and biopharmaceutical industries are highly competitive. Many firms engage in activities similar to those of the Company, including research and development of applications intended for human use. More specifically, competitors developing new nutraceutical products are focusing on cosmetic and pharmaceutical applications based on the specific properties of their products.

A number of these firms have financial resources, research and development capabilities, as well as manufacturing and marketing facilities greater than the Company. Moreover, educational institutions, government agencies and other research bodies are conducting research in the same sectors as the Company. They are also capable of marketing products, either through their own means, or via collaboration agreements.

The Company recognizes that it faces major competition with respect to its nutraceutical products. In addition, certain biomedical and biotechnological firms, including large pharmaceutical companies, have announced that they are working in the field of

nutraceutical-based therapies. The Company is aware that other companies or institutions are developing new nutraceutical-based therapies that are directly targeting the applications for which the Company is developing its own nutraceutical products.

According to its review of the industry, the Company is unaware of any other company using a cold krill oil extraction process. However, an emerging Quebec company is focused on producing lyophilized krill in powder and capsule form as a food supplement. Finally, the Company also expects that its technological platform for the exploitation of krill will attract the attention of other significant competitors over the years.

## Neptune Technologies & Bioresources inc.

(A development-stage company)

### Interim Consolidated Statement of Earnings

(unaudited)

	Three months ended August 31, 2002	August 31, 2001	Cumulative from October 9, 1998 to August 31, 2002
	\$	\$	\$
Operating expenses			
Research (note 4)	213,019	127,656	2,125,020
Marketing	75,907	17,553	233,409
Administration (note 5)	301,638	309,343	2,012,737
Financial communications	83,350	61,607	359,439
Interest on long-term debt	87,118		145,652
Depreciation of fixed assets	10,845	7,428	56,068
Loss before interest income	771,877	523,587	4,932,325
Interest income	11,507	20,843	135,369
<b>Net loss</b>	<b>760,370</b>	<b>502,744</b>	<b>4,796,956</b>
Basic and diluted loss per share	0.049	0.039	
Weighted average number of shares outstanding	15,640,000	12,871,739	

### Interim Consolidated Statement of Deficit

(unaudited)

	Three months ended August 31, 2002	August 31, 2001
	\$	\$
Balance, beginning of period	5,159,563	1,662,427
Net loss	760,370	502,744
Share issue expenses		848,099
Balance, end of period	<b>5,919,933</b>	<b>3,013,270</b>

# Neptune Technologies & Bioresources inc.

(A development-stage company)

## Interim Consolidated Statement of Cash Flows

(unaudited)

	Three months ended August 31, 2002	August 31, 2001	Cumulative from October 9, 1998 to August 31, 2002
	\$	\$	\$
<b>OPERATING ACTIVITIES</b>			
Net loss	(760,370)	(502,744)	(4,796,956)
Non-cash items			
Depreciation of fixed assets	10,845	7,428	56,068
Interest on long-term debt	56,250		112,500
Changes in working capital items	(131,018)	(603,956)	(39,549)
Cash flows from operating activities	<b>(824,293)</b>	<b>(1,099,272)</b>	<b>(4,667,937)</b>
<b>INVESTING ACTIVITIES</b>			
Banker's acceptance			(116,627)
Fixed assets	(1,678,244)	(6,004)	(4,033,127)
Patents and start-up costs	(602,164)	(86,518)	(1,263,377)
Cash flows from investing activities	<b>(2,280,408)</b>	<b>(92,522)</b>	<b>(5,413,131)</b>
<b>FINANCING ACTIVITIES</b>			
Bank loan	(437,000)	437,000	
Demand note	972,790		972,790
Due to a company controlled by an officer and administrateur			116,510
Long-term debt	1,260,286		1,819,626
Issue of convertible debenture			1,500,000
Issue of capital stock		5,000,000	7,230,054
Issue of warrants	89,259		89,259
Issue expenses		(848,099)	(1,021,977)
Deferred charges		283,842	
Cash flows from financing activities	<b>1,885,335</b>	<b>4,872,743</b>	<b>10,706,262</b>
<b>Increase (decrease) in cash and cash equivalents</b>	<b>(1,219,366)</b>	<b>3,680,949</b>	<b>625,194</b>
Cash and cash equivalents, beginning of period	<b>1,844,560</b>	<b>158,136</b>	
Cash and cash equivalents, end of period	<b>625,194</b>	<b>3,839,085</b>	<b>625,194</b>

# Neptune Technologies & Bioresources inc.

(A development-stage company)

## Interim Consolidated Balance Sheets

	Unaudited August 31, 2002	Audited May 31, 2002
	\$	\$
<b>ASSETS</b>		
Current assets		
Cash	625,194	1,844,560
Banker' s acceptance, 2.9 %	116,627	116,627
Accounts receivable	257,205	384,455
Research tax credits receivable	769,339	918,911
Inventory	683,410	106,930
Prepaid expenses	74,779	25,148
	<b>2,526,554</b>	<b>3,396,631</b>
Fixed assets (note 6)	<b>4,133,960</b>	<b>2,309,660</b>
Other assets	<b>1,263,377</b>	<b>661,213</b>
	<b>7,923,891</b>	<b>6,367,504</b>
<b>LIABILITIES</b>		
Current liabilities		
Bank loan		437,000
Demand note, face amount of \$1,000,000, 15 %	972,790	
Accounts payable and accrued liabilities	1,745,694	1,527,423
Instalments on long-term debt	263,377	160,000
	<b>2,981,861</b>	<b>2,124,423</b>
<b>LONG-TERM DEBT</b> (note 7)	<b>1,713,150</b>	<b>399,340</b>
<b>DEBENTURE</b> (note 8)	<b>1,612,500</b>	<b>1,556,250</b>
	<b>6,307,511</b>	<b>4,080,013</b>
<b>SHAREHOLDERS' EQUITY</b>		
Capital stock and warrants (note 9)	7,536,313	7,447,054
Deficit	<b>(5,919,933)</b>	<b>(5,159,563)</b>
	<b>1,616,380</b>	<b>2,287,491</b>
	<b>7,923,891</b>	<b>6,367,504</b>



# Neptune Technologies & Bioresources inc.

(A development-stage company)

## Notes to Interim Financial Statements

August 31, 2002 (unaudited)

### **1 - INTERIM FINANCIAL INFORMATION**

These interim consolidated financial statements as at August 30, 2002 are unaudited. They have been prepared by the company in accordance with generally accepted accounting principles in Canada for interim information and use the same accounting policies and methods in the preparation of the company's most recent annual consolidated financial statements with the exception of the accounting change described in Note 2. These interim consolidated financial statements should be read in conjunction with the audited annual consolidated financial statements and notes thereto in the company's 2002 annual report.

### **2 - CHANGE IN ACCOUNTING POLICIES**

On June 1st, 2002, the Company adopted prospectively the recommendations of the Canadian Institute of Chartered Accountants Handbook Section 3870, *Stock-based Compensation and Other Stock-based Payments*. This section defines notably recognition, measurement and disclosure standards for stock-based compensation to non-employees and employees. According to the new standards, stock-based payments to non-employees should be recorded systematically in the financial statements of the Company. These standards define a fair value-based method of accounting and encourage entities to adopt this method of accounting for its stock-based employee compensation plan. Under this method, compensation cost should be measured at the grant date based on the fair value of the award and should be recognized over the related service period. An entity that does not adopt the fair value method of accounting for its awards granted to employees is required to include in its financial statements pro forma disclosures of net income and earnings per share as if the fair value method of accounting had been applied. The Company has adopted the later alternative treatment. As no options were granted during the quarter, no such disclosure was required.

### **3 - RELATED PARTY TRANSACTIONS**

The Company has signed a service agreement with a shareholder (company controlled by an officer and director) which is renewable annually. Under the terms of this agreement, the Company pays monthly service fees of \$10,000 (\$10,000 in 2001). A monthly amount of \$2,000 is deducted for the use of the Company's premises by this shareholder. During the period, total fees amount to \$24,000 (\$24,000 in 2001). The \$24,000 fees include \$15,000 in management fees, \$15,000 in research fees and the total amount is reduced by a \$6,000 reduction for the use of the Company's premises by this shareholder. As at August 31, 2002, the balance due to this shareholder is nil (nil as at August 31, 2001).

These transactions occurred in the normal course of operations and are measured at the exchange amount, which is the amount of consideration determined and accepted by the parties involved.

The Company has also entered into an agreement calling for payments to a company controlled by an officer and director, as of June 1, 2002, in semi-annual instalments, of 1% of net annual sales, for an unlimited period, as royalties, to a maximum of net earnings before taxes, interest and depreciation.

## Neptune Technologies & Bioresources inc.

(A development-stage company)

### Notes to Interim Financial Statements

August 31, 2002 (unaudited)

#### 4 - INFORMATION REGARDING RESEARCH PROJECTS IN PROGRESS

	Three months ended		Cumulative from
	August 31,		October 9, 1998 to
	2002	2001	August 31, 2002
	\$	\$	\$
Service fees (note 3)	15,000	15,000	235,000
Salaries and employee benefits	106,389	69,823	749,103
Subcontracting	137,924	101,981	2,113,136
General and study expenses		260	33,311
Travel and entertainment expenses	1,057	996	49,199
	<b>260,370</b>	188,060	3,179,749
Research tax credits	(47,351)	(60,404)	(1,054,729)
Research expenses	<b>213,019</b>	127,656	2,125,020

Research tax credits recorded by the Company must be reviewed and approved by the tax authorities; accordingly, amounts granted may differ from amounts recorded.

#### 5 - INFORMATION REGARDING ADMINISTRATION COST

	Three months ended		Cumulative from
	August 31,		October 9, 1998 to
	2002	2001	August 31, 2002
	\$	\$	\$
Royalties			5,000
Salaries and employee benefits	136,826	114,570	902,853
Board of Directors	9,375	17,500	71,625
Travel and entertainment	47,055	17,806	142,285
Rent	20,462	19,363	135,780
Maintenance and repairs	4,123	4,331	30,488
Insurance	4,888	3,978	27,511
Communication	3,651	3,628	24,779
Taxes and permits	32,525	4,759	77,346
Office expenses	7,259	5,843	60,892
Professional fees	11,132	97,096	353,428
Management fees (note 3)	15,000	15,000	135,000
Financial expenses	9,342	5,469	45,750
	<b>301,638</b>	309,343	2,012,737

## Neptune Technologies & Bioresources inc.

(A development-stage company)

### Notes to Interim Financial Statements

August 31, 2002 (unaudited)

#### 6 - FIXED ASSETS

August 31, 2002

	Accumulated		Net
	Cost	depreciation	
	\$	\$	\$
Leasehold improvements	645,794	16,466	629,328
Furniture and fixtures	94,455	20,876	73,579
Office equipment	51,445	7,331	44,114
Processing equipment	3,185,325		3,185,325
Computer equipment	53,758	10,798	42,960
Software	2,350	597	1,753
Assets under capital leases	156,901		156,901
	<b>4,190,028</b>	<b>56,068</b>	<b>4,133,960</b>

May 31, 2002

	Accumulated		Net
	Cost	depreciation	
	\$	\$	\$
Leasehold improvements	427,937	13,859	414,078
Furniture and fixtures	88,278	17,753	70,525
Office equipment	51,445	5,095	46,350
Processing equipment	1,746,818		1,746,818
Computer equipment	38,055	8,213	29,842
Software	2,350	303	2,047
	<b>2,354,883</b>	<b>45,223</b>	<b>2,309,660</b>

#### 7 - LONG-TERM DEBT

	August 31, 2002	May 31, 2002
	\$	\$
Mortgage loan, authorized amount, \$1,200,000, of which \$291,160 will be receivable during the coming year, secured by processing equipment, having a depreciated cost of \$3,185,325, prime rate plus 6%, payable in monthly capital instalments of \$20,000 starting in October 2002, maturing in September 2007	908,840	559,340
Mortgage loan, face amount of \$980,000, payable in 60 monthly capital instalments of \$16,333 plus an annual interest at the weekly variable rate plus 1 %, starting in September 2004, maturing in August 2009	917,951	
Obligations under capital leases, maturing at various date until 2005, interest rate varying between 9.25 % and 12.67 %, payable in monthly instalments	149,736	
	<b>1,976,527</b>	559,340
Instalments due within one year	263,377	160,000
	<b>1,713,150</b>	<b>399,340</b>

## Neptune Technologies & Bioresources inc.

(A development-stage company)

### Notes to Interim Financial Statements

August 31, 2002 (unaudited)

#### 8 - DEBENTURE

	August 31, 2002	May 31, 2002
	\$	\$
Convertible debenture for a face amount of \$1,500,00, bearing interest at 15%	<b>1,612,500</b>	1,556,250

#### 9 - CAPITAL STOCK AND WARRANTS

	August 31, 2002	May 31, 2002
	\$	\$
<b>Issued and fully paid</b>		
15,640,000 (2002-05-31 : 15,640,000) common shares	<b>7,443,049</b>	7,443,048
4,050,000 Series "A" warrants	<b>4,003</b>	4,003
1,000,000 Series "B" warrants	<b>1</b>	1
(2002-05-31 : 2,490,000) Series "C" warrants		1
100,000 Series "D" warrants	<b>1</b>	1
196,000 Series "E" warrants	<b>62,049</b>	
100,000 Series "F" warrants	<b>27,210</b>	
	<b>93,264</b>	4,006
	<b>7,536,313</b>	7,447,054