

# CV Technologies Inc.

## MANAGEMENT'S DISCUSSION AND ANALYSIS

Second Quarter  
March 31, 2007



# CV Technologies Inc.

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# CV Technologies Inc.

Quarterly Report for the Three and Six Month Periods Ended

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## MANAGEMENT'S DISCUSSION AND ANALYSIS

*The interim consolidated financial statements of CV Technologies Inc. (the Company) are prepared in accordance with Canadian generally accepted accounting principles (GAAP). All references to GAAP refer to Canadian generally accepted accounting principles. These accounting principles require the Company to make certain estimates and assumptions that affect the reported amounts of assets, liabilities, revenue, expenses, and related disclosure of contingent assets and liabilities. Management believes that the estimates and assumptions, which it relies upon, are reasonably based on information available at the time that these estimates and assumptions were made. These estimates and assumptions have been discussed with the Audit Committee of the Board of Directors of CV Technologies Inc. Actual results may differ under different assumptions and conditions. The following information should be read in conjunction with the restated audited consolidated financial statements for the year ended September 30, 2006, the restated unaudited interim consolidated financial statements for the three month period ended December 31, 2006, and the unaudited interim consolidated financial statements for the three and six month period ended March 31, 2007 and accompanying notes. All expressed amounts are in Canadian dollars, unless specified otherwise. Additional information is available at [www.sedar.com](http://www.sedar.com).*

*This discussion and analysis for the three month period ended March 31, 2007 is prepared and contains disclosure of material changes occurring up to and including June 14, 2007.*

### **Forward-looking Statements**

*Management's discussion and analysis (MD&A) contains certain forward-looking information and statements within the meaning of applicable securities laws. The forward-looking information and statements included in this MD&A are not guarantees of future performance and should not be unduly relied upon. Such information and statements involve known and unknown risks, uncertainties and other factors that may cause actual results or events to differ materially from those anticipated in such forward-looking information or statements including, without limitation: those comments predicting the timing and/or initiation of clinical trials, clinical trial results, and associated regulatory clearances, financing and acceptance of COLD-FX® in the marketplace. The use of any of the words "expect", "anticipate", "continue", "estimate", "objective", "ongoing", "may", "will", "project", "should", "believe", "plans", "intends" and similar expressions are intended to identify forward-looking statements. In addition to the risks outlined in the Risks and Uncertainties section, this MD&A contains forward-looking information and statements pertaining to the following: the impact of competition; consumer confidence and spending levels; general economic conditions; interest and currency exchange rates; unseasonable weather patterns; the cost and availability of capital; the cost and availability of grants/funding; and product development. The Company believes that expectations and assumptions reflected in the forward-looking information and statements contained herein are reasonable but no assurance can be given that these expectations and assumptions are correct and that the results, performance or achievements expressed in, or implied by, forward-looking statements within this disclosure will occur, or if they do, that any benefits may be derived from them. All forward-looking statements are expressly qualified in their entirety by this cautionary statement.*

*The forward-looking information and statements contained in this MD&A speak only as at the date of this MD&A, and none of the Company or its subsidiaries assumes any obligation to publicly update or revise them to reflect new events or circumstances, except as may be required pursuant to applicable laws.*



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## **Restatement of Financial Results**

*As disclosed in the Company's financial statements, the Company has restated its previously reported consolidated financial statements for the year ended September 30, 2006 and interim consolidated financial statements for the three month period ended December 31, 2006. The restatement of the Company's consolidated financial statements followed an internal review of the Company's consolidated financial statements and its revenue recognition policy as it related to product returns in the U.S.*

*In the fourth quarter of 2006, the Company entered the U.S. market and recognized revenue with the revenue recognition criteria described in the notes to the consolidated financial statements. Given that the U.S. was a new market and COLD-fX<sup>®</sup> was a new product for this market, the Company has now realized that in an absence of history of returns, the criteria to recognize revenue was not met. The appropriate application of the recognition policy would have prevented the recognition of such revenues until the right of return had expired. Analysis of the Company's revenue recognition policy following the determination of slower than anticipated consumer product purchases indicated greater than anticipated risk of product return. Prior to this restatement, the Company recorded revenue from the U.S. with estimates for product returns. However, subsequent experience has now indicated that there was significant uncertainty in estimating product returns from this new market. This uncertainty should have precluded the recognition of revenue until the risk of returns was substantially eliminated.*

*The Board of Directors determined that restatement of the Company's consolidated financial statements and the appropriate application of its revenue recognition policy was warranted to correct the effects of this policy application oversight, to ensure consistency with GAAP, and to correct an overstatement of U.S. product sales. The effect of the restatement, including the identification and correction of related misstatements in the previously issued consolidated financial statements, are reflected in the Company's restated consolidated financial statements and accompanying notes.*

*The appropriate application of the revenue recognition policy also affected the Company's policy on the translation of foreign currencies. Given the effects of the restatement and the change in the financial condition of its wholly owned subsidiaries, the Company has re-evaluated its classification of its foreign subsidiaries as self-sustaining. The Company concluded that COLD-fX Pharmaceuticals (USA) Inc. and fX Life Sciences International GmbH should have been classified as integrated rather than self-sustaining foreign operations. The translation of these subsidiaries, which operate in U.S. dollars, has been amended from the current rate method to the temporal method.*

*The total cumulative impact of the restatement of the financial statements for the fiscal year ended September 30, 2006 was to decrease shareholders' equity by \$3.4 million. The cumulative impact on shareholders' equity as at September 30, 2006 was primarily the result of a reversal of \$5.6 million in net revenue recognized on U.S. shipments, which resulted in a decrease of net earnings by \$3.5 million. Total assets decreased by \$1.2 million and total liabilities increased by \$2.2 million.*

*The total cumulative impact of the restatement of the financial statements for the three month period ended December 31, 2006 was to decrease shareholders' equity by \$5.5 million. The cumulative impact on shareholders' equity as at December 31, 2006 was primarily the result of a reversal of \$2.5 million in net revenue recognized on U.S. shipments. Total assets increased by \$2.7 million and total liabilities increased by \$8.2 million.*

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## Company Overview

CV Technologies Inc. (TSX: CVO) is a life sciences and technology company, founded in 1992 and headquartered in Edmonton, Alberta, Canada. The Company has developed, commercialized and patented a proprietary technology, known as ChemBioPrint, which is used to discover and biologically standardize natural products that deliver consistent, verifiable and provable health benefits. In 2003, the Company shifted from research and development to product commercialization. Using the ChemBioPrint discovery and standardization platform, the Company's scientists are able to identify precisely the chemical profile and biological activity of natural products. The process involves a combination of chemical and biological fingerprinting ensuring the creation and scientific substantiation of its natural health products to be safe, effective and consistent. The Company is committed to using a pharmaceutical model (rigorous drug discovery and testing methods) to develop natural therapeutics for health maintenance and disease prevention. Its efforts in scientific research and product innovation are key factors enabling the Company to secure the trust of consumers, trade professionals, healthcare practitioners and government.

The Company's lead product, COLD-fx<sup>®</sup>, is designed to aid in the prevention and relief of colds and flu by strengthening the immune system. In February 2007, Health Canada issued a Natural Product Number (NPN) for COLD-fx<sup>®</sup> with the claim it "helps reduce the frequency, severity and duration of cold and flu symptoms by boosting the immune system". A U.S. Food and Drug Administration (FDA) regulated Phase II Clinical Trial showed COLD-fx<sup>®</sup> reduces the risk of getting a lab-confirmed influenza and respiratory syncytial virus (RSV) infection in a nursing home senior population by 89%. A Canadian trial in the general population, which was reported in the Canadian Medical Association Journal October 2005, showed COLD-fx<sup>®</sup> reduced the average number of infections per person by 25% and reduced the number of recurrent infections by 56%. Severity was reduced by 31% and duration was reduced by 35%. All the Company's products are designed to support normal physiological/body functions with a user-friendly, natural formula. Utilizing its patented ChemBioPrint technology, the Company has developed and commercialized a selection of premium quality natural health products for health maintenance and disease prevention.

The three principle commercial products are:

- COLD-fx<sup>®</sup>                      Helps reduce the frequency, severity and duration of cold and flu symptoms by boosting the immune system
- REMEMBER-fx<sup>®</sup>              Helps enhance memory and mental alertness
- CELL-fx<sup>®</sup>                      Helps relieve symptoms of bone and joint pain and assists in the formation of connective tissue

While the Company has no plans to market PRESSURE-fx<sup>®</sup> in Canada, it does have a distribution partner currently selling PRESSURE-fx<sup>®</sup> in the U.S. Management is contemplating the re-launch of AD-fx<sup>®</sup> and MENTA-fx<sup>®</sup> in 2008 for the Canadian market. No decision on a launch date has been reached at this time.

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## Second Quarter Highlights

- Natural Product Number received from the Natural Health Products Directorate for COLD-fx®
- Sales slow with a mild cough and cold season
- U.S. product returns
- Clinical study initiated at Hackensack University Medical Center, New Jersey

## Liquidity and Capital Resources

### Cash and working capital

As at March 31, 2007, the Company had \$11.4 million of cash or cash equivalents on hand and had \$7.7 million in working capital (Non-GAAP Financial Measure). The reduction in working capital resulted from investments in the construction of its new headquarters and research centre, and losses related to slow U.S. sales as well as significant investments in brand building and marketing in the U.S.

<b>Comparative liquidity and capital structure</b> (in thousands)	Quarter 2 Mar 31, 2007	Quarter 2 Mar 31, 2006	Fiscal Year Sep 30, 2006 Restated	Fiscal Year Sep 30, 2005
Cash and cash equivalents	11,431	21,274	7,913	5,952
Working capital <sup>1</sup>	7,654	23,995	16,385	16,928
Year to date EBITDA <sup>1</sup>	(2,636)	9,695	4,464	8,967
Long-term liabilities	764	95	745	70
Shareholders' Equity	18,093	26,946	23,525	19,840

<sup>1</sup> See Non-GAAP Financial Measures and Reconciliations

The combined effects of investments in sales, marketing and public awareness programs related to entry into the U.S. marketplace and slow U.S. sales contributed to the \$12.3 million reduction in year to date net earnings from the prior year. Consolidated loss after tax was \$3.3 million compared to net earnings of \$1.0 million for the same quarter of the previous year. Cash flows from the Canadian operations in the second quarter partially offset the effects of slow sales, and higher advertising and marketing expenditures in the U.S.

### Cash flow from operations

The Company's total operating expenses for the quarter was \$8.2 million and for the six month period ended March 31, 2007 was \$25.0 million. These expenses included non-cash operating costs (stock

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compensation and amortizations) of \$815 thousand for the three month period and \$1.6 million for the six month period ended March 31, 2007.

In the second quarter of fiscal year 2007, the cash flow used by operations was \$6.3 million. The primary differences were from a loss for the quarter (\$3.3 million), a decrease in accounts payables (\$6.6 million) and decrease in income taxes payable (\$1.5 million), offset by future taxes (\$1.2 million) and increases in accounts receivables (\$2.7 million), stock-based compensation (\$0.6 million) and inventory (\$0.5 million).

In comparison to the second quarter of the prior year when cash generated by operations was \$4.0 million, the cash flow used in the second quarter of fiscal year 2007 was \$6.3 million. The primary differences between the quarters were from decreases in earnings of (\$4.3 million), accounts payables (\$5.4 million) and taxes payable (\$2.6 million) offset by increases in futures taxes (\$1.2 million) and inventory (\$1.5 million).

In comparison to the first six months of the prior year when cash flow generated by operations was \$15.6 million, the cash flow generated in the first six months of fiscal year 2007 was \$7.1 million. Year to date, the primary differences contributing to the reduction of \$8.5 million in cash were a result of a decrease in earnings of (\$12.3 million), a decrease in accounts receivables (\$2.1 million), a decrease in future income taxes (\$1.9 million), a decrease in inventory (\$1.7 million), a decrease in accounts payable (\$1.4 million) and a decrease in taxes payable (\$5.5 million). These cash outflows were offset by an increase in customer deposits (\$15.6 million) and a decrease in prepaid expenses (\$0.9 million).

Cash was used to invest in inventory. The Company manages supply risk by establishing and maintaining a scheduling program to ensure a one-year supply of bulk ingredients and a finished goods inventory is maintained to meet seasonal demand. Slow U.S. sales and planning decisions to build inventory to ensure product availability in the U.S. with uncertain consumer demand in the U.S. marketplace resulted in significant quantities of inventory on hand. Inventory valuation is based on direct costing of its products. Product sales of \$50 million require approximately \$8 million in finished goods and bulk ingredients.

<b>Major cash flow components (in thousands)</b>	<b>Quarter 2 Mar 31, 2007</b>	<b>Quarter 2 Mar 31, 2006</b>	<b>Year to Date Mar 31, 2007</b>	<b>Fiscal Year Sep 30, 2006 Restated</b>	<b>Fiscal Year Sep 30, 2005</b>
Operating activities	(6,312)	3,998	7,109	4,180	6,124
Financing activities	14	152	194	296	855
Investing activities	(2,156)	(255)	(3,785)	(2,515)	(846)

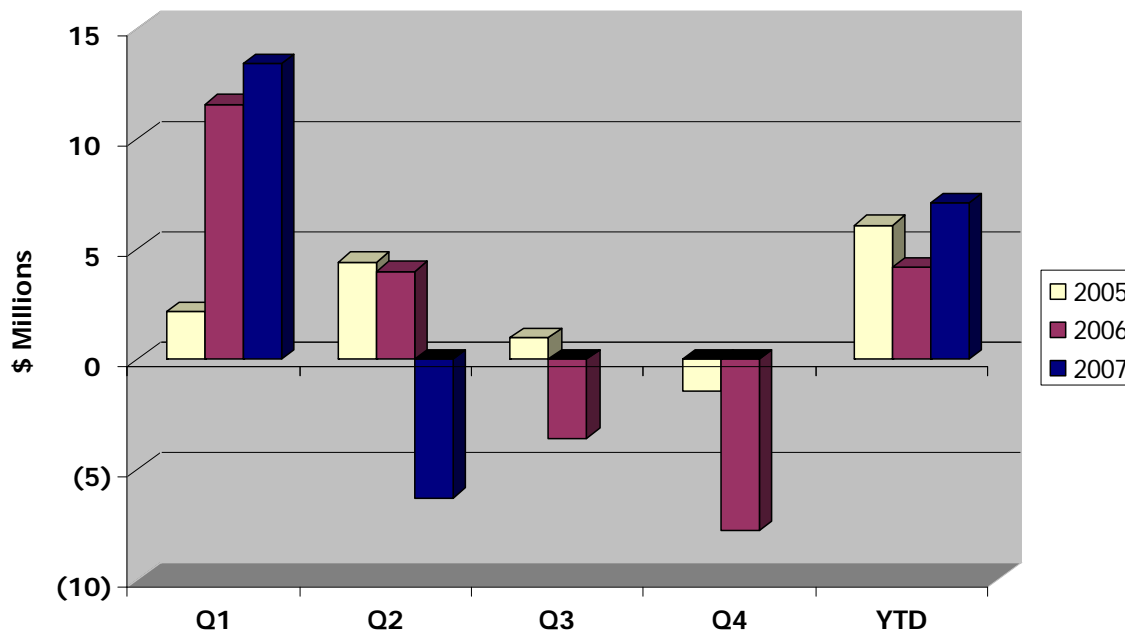
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The following chart illustrates quarterly cash flows from operations in fiscal years 2005 through 2007.

Cash Flow from Operations



## Cash flow from financing activities

The Company's financing activities in the second quarter of fiscal year 2007 provided \$14 thousand in cash (\$152 thousand in same quarter of fiscal year 2006). Financing activities for 2007 were predominantly composed of \$18 thousand received through the issuance of capital stock on the exercise of stock options (25,500 common shares at an average of \$0.71 per share). Repayment of leases in the second quarter was \$4 thousand compared to \$6 thousand in the same quarter of fiscal 2006.

## Cash flow used in investing activities

The Company's investing activities in the second quarter used \$2.2 million (\$255 thousand in the second quarter of fiscal year 2006). Investing activities primarily involved the construction of the Company's new corporate headquarters and research centre. The forecasted cost of the building construction is \$9.6 million. Expenditures for patents and registered trademarks involved the protection and development of its intellectual property.

The Company announced the construction of a new headquarters on July 17, 2006. The 28,320 square foot two-storey Edmonton building is located on a 4.6-acre parcel of land leased by the Company under Edmonton Economic Development Corporation's Biotechnology Lease Program. To date, construction is estimated to be 65% complete. The forecasted occupancy date is mid-August 2007. Although the project is slightly behind schedule, Management anticipates no significant delays. The schedule was lengthened due

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to availability of trades and general labourers, certain materials, and exceptionally wet winter and spring seasons. No major spending variances are expected given that most major contracts have been finalized.

## Liquidity

In the restated first quarter interim consolidated financial statements, the Company has reversed the revenue recognition of U.S. product shipments with an implicit or explicit right of return and reclassified customer payments on shipments of inventory as customer deposits. In the previously issued financial statements, management recorded a provision for returns, reducing net revenues by \$0.3 million for the fiscal year ended September 2006 and \$12.5 million in the first quarter ended December 31, 2006.

At the end of March 31, 2007, customer deposits of \$17.4 million represented payments received on shipments of inventory with a right of return. When the risk of product return is substantially eliminated, the revenue from the product shipped is recognized and liability is eliminated. If the product is returned, the customer is entitled to a refund of the deposit. Subsequent to March 31, 2007, the Company refunded \$5.8 million of customer deposits. Additional returns have been authorized requiring refund of approximately \$5.9 million. The amount and the timing of the actual returns and the effect of cash refunds on the Company's cash position is difficult to predict. The Company is also discussing plans with U.S. retailers to delay customer refunds until the fall selling season. The initial response has been positive.

As of March 31, 2007, estimated inventories were \$20.2 million. Although a large inventory positively affects working capital, the turnover of the U.S. inventory is anticipated to be slow over the next 6 to 12 months. Consequently, the Company has decided that it is prudent to bring some U.S. product into Canada for sale this fall. Bottled U.S. product, which has undergone the same quality testing as performed in Canada, can be repackaged making it available for Canadian sales. The additional costs to repackage inventory are anticipated to reduce gross margins by 5 to 7%. Because sales are seasonally slow during the summer, initiation of the cycling of inventory into receivables and cash receipts in Canada is anticipated to take place in the fourth quarter of fiscal year 2007, and the first two quarters of fiscal year 2008. As of December 31, 2006, the estimated inventory was \$20.7 million, of which \$3.5 million is product shipped to customers with the right of return.

The Company's U.S. experience has shown that shipments and the resulting invoices may be at risk of payment delay as customers are monitoring their sales to consumers. Though the customer has been invoiced and payment is expected, U.S. receivables are not recognized in the consolidated financial statements until the risk of return is substantially eliminated. The turnover of payment on invoiced U.S. shipments is expected to be slow. In Canada, cash receipts of accounts receivable are typically within 30 to 60 days. In the summer months, cash flow from collection of receivables decreases, with slowing sales.

The timing of refunds on customer deposits related to returned product and slow summer sales will affect cash flow and likely require the Company to utilize its bank line or alternative sources of funding. There is uncertainty on when customer returns will occur and when customer refunds will be expected. The current bank line of credit has an inventory ceiling of \$5 million or 50% of inventory, whichever is lower (See Subsequent Events).

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Until the Company completes the restatements and meets the conditions set forth in the cease trade order, the Company can not finalize discussions on equity financing. The Company continues to work diligently to have such cease trade orders lifted (See Subsequent Events).

The Company's working capital and capital expenditure requirements depend upon numerous other factors including the success and timing of the introduction of new products or entry into new markets, consumer demand, right of returns held by customers, timing of market development programs, construction costs and long-term focus on product research and development activities. The Company anticipates developing a need for additional capital to fund operations, capital asset additions, research and development, new product launches, and strategic initiatives.

## Share capital, stock-based compensation and director's compensation

On December 8, 2006, the directors approved a compensation system to align with industry standards. Effective January 1, 2007, director compensation moved to cash compensation increasing the annual retainer to all Board members, the Board chair and committee chairs. The revised compensation system is as follows: Annual Retainer-\$25,000, Board Chair-additional \$15,000, Committee Chair-additional \$5,000, Board Meeting-\$1,000 and Committee meeting-\$500. The Compensation Committee annually reviews and recommends to the Board the form and amount of director compensation.

On December 14, 2006, the Board granted 100,000 options for common shares exercisable at a fair market value of \$2.98 per share vesting at 20% per year. The fair value of options granted was \$235 thousand or \$2.35 per option. This grant was subject to shareholder approval and passed at the Annual General Meeting held in February 2007.

In January 2007, an employee exercised 25,500 options for cash proceeds of \$18,105.

Pursuant to a shareholder resolution on February 21, 2007, the Company adopted amendments to the Company's stock option plan that permits the Board of Directors to grant to employees, officers and directors options to purchase from Treasury up to 22,170,442 common shares. This change is an increase of 3,000,000 common shares from the previous limit of 19,170,442 common shares.

Subsequent to March 31, 2007 Dr. Shan voluntarily surrendered and relinquished all rights and privileges associated with the March 2005 option grant. (See Subsequent Events).

## Lease obligations

The Company has renewed existing operating leases and entered into new operating leases related to premises. These leases expire at various dates ranging from May 31, 2008 to October 31, 2009. As of March 31, 2007 the cumulative obligation of these leases is \$111,924.

## Related party transactions

There were no related party transactions for the three month period ended March 31, 2007.

During the fiscal year 2006, the Company paid \$14,914 (2005 - \$30,080) in supplemental study fees to an independent third party on behalf of Vet Ex Inc., which is controlled by the Company. This project involves

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an animal study on the effect of HT1001, the active ingredient in REMEMBER-FX<sup>®</sup> on memory and cognition in adult dogs. The central nervous systems of dogs have similarities to humans and findings in this study would support research on REMEMBER-FX<sup>®</sup>.

## Outstanding shares

As of June 14, 2007;

- Number of issued and outstanding common Class A shares 103,551,006
- Number of outstanding, unexercised stock options 10,592,935

(Exercise price ranges from \$0.15 to \$4.32 per share with expiration dates ranging from 2007 to 2011.)

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## Results of Operations

### Profitability

Consolidated loss after taxes was \$6.9 million compared to consolidated net earnings of \$5.4 million for the six month period of the prior year, a decrease of \$12.3 million. The loss before taxes was \$2.9 million compared to net earnings of \$9.6 million for the same six month period last year.

The quarterly consolidated loss after taxes was \$3.3 million compared to consolidated net earnings of \$1.0 million for the same quarter of the prior year, a decrease of \$4.3 million. The loss before taxes was \$2.1 million compared to net earnings of \$2.1 million for the same quarter last year.

Slow product sales in the U.S., higher fixed operating costs, expenditures in marketing and business development, and higher cost of goods manufactured for the U.S. affected consolidated net earnings. The consolidated loss in the second quarter reflected the expenditures in distribution, logistics, marketing and business development incurred in the execution of the launch of COLD-fx<sup>®</sup> into the U.S. market. Canadian sales and gross margin in the second quarter partially offset the impact of U.S. investment expenditures. An analysis of components of the earnings statement is as follows.

### Revenue

The Company reported net product sales of \$7.8 million for the second quarter, a decrease of 28.1% from the \$10.9 million reported in the same quarter in fiscal 2006. Net sales for the first six months of fiscal 2007 totalled \$30.5 million, an increase of 2.0% from the \$29.9 million of the corresponding period in the previous year.

The Company enjoyed a 19.4% increase in net sales in the first quarter when compared to the same quarter of the prior year, led by the Company's lead product COLD-fx<sup>®</sup> in Canada. The second quarter sales compared to the same period last year decreased, as there was a decline in the incidence of colds and flu in Canada, which slowed customer replenishment orders in the second quarter. A national decrease of 9% in the number of respiratory illnesses as reported by the Flu/Cold/Respiratory Illness Activity Notification (FAN<sup>®</sup>) Program from Surveillance Data Intelligence (SDI) for the 28-week period ending March 23, 2007 contributed to a decline in consumer demand. The decrease in cold and flu activity was most pronounced in Western Canada, historically the leading sales region for COLD-fx<sup>®</sup>.

Although second quarter U.S. net sales were \$367 thousand, the Company made good progress in developing strong distribution channels with the major U.S. drug store chains for its U.S. launch in October.

U.S. sales growth was less than anticipated, partially because of higher introductory promotional programs, discounts, and allowances, which collectively reduced gross sales by more than the anticipated 10 to 12%. In addition, non-refundable discounts on shipments with a right of return were applied to gross revenues from recognized sales. The U.S. market will require time to develop consumer awareness, permit consumers to try COLD-fx<sup>®</sup> and generate the positive word of mouth experiences already achieved within Canada.

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The science and credibility behind the brand is not limited to Canada. Management will build on the scientific evidence and focus on building awareness through alternative and medical channels. This approach should help to leverage sales through the strong distribution channels developed over the past months. The lifecycle of the brand development is at an earlier point within the U.S. when compared to Canada. Execution across consumer and medical segments should position COLD-fx<sup>®</sup> favourably in the long term.

The Company has achieved extensive brand exposure in many different media segments in support of the U.S. launch through a comprehensive program of marketing and public awareness. However, brand building in the U.S. will also require patience to garner the same success experienced in Canada. As the Company executes its business plan, management believes consumers will benefit from and experience the medical benefits of COLD-fx<sup>®</sup>.

The second quarter also represented a period of reduced investment in marketing support in the U.S. to better align expenses with sales.

COLD-fx<sup>®</sup> continues to be the number one selling cold and flu remedy in Canada (ACNielsen's MarketTrack Drug Service for Cold Remedies, Natural Supplements & Vitamins Categories for the 52-week period ending September 2, 2006).

## Gross margin and inventories

Gross margin in the second quarter was 70.9%, a decrease of 4.7 % from 75.6% in the same quarter in fiscal year 2006 and a decrease of 3.0% from 73.9% in the first quarter of fiscal year 2007. The gross margin decrease was primarily the result of distribution and logistic costs associated with the U.S. inventories and an expensing of display materials on product with a right of return. In addition, the decrease in gross margin is attributed to reworking of products returned by U.S. retailers. Gross margins are expected to decrease during the summer as sales decrease relative to fixed costs and as U.S. inventories are repackaged.

In order to manage the Company's inventory levels, no new manufacturing activities were carried out in Canada and the U.S. during the second quarter. This curtailment will continue until on-hand inventory has been consumed.

The Company's inventory management strategy has the following priorities:

1. Package all bulk capsule inventories already in Canada
2. Repackage returning U.S. finished goods
3. Package all bulk capsules returning from the U.S.
4. Encapsulate and package bulk extracts from the U.S.
5. Encapsulate and package bulk extracts already in Canada and
6. Extraction of ingredients from raw materials

The Company plans to ship excess U.S. inventory to Canada for repackaging. All returning products must meet a rigorous quality assurance and control process. The Company does not anticipate any border crossing issues and anticipates commencing the repackaging of U.S. materials in late summer of 2007. Cost of shipment of products back to Canada is approximately US\$90,000.

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The Company is actively seeking refunds from U.S. Customs for duties previously paid based on a previous favorable ruling. In the interim, the Company is still subject to a U.S. import duty, applied to the declared value of COLD-fX<sup>®</sup> raw material, work in process and finished goods. No U.S. bound COLD-fX<sup>®</sup> shipments were made in the second quarter of 2007. On December 18, 2006, the Company received an advance ruling from Canada Border Services Agency (CBSA) supporting the Company's request to reclassify COLD-fX<sup>®</sup> bulk powder to support a 0% related duty. The Company plans to use the Canadian ruling to classify its product in its application to the U.S. for the elimination and refund of duties paid on imports into the U.S. in the current and past fiscal years.

Management anticipates that the current manufacturing stoppage will affect the Company's Contract Manufacturing Organizations (CMO's). As a result, one of the priorities for the third quarter is to protect working relationships with suppliers and CMO's. The Company plans to provide frequent updates to its partners on future production and distribution plans.

## Operating expenses

The second quarter operating costs as a percentage of sales increased from 57.5% to 104.0% on a quarter-over-quarter basis (from 41.2% in fiscal year 2006 to 82.2% in fiscal year 2007, on a year to date basis). The Company invested heavily in its U.S. launch resulting in a significant increase in advertising and marketing expenses in the first six months of fiscal year 2007. Operating expenses for the second quarter of fiscal year 2007 were \$8.2 million as compared to \$6.3 million in same quarter of the prior year.

This \$1.9 million (30.2%) increase over the same quarter from the prior year is comprised of the following:

- Advertising and marketing expenses increased by \$1.8 million (84.9%) in efforts to support entry and meet commitments in the U.S. Expenses decreased by \$7.0 million from the first quarter. Expenditures included a continuation of brand building efforts for COLD-fX<sup>®</sup>, REMEMBER-fX<sup>®</sup> and CELL-fX<sup>®</sup>, reductions in media and promotional activities in the U.S., and maintenance of sponsorship commitments. In fiscal year 2006, second quarter spending was 18.9% of net sales compared to 48.7% for the same quarter in fiscal year 2007.
- Contracted services, consulting and professional fees decreased by \$0.1 million (13.9%) from the same quarter in the previous year, and \$1.5 million from the previous quarter. The Company reduced the number of contractors and professionals in sales, marketing, brand building, and regulatory affairs to support its entry into the U.S. Included in these costs were ongoing contracts supporting sales, marketing, and public relations. In fiscal year 2007, these second quarter expenditures were 10.3% of net sales compared to 8.6% for the same period in the prior year.
- Salaries and stock-based compensation increased by \$0.1 million (7.3%). This increase reflects the increase in the number of employees in support of the U.S. expansion. The Company anticipates reducing costs to compensate for U.S. sales and marketing spending. Stock-based compensation expense decreased \$0.3 million while wages increased \$0.4 million. In fiscal year 2006, second quarter spending was 16.2% of net sales compared to 24.2 % in fiscal year 2007.

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- Research and development expenditures for the second quarter increased \$0.2 million (31.9%) from the same quarter of last year. This increase was primarily the result of additional staff and costs that included clinical research and development associated with ongoing studies. The Company continued its clinical trial in collaboration with Capital Health of Edmonton and the University of Alberta, including a multi-centre clinical trial involving senior citizens in Vancouver, Edmonton, Toronto and Halifax. These expenditures were 9.1% of net sales in the second quarter of 2007 compared to 5.0% for the same period in the prior year.
- Administration, occupancy and insurance costs decreased by \$55 thousand (7.3%). These costs were 8.9% of net sales in the second quarter of 2007 compared to 6.9% for the same period in the prior year.

The Company had a foreign currency translation loss of \$340 thousand. The Company is now classifying its foreign subsidiaries as integrated operations rather than self-sustaining. Prior to restatement, the financial statements reported the foreign currency translations as other comprehensive income in the statement of equity.

Income taxes for the quarter were \$1.2 million compared to \$1.1 million for the same period last year. Income taxes exceeded the consolidated before tax earnings. While Canadian earnings attracted tax, investments in the U.S. market created a loss from foreign operations. Since the Company is taxed in the countries in which it operates, application of losses from one country against the taxable income of another country is not possible.

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## U.S. launch

During the fourth quarter of fiscal year 2006 and first quarter of 2007, the Company completed initial shipments to U.S. national accounts to stock stores and warehouses. Completion of the national distribution and listings phase was a significant milestone in the execution of the U.S. plan. This created a base and presence supporting sales and further product awareness and brand building across North America.

Sales to U.S. consumers are expected to slow during the summer and increase at the end of the summer. Customers have stocked their stores. Consumer awareness and acceptance will take time to build.

<b>Segmented Revenue</b>					
<small>(in thousands)</small>					
<b>2007</b>	<b>1<sup>st</sup> Quarter Dec 31, 2006 Restated</b>	<b>2<sup>nd</sup> Quarter Mar 31, 2007</b>	<b>3<sup>rd</sup> Quarter Jun 30, 2007</b>	<b>4<sup>th</sup> Quarter Sep 30, 2007</b>	<b>Year to Date 2007 Restated</b>
Canada	22,191	7,483			29,674
U.S.	424	366			790
Other	-	-			-
<b>Total</b>	<b>22,615</b>	<b>7,849</b>			<b>30,464</b>
<b>2006</b>	<b>1<sup>st</sup> Quarter Dec 31, 2005</b>	<b>2<sup>nd</sup> Quarter Mar 31, 2006</b>	<b>3<sup>rd</sup> Quarter Jun 30, 2006</b>	<b>4<sup>th</sup> Quarter Sep 30, 2006 Restated</b>	<b>Fiscal Year 2006 Restated</b>
Canada	18,939	10,873	3,242	8,282	41,336
U.S.	-	2	-	8	10
Other	1	40	-	-	41
<b>Total</b>	<b>18,940</b>	<b>10,915</b>	<b>3,242</b>	<b>8,290</b>	<b>41,387</b>
<b>2005</b>	<b>1<sup>st</sup> Quarter Dec 31, 2004</b>	<b>2<sup>nd</sup> Quarter Mar 31, 2005</b>	<b>3<sup>rd</sup> Quarter Jun 30, 2005</b>	<b>4<sup>th</sup> Quarter Sep 30, 2005</b>	<b>Fiscal Year 2005</b>
Canada	11,304	10,474	2,775	7,189	31,742
U.S.	-	3	61	-	64
Other	-	44	-	-	44
<b>Total</b>	<b>11,304</b>	<b>10,521</b>	<b>2,836</b>	<b>7,189</b>	<b>31,850</b>

Consolidated advertising expenditures for the first six months were \$14.7 million (48.2%) of product sales. Media and advertising expenses related to the U.S. were \$10.1 million for the first six months (\$1.9 million in the second quarter). The Company anticipates reducing spending in the U.S. in the remainder of 2007.

The large increase in advertising expenditures experienced to support sales was the result of efforts to build brand awareness of COLD-fX<sup>®</sup> through mass media channels, and to support a national launch by retailers in October in the U.S. The Company has fixed expenses under contract with the NHL, Mark Messier International, and other commitments.

When it was determined that the advertising and marketing expenditures were not generating the anticipated sales, the Company significantly reduced spending in the second quarter of fiscal year 2007. The Company anticipates a continuation of marketing sponsorship, professional education, and promotion expenditures in a consistent manner for the balance of 2007 fiscal year, but it has reduced advertising

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expenditures through the media. In the U.S., expenditures in the second quarter were significantly higher than achieved product sales. However, a continued reduction and alignment of marketing expenditures will take place in the last half of fiscal year 2007 as the Company implements a more disciplined approach to growth and controls. Part of that discipline will be demonstrated by a more targeted marketing plan, which is expected to involve alternative distribution channels in addition to mass retailers and more targeted communication channels to reach consumers.

## Research and development activity

fX Life Sciences International GmbH, a wholly owned subsidiary, reported last quarter that a second patent was allowed in the U.S. for its CVT-E002 extract, the active ingredient in COLD-fX<sup>®</sup>. As of March 6, 2007 the patent was issued and assigned the U.S. patent number 7 186 423. This patent application is a continuation of the composition patent and further protects CVT-E002 for use in therapeutic applications for preventative, immune-related indications, such as cold and flu infections, hepatitis, HIV, and primary and supportive cancer therapy.

The fX Life Science International GmbH patent entitled "A preparation derived from shark cartilage for treatment of diseases related to excessive PHF (Parathyroid Hypertensive Factor) or excessive intracellular calcium" has also been issued in China and allowed in Hong Kong.

The Company is in the second year of the multi-centre trial, led by Dr. Gerald Predy, Edmonton's Medical Officer of Health, to test the effects of COLD-fX<sup>®</sup> on influenza and cold viral infections. Completion of recruitment for all four sites occurred in December 2006 and the study has moved into the treatment period for the current cold and flu season.

The Company continues to review the potential of a Phase III clinical trial to support a U.S. Over-The-Counter (OTC) new drug cold and flu application for CVT-E002, the active ingredient in COLD-fX<sup>®</sup>.

The Company continued the funding for a pre-clinical research study at McGill University under the direction of Dr. Sandra Miller, Professor, Department of Anatomy and Biology in the Faculty of Medicine until the end of 2006. This study investigated the potential of CVT-E002 (the active ingredient in COLD-fX<sup>®</sup>) to ameliorate leukemia caused by viral infection and the positive results support the hypothesis that CVT-E002 may have potential as a cancer therapy and may also support the immune system during cancer treatment. The project has ended on schedule and the data is currently being prepared for submission to a scientific journal for publication. The Company is currently investigating future developments in this area.

The National Research Council (NRC) under the Industrial Research Assistance Program (IRAP) is currently funding the Company's research program to clarify the molecular mechanism of action of CVT-E002. Under this program, the Company has entered into a research contract with McMaster University in Hamilton to support a study on CVT-E002 led by Dr. Kenneth Rosenthal, Professor and Director of Molecular Medicine in the Department of Pathology and Molecular Medicine at McMaster University. This study is under way for the remainder of 2007 and the Company is exploring further collaborations under this program.

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On February 7, 2007, the Company announced that doctors and nurses at Hackensack University Medical Centre (HUMC) in New Jersey would participate in a randomized, double-blind, placebo-controlled trial of COLD-fx<sup>®</sup> to evaluate improvements in the immune health of front line medical workers.

HUMC infectious diseases researcher, Dr. Steven Sperber, is heading the study, which will include blood tests to investigate the hypothesis that COLD-fx<sup>®</sup> works by simultaneously boosting two different immune pathways: the innate response (macrophages and Natural Killer (NK) cells) and the Th1 adaptive response. Both pathways are critical for fighting viruses and maintaining good health. The hypothesis is supported by previously published clinical research which demonstrated that regular intake of COLD-fx<sup>®</sup> over one cold season enhanced NK cells and T-helper cells.

If confirmed, COLD-fx<sup>®</sup> will be the first dietary supplement clinically proven to work synergistically by enhancing both of these immune pathways. There are currently no approved medicines, which act in this novel manner. The study will complement additional Canadian government-funded research being conducted at McMaster University in Ontario on the precise molecular mechanism of action of COLD-fx<sup>®</sup>.

Dr. Sperber is recruiting healthy staff members from HUMC for the trial including doctors and nurses. The parameters being measured are blood immune factors which are highly sensitive and therefore do not require a high number of trial subjects.

As previously mentioned, Health Canada approved a new wide-ranging health claim for COLD-fx<sup>®</sup> on February 13, 2007. After an extensive review, the NHPD issued a product license and NPN for COLD-fx<sup>®</sup>. The comprehensive treatment claim for COLD-fx<sup>®</sup> approved by Health Canada states that the product "helps reduce the frequency, severity and duration of cold and flu symptoms by boosting the immune system". The approved dosage is two capsules per day. Comprehensive therapeutic claims require support by the highest level of scientific evidence: randomized, double-blind, placebo-controlled clinical trials. The Company is seeking a separate NPN for a higher acute dose similar to the dosing regimen of the previous DIN for COLD-fx<sup>®</sup> under an application that was submitted to the NHPD on March 9, 2007.

On March 1, 2007, the Company announced that the American Botanical Council (ABC), North America's leading nonprofit research and education organization on herbal medicines published a major U.S. scientific review (monograph) of COLD-fx<sup>®</sup>, conducted by leading American cold and flu experts. Five independent U.S. physicians and scientists, well recognized in the field of natural medicines, were involved in the writing and peer review of this scientific report on COLD-fx<sup>®</sup>, which concludes the cold and flu remedy delivered "impressive" benefits to users.

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<b>Summary of Quarterly Results</b> (in thousands)					
<b>2007</b>	<b>1st Quarter</b> Dec 31, 2006 Restated	<b>2nd Quarter</b> Mar 31, 2007	<b>3rd Quarter</b> Jun 30, 2007	<b>4th Quarter</b> Sep 30, 2007	<b>Year to Date</b> 2007 Restated
Product sales	22,615	7,849			30,464
Gross margin	16,710	5,569			22,279
Gross margin %	73.9%	70.9%			73.1%
Earnings (loss) before tax	(741)	(2,123)			(2,864)
Earnings (loss) after tax	(3,584)	(3,296)			(6,880)
EPS – Basic	\$(0.03)	\$(0.03)			\$(0.07)
EPS – Diluted	\$(0.03)	\$(0.03)			\$(0.07)
Total assets	60,078	49,254			49,254
Total liabilities	39,335	31,162			31,162
<b>2006</b>	<b>1st Quarter</b> Dec 31, 2005	<b>2nd Quarter</b> Mar 31, 2006	<b>3rd Quarter</b> Jun 30, 2006	<b>4th Quarter</b> Sep 30, 2006 Restated	<b>Fiscal Year</b> 2006 Restated
Product sales	18,940	10,915	3,242	8,290	41,387
Gross margin	13,414	8,253	2,220	4,213	28,100
Gross margin %	70.8%	75.6%	68.5%	50.8%	67.9%
Earnings (loss) before tax	7,463	2,087	(2,428)	(2,982)	4,140
Earnings (loss) after tax	4,416	987	(1,772)	(2,992)	639
EPS – Basic	\$0.04	\$0.01	\$(0.02)	\$(0.02)	\$0.01
EPS – Diluted	\$0.04	\$0.01	\$(0.02)	\$(0.02)	\$0.01
Total assets	32,319	34,277	33,545	43,132	43,132
Total liabilities	7,458	7,331	7,737	19,607	19,607
<b>2005</b>	<b>1st Quarter</b> Dec 31, 2004	<b>2nd Quarter</b> Mar 31, 2005	<b>3rd Quarter</b> Jun 30, 2005	<b>4th Quarter</b> Sep 30, 2005	<b>Fiscal Year</b> 2005
Product sales	11,304	10,521	2,836	7,189	31,850
Gross margin	8,355	8,352	2,250	5,162	24,119
Gross margin %	73.9%	79.4%	79.3%	71.8%	75.7%
Earnings (loss) before tax	4,196	3,081	(466)	1,725	8,536
Earnings (loss) after tax	4,196	3,081	(466)	3,282	10,093
EPS – Basic	\$0.05	\$0.03	\$(0.00)	\$0.02	\$0.10
EPS – Diluted	\$0.04	\$0.03	\$(0.00)	\$0.02	\$0.09
Total assets	13,819	17,762	17,909	23,717	23,717
Total liabilities	4,020	2,377	2,182	3,876	3,876

COLD-fx<sup>®</sup> is the Company's best selling product. Consumers use the product to strengthen their immune system to prevent and treat colds and flu. As a result, COLD-fx<sup>®</sup> sales exhibit a seasonal sales pattern. Customers commence purchasing in the fourth quarter, which carries forward into the first and second quarters of the following year. The spring and summer months are slow selling periods, while late summer, fall and winter experience significantly greater sales volume with the increase in the frequency and severity of colds and flu. Retailers will commence purchasing in late August and September and replenish stock as required.

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## Corporate Development

On February 13, 2007, the status of Vet Ex Inc., the joint venture with Centaur Pharmaceuticals became inactive.

## Changes in Senior Management

On February 21, 2007, the marketing responsibilities of Norman Oliver were reassigned to John Rea, who was appointed Vice President, Marketing and Communications. Dr. Sharla Sutherland was appointed Vice President, Regulatory & Scientific Affairs.

On March 26, 2007, Norman Oliver, Senior Vice President Sales & Customer Development, was no longer associated with CV Technologies Inc. Mr. Oliver's initial responsibilities included marketing and sales in Canada and the U.S. Mr. Oliver's most recent responsibilities included sales and customer development. Those duties have been reassigned internally on an interim basis.

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## Subsequent Events

### Stock options

On May 10, 2007, Dr. Jacqueline Shan voluntarily surrendered and relinquished all rights and privileges associated with the March 2005 option grant. This was accepted by the Board of Directors at the May 14, 2007 meeting. The forfeiture of these options results in a recovery of \$3.6 million of stock-based compensation expense previously recognized. This was accepted by the Board of Directors at their May 14, 2007 meeting.

### Senior management

On May 7, 2007, the Company announced the appointment of Ross Montagano as Chief Operating Officer, effective May 28, 2007.

### Business development

On April 19, 2007, the Alberta Securities Commission (ASC) issued an Interim Cease Trade Order (ICTO) halting trading of the Company's securities for 15 days. The action followed the Company's April 11, 2007 announcement that it was voluntarily planning to restate its consolidated financial statements for the year ended September 30, 2006, as well as its interim consolidated financial statements for the three month period ended December 31, 2006 due to revenue recognition in the U.S. market. The Company, under the guidance of the Board of Directors decided to correct the Company's revenue as it relates to the entry into new markets or introduction of new products where the right of return is uncertain. The Company has corrected the application of this policy because of the difficulty in estimating consumer uptake and the risk of product return by retailers.

On May 2, 2007, the ASC issued a Consent Order extending the Interim Cease Trade Order of April 19, 2007 until the earlier of the satisfaction of the conditions set forth below and June 15, 2007.

The conditions set forth in the Consent Order include that:

- (i) All deficiencies, inconsistencies and omissions in the Company's previously delivered Financial Statements have been corrected by filing revised or amended Financial Statements pursuant to Part 4 of National Instrument 51-102 Continuous Disclosure Obligations (NI 51-102) that are in accordance with acceptable accounting principles as required by section 3.1 of National Instrument 52-107 Acceptable Accounting Principles, Auditing Standards and Reporting Currency;
- (ii) The Company has issued a press release pursuant to Part 11 of NI 51-102 explaining the reasons for requiring revised or amended Financial Statements;
- (iii) The Company is not in default of any other filing requirements under the Securities Act (Alberta); and
- (iv) The staff of the ASC has confirmed in writing that CV Technologies Inc. has satisfied the three foregoing conditions.

If all four conditions are not satisfied by June 15, 2007, CVQ and Staff of the ASC are directed to appear before the ASC for further advice and direction.

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The Company was subject to a similar Temporary Order of the Ontario Securities Commission (OSC) dated April 23, 2007, which ceases all trading in and all acquisitions of the securities of the Company, whether direct or indirect, for a period of 15 days from April 23, 2007. A hearing before the OSC in respect of the Temporary Order was held on May 4, 2007.

On May 7, 2007, the OSC implemented an Order which has the effect of continuing the foregoing cease trade for an indefinite period. Staff of the OSC have confirmed to the Company that as the ASC is the principal regulator of the Company in accordance with CSA Staff Notice 51-312 Harmonized Continuous Disclosure Review Program (CSA Staff Notice 51-312), it is the intention of Staff of the OSC to apply the principles described in CSA Staff Notice 51-312 for the purposes of assessing the satisfaction of the Company's voluntary plan to restate its consolidated financial statements for the year ended September 30, 2006, as well as its interim consolidated financial statements for the three month period ended December 31, 2006.

The Company was subject to a Cease Trade Order of the British Columbia Securities Commission (BCSC) dated May 24, 2007, which ceases all trading in and all acquisitions of the securities of the Company, whether direct or indirect, until:

- (i) The Company files an interim financial statement for the financial period ended March 31, 2007 and a Form 51-102F1 Management's Discussion and Analysis for the financial period ended March 31, 2007.
- (ii) The Executive Director makes an order under section 164 of the Securities Act revoking this cease trade order.

## Financing facilities

On June 12, 2007, the Company entered into a commitment letter granting the Company a demand operating line of credit up to a maximum of \$10,000,000. The demand operating line of credit is based on 75% of accounts receivable plus 50% of finished goods inventory for the period of September to February or 65% of finished goods inventory for the period of March to August. Inventory has a maximum limit of \$6.0 million. As part of the operating line facility, the Company has the ability to issue up to \$1 million of letters of guarantees. Interest under the operating line facility is based on the Bank of Canada prime rate or Bankers' Acceptance rate plus 1.5% per annum.

In addition, the new financing arrangement offers a three year term financing for the construction of the new headquarters and research centre on land held under a capital lease. The amount of term financing will be based on 65% of the revised appraised value of the building or 65% of the cost of the building, whichever is lower. The interim facility will bear interest at the Bank of Canada rate plus 0.75% per annum; the Company can also fix the interest rate.

The collateral security lodged by the Company to support both financing facilities is a General Security Agreement constituting a first ranking security interest in all personal property of the Company, a Collateral Mortgage constituting a first fixed charge on the Company's headquarters and research centre on the subleased land and a guarantee provided by an insider of the Company, secured by common shares.

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## Outlook

The U.S. market will require time to develop consumer awareness, permit consumers to try COLD-fx<sup>®</sup> and generate the word of mouth confidence already achieved within Canada. The science and credibility behind the brand is not limited to Canada. Management will build on the scientific evidence and focus on building awareness through alternative and medical channels. This approach should help to leverage sales through the strong distribution channels developed over the past months. The lifecycle of the brand development is at an earlier point within the U.S. when compared to Canada. Execution across consumer and medical segments should position COLD-fx<sup>®</sup> favourably in the long term.

The Company will continue to strengthen and restructure the senior management team, optimize and align its U.S. investment strategy with sales, and implement its marketing plan that is more targeted to health conscious consumers and their influencers. The Company is strengthening its team with the addition of Ross Montagano, who joined in late May as Chief Operating Officer. The Company is implementing a number of sales (including the possible launch of new products in Canada this year), marketing and public relations strategies and programs to achieve these goals. These strategies include the pursuit of marketing and distribution strategic partners for the U.S.

Management will also work to enhance demand for REMEMBER-fx<sup>®</sup> and CELL-fx<sup>®</sup> in Canada and strive to continue to build sales and profits through effective brand management, targeted sales and marketing efforts, public relations activities, focusing on operational excellence in cost management, maintaining its supply chain management to meet growing demand and increasing awareness and sales of its products.

The Company is also realigning its manufacturing priorities with the objective of converting existing inventory into receivables and cash as soon as possible. This plan includes shipping excess U.S. inventory to Canada for repackaging and sale. The Company continues to reduce its operating expenses while actively seeking a strategic business partner in the U.S. to assist in marketing and distribution. The Company plans to contain and lower costs in sales and marketing, distribution, operations and quality control activities for the remainder of 2007.

Management will monitor its cash flow through the summer and develop contingency plans for financing of the Company's inventories and new building.

Management plans to improve consumer awareness and education of healthcare professionals to develop its business and to focus on a strategy of educating consumers and building awareness of the year-round preventative use of COLD-fx<sup>®</sup>. Management will continue to execute its plans to achieve its growth objectives for the U.S. with COLD-fx<sup>®</sup>. Management believes the future for COLD-fx<sup>®</sup> is very promising.

The Company will continue to explore carefully the option of an FDA application for the active ingredient of COLD-fx<sup>®</sup> as an OTC drug for the prevention of cold and flu, which would allow the Company to make strong and specific medical claims and afford label exclusivity in the U.S. This approach would require the successful completion of a Phase III clinical trial, which would enhance product differentiation from the U.S. competition.

Management is committed to making the Company's products strong performers within their categories. The Company will continue to prove its leadership in the discovery and commercialization of science-based natural therapeutics for health maintenance and disease prevention, and to become a well-

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recognized and respected supplier to consumers and the natural health products industry while providing a return on investment to shareholders.

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## Internal Controls over Financial Reporting

The Enterprise Risk Management Committee (a subcommittee of the Audit Committee) oversees risk assessment and review processes of the Company's internal controls over financial reporting to meet the requirements under MI 52-109. The Committee provides regular updates to the Audit Committee and Board. At the end of fiscal year 2006, the design and documentation of internal controls over financial reporting were completed, with the exception of the design and documentation of entity level controls (control environment) which was completed in February 2007. Certain non-material control gaps and remediation of those deficiencies are expected to carry through the 2007 fiscal year. The Company is in a period of rapid growth and will continue, as required, to modify the design, and implement controls over financial reporting during 2007.

In March 2007, the Company initiated a review of its revenue recognition policy and practices following awareness of the potential for significant product returns from U.S. customers. The potential for U.S. returns was significantly greater than estimated that the Company had made for the initial shipments. In this evaluation, management concluded the following material weaknesses existed in its internal controls over financial reporting:

- Instances of non-compliance with policies and procedures related to reviewing and communicating material arrangements entered into on behalf of the Company in a timely manner, including the identification and analysis of sales arrangements containing a right of return, adequate records of customer and vendor files, and documentation of the application of GAAP to such transactions;
- Non-compliance with policies and procedures related to processing and shipping of sales orders to new customers, including shipments without internal release of the sales order, confirmation of customer sales arrangements, credit review, and sufficient customer documentation; and
- Failure to appropriately apply GAAP to the initial recording of product sales when entering into a new market where a reasonable estimate for product returns was not possible; and insufficient internal cross-functional and external communication and coordination, including compliance with internal control processes, management override, and insufficient segregation of duties and training in certain areas, all of which affected the appropriate application of the revenue recognition policy.

These control deficiencies resulted in the restatement of the Company's consolidated financial statements for the year ended September 30, 2006 and interim financial statements for the three month period ended December 31, 2006 and materially affected revenue, cost of goods sold, income taxes, accounts receivable, inventory, liabilities, net earnings and retained earnings.

As part of the measures to correct the above weaknesses in internal controls over financial reporting, the Company has improved its contract review process and communicated the revised process within the Company. The Company has created a team, comprised of representatives from operations, finance and, if required, external legal counsel to analyze, review and document customer and vendor arrangements for their effects on the business, financial reporting and disclosures.

Intensive efforts will be initiated to expedite employee training and to complete the implementation of designed controls and procedures, with priority in the sales and purchasing cycles.

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These efforts include the restructuring of management, including the hiring of Ross Montagano as Chief Operating Officer, the splitting of the sales and marketing responsibilities between two executive roles, and improving the environment of accountability, workloads, training, communication, and information flow between functional areas. Management and the Audit Committee also review performance and variance reporting to improve risk management, monitoring and accountability.

In certifying the previous financial statements for fiscal year ended September 30, 2006 and the three month period ended December 31, 2006, the Chief Executive Officer (CEO) and Chief Financial Officer (CFO) acknowledged responsibility for establishing and maintaining the Company's disclosure controls and procedures, and had evaluated, tested, and certified their design and effectiveness, according to MI 52-109, based on the information available at the time.

In that evaluation of disclosure controls, the following deficiencies were identified:

- Education of employees, and
- Control of website updates were non-current and obsolete information was not removed and information was not reviewed for material content.

Although employees have read the Disclosure and Insider Trading Policies, Core Values and Code of Conduct, and Employee and Business Protection Guide, the Company believes that educational sessions for new employees will provide additional assurance that there will be compliance with these policies. This educational process has commenced. A committee was formed and is comprised of representatives of Investor Relations, Communications, Scientific and Regulatory Affairs, Human Resources and Financial departments with the purpose to review, on a regular basis, website updates to mitigate risks of errors or omissions.

Awareness of significant returns subsequent to the original certification of disclosure controls caused the CEO and CFO to reconsider their conclusions on the effectiveness of disclosure controls and procedures. The Chief Executive Officer and Chief Financial Officer proceeded to retest and re-evaluate the disclosure controls and procedures to determine if their conclusions were correct.

In re-evaluating disclosure controls, the following deficiency was identified:

- Non-compliance with policies and procedures in the sub-certification process of the filing of the Company's disclosures, in that material information on the conditions of business contracts and arrangements were not communicated in a timely manner

This deficiency contributed to a weakness in the Company's disclosure controls and procedures, which has now been corrected. Management believes a lack of understanding of the need to properly communicate material agreements appeared to have resulted in incomplete information being provided on the risk of product returns and consumer acceptance, and on sales and vendor agreements, which contributed to the accounting errors in revenue recognition. As discussed under Internal Controls over Financial Reporting, a review process was established to evaluate business arrangements and it is believed that this issue is resolved. Management is committed to implementing the improvements to the disclosure processes and controls. Management will foster a culture of open communication and

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accountability in compliance with policies and procedures on a proactive basis. The Disclosure Committee has emphasized to Executive Management the importance of the communication of material information and changes in control systems in a timely manner to the CEO and CFO.

The CEO and CFO have concluded that the Company's disclosure controls and procedures do provide management with a reasonable level of assurance that the information required to disclose continuously in its annual and interim filings and other reports, is recorded, processed, summarized and reported or disclosed on a timely basis. This process continues to be frequently reviewed and refined. The Board of Directors and management are concerned with the above control deficiencies, take these matters very seriously and are determined to ensure correction of these deficiencies that contributed to the need for restatement of the financial statements.

The Enterprise Risk Management Committee and Management continue to monitor the progress and improvements in the design, efficiency and implementation of controls over financial reporting and disclosures, with particular attention to the above internal control deficiencies and weakness. Notwithstanding the foregoing, no assurance can be made that the Company's disclosure controls and procedures will detect or prevent all failures of people within the Company to disclose material information otherwise required to be set forth in the Company's reports.

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## Risks and Uncertainties

The Company is in the growth stage with its lead natural health products, COLD-fx<sup>®</sup>, REMEMBER-fx<sup>®</sup> and CELL-fx<sup>®</sup>. In order to gain a successful market share, the Company will be required to incur expenditures for marketing, advertising and public awareness programs. Future success is dependent on these activities, together with the effectiveness and safety of the Company's products, regulatory review and approval for its products, the degree of patent protection afforded to particular products and seasonality of demand for its products. The Company has Quality Control and Quality Assurance programs to monitor product quality. The Company also maintains product liability insurance; however, it is possible that this coverage will not provide full protection against all risks.

The Company currently has operations in North America and Europe. The Company is economically dependent, to varying extents, on certain customers and vendors in each of these regions. Political and regulatory environments, economic conditions and other factors may affect revenues and operations. However, these risks may be mitigated by geographic diversification of sales and supply. Entry into new markets will subject the Company to additional risk as supply chains and customer relationships are developed, and consumer acceptance is sought. Risks include, but are not limited to, initial product sales to fill pipeline, replenishment rates, consumer purchases, product returns, inventory levels, and consumer preferences and adoption rates. In entering new markets, retailers may rebalance inventories and request to return stock depending on consumer demand and sell-through rates. There can be no assurance that the Company will be able to cost-effectively operate, generate revenues, generate adequate funds or maintain relationships with such customers, vendors, employees, collaborators and other third parties. The Company mitigates these risks with monitoring of activities, developing and implementing action plans and diversification of vendors and customers to mitigate risk areas.

Expectations about the Company's financial and scientific results could have a significant effect on the trading price of the Company's shares. Certain risks exist in the timing of scientific and regulatory reviews, filings and approvals, and the Company's ability to commercialize products in its pipeline. In this three month period ended, four (2006 – four) major customers accounted for \$4.7 million or 56.9% (2006 - \$7.5 million or 68.6%) of net product sales.

Prospects for the Company's new technologies and products are uncertain and should be regarded as highly speculative. It is not possible to predict the results of studies or regulatory approvals. If products are approved for sale, there can be no assurance that they will result in significant sales.

Except for historical information, certain matters discussed in this report are by their nature forward-looking statements that involve risks and uncertainties, which may cause actual results to differ materially from the statements made.

### Financial risks and risk management

The risks and uncertainties described below are those that the Company currently believes may materially affect its operations. This is not an exhaustive list and can change as the Company develops. Additional risks and uncertainties that the Company is unaware of or currently deems immaterial may become important factors that may materially affect the business. A more comprehensive discussion is available in the Company's Annual Information Form available on SEDAR.

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## Liquidity risk

Liquidity risk is the risk arising from the inability to meet obligations when they come due in a timely manner. The Company's liquidity strategy is to maintain the capacity to fund assets and repay liabilities in a timely and cost-effective manner under adverse market conditions. This capacity primarily arises from the Company's earnings, issuance ability in the debt and equity markets as well as its ability to generate liquidity from its balance sheet

The Company's strategy is to diversify its sources of funding and allocate its funding activities in accordance with market conditions, relative costs, and other factors. The Company believes that debt and securitization funding, combined with operating and investing activities, will provide sufficient liquidity to meet future funding requirements.

As the Company's operations are seasonal in nature, sales and incoming cash flows are lowest in the third quarter. Customers have exercised the right of return on significant product shipments resulting in the requirement to refund certain existing customer deposits. The Company's short-term cash requirements may exceed cash balances for the last six months of the fiscal year ending September 30, 2007. The availability of cash is dependent upon the earnings, availability of existing or alternate financing facilities, and the timing and extent of product returns and repayment terms. The outcome of these events are difficult to predicted.

## Inventory valuation, obsolescence and spoilage risk

The Company's inventories have a finite shelf life (up to five years). Raw materials, work in process and finished goods have expiry dates and are subject to competitive pricing, obsolescence and spoilage. All inventory items are reviewed with the sales and operations groups for obsolescence including products that are discontinued or may not be saleable, or materials that are no longer used in production. These revaluations and allowances are charged to the cost of goods sold as identified or required.

## Foreign exchange risk

The Company is exposed to market risk related to operations in foreign countries, and transactions and changes in foreign currencies. These changes could adversely affect the value of the Company's monetary assets and liabilities, as well as impact revenues and earnings. In Canada, the Company's expenditures on goods and services and revenues are primarily in Canadian dollars. In the United States, the Company's expenditures on goods and services and revenues are primarily in U.S. dollars. In Switzerland, the Company's expenditures on goods and services and revenues are primarily in U.S. dollars and to lesser degree Swiss francs.

As of March 31, 2007, the Company has not entered into any forward currency contracts (forwards, futures or options) or other financial derivatives to hedge foreign exchange risk, and therefore is subject to foreign currency transaction and translation gains and losses.

## Credit risk

Credit risk arises from the possibility that the entities to which the Company sells products may experience financial difficulty and be unable to fulfill their contractual obligations. This risk is mitigated

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by credit management practices that include monitoring of the debtor's payment history and performance. The customer base is comprised of well established, reliable retailers and wholesalers.

## Interest rate risk

The Company is exposed to interest rate fluctuations. The Company's investment strategy of cash surpluses is protection of principal as such investments are made on high quality short-term deposits at Schedule "A" banks in the form of term deposits and bankers acceptances. With respect to borrowings, the Company would be exposed to Canadian dollar prime rate fluctuations. The Company currently does not utilize hedging instruments to manage interest rate risk.

## Regulatory environment

The Company is subject to extensive laws and regulations in respect of securities, commercial activities, taxation, product quality, processing, labeling, and testing of its products. Changes to these laws and regulations could have a significant impact and can vary by country. There can be no assurance that the Company will be able to comply cost-effectively with future laws and regulations. The Company complies with the guidelines set by regulatory agencies and "Good Manufacturing Practices". The Company also has established and reviews policies and procedures to mitigate risk of non-compliance.

## Market risk

In order to gain successful market share, the Company may be required to increase investments in marketing, advertising and public awareness programs. Future success depends on these activities, together with the effectiveness and safety of the Company's products, regulatory review and approval of its products, the degree of patent protection afforded to particular products and seasonality of demand for its products.

Consumer acceptance of the Company's products will depend upon a number of factors, including demonstration of clinical efficacy and safety; scientific and marketing advantages of its products over competitors' offerings; availability of acceptable pricing and adequate third-party reimbursement; and effectiveness of marketing and distribution methods for the products.

The Company may not have all the required clinical data and results to market its product pipeline in any jurisdiction. Current and future clinical or preclinical results may be negative, inconclusive or insufficient to allow the Company to market any of its product candidates. Obtaining data and results may also take longer than planned, or may not be obtained at all.

## Critical Accounting Policies and Estimates

Critical accounting policies and estimates are those policies, assumptions and estimates most important in the preparation of the Company's consolidated financial statements. Selection of policies requires Management's subjective and complex judgment from many alternatives and estimates involving matters that are inherently uncertain. Management believes that those policies, assumptions and estimates are reasonable, based on the information available. Those policies, assumptions and estimates affect the reported amounts of assets and liabilities at the date of the financial statements and revenues and expenses during the period represented.

The preparation of the Company's financial statements requires estimates and judgments that affect the reported amounts of assets, liabilities, equity, and revenues and expenses, and related disclosure of contingencies. Management evaluates the assumptions and estimates, including those related to product sales, bad debts, inventories, deferred costs, investments, intangible assets, accrued liabilities and legal issues. Management bases its estimates on historical experience and on various other assumptions believed to be reasonable under the circumstances. The results of those estimates form the basis for making judgments about the carrying values of assets and liabilities that are not readily apparent from other sources. The actual results might differ materially from these estimates under different assumptions or conditions. The methodologies used and assumptions selected by management in making these estimates, as well as the related disclosures, have been reviewed by and discussed with the Audit Committee of the Board of Directors. Management believes the following critical accounting policies affect the more significant judgments and estimates used in the preparation of the consolidated financial statements.

Critical accounting policies and estimates relate to the following:

- Revenue recognition;
- Useful lives and impairment of intangible assets and deferred development costs;
- Contingencies;
- Income taxes;
- Inventory valuation;
- Stock-based compensation; and
- Capitalized interest.

Because of the identified correction in application of the revenue recognition policy, the Company has updated its revenue recognition policy in conjunction with the restatements of fiscal year ended September 30, 2006 and the three month period ended December 31, 2006.

### Revenue recognition

The Company recognizes revenue in accordance with the CICA handbook Section 3400 Revenue and Emerging Issues Committee (EIC) Abstract 141 Revenue Recognition. EIC-141 states that revenue recognition should take place when realized or realizable and earned. Revenue recognition occurs upon meeting all of the following criteria:

- Evidence of an arrangement exists;
- Upon delivery of the product or rendering of services;
- The seller's price to the buyer is fixed and determinable; and
- Collection is reasonably assured.

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EIC-141 also states that revenue recognition occurs at the time of the sales transactions where the buyer has the right to return the product only if:

- (1) The seller's price to the buyer is substantially fixed or determinable at the date of sale;
- (2) The buyer has paid the seller, or the buyer is obligated to pay the seller and the obligation is not contingent on resale of the product;
- (3) The buyer's obligation to the seller would not be changed in the event of physical destruction, loss or damage of the product;
- (4) The buyer acquiring the product for resale has economic substance apart from that provided by the seller;
- (5) The seller does not have significant obligations for future performance to directly bring about resale of the product by the buyer; and
- (6) The amount of future returns can be reasonably estimated.

The Company recognizes revenues for product sales when the title and risk of ownership transfers to the customer, and the criteria of EIC-141 are satisfied, which is generally at the time of delivery of products to customers. Product sales represent total gross revenues less allowances for customer credits, including estimates of discounts and allowances, rebates, charge-backs, and product returns.

The Company establishes allowances for estimated rebates, charge-backs and product returns based on numerous qualitative and quantitative factors, which include:

- The number of and specific terms of arrangements with customers;
- Estimated levels of inventory in the distribution channel;
- Historical rebates, coupon redemption rates, charge-backs and returns of products;
- Direct communication with customers;
- Anticipated introduction of competitive products;
- Anticipated pricing strategy changes by the Company and/or its competitors;
- Analysis of sales data gathered by a third-party data provider;
- The effect of regulatory changes; and
- The estimated remaining shelf life of products.

The Company uses internal forecasts, historical sales data, information gathered from customers and external data providers and judgment, to determine the estimated amount of product sold to customers, product in the sales channel or customer inventories, and to assess risk of returns. This forecast is based on input from members of the sales, marketing and operations groups. The adjusted forecasts take into account numerous factors including, but not limited to, new product introductions, promotional programs, direct communication with customers and potential product expiry issues. Consistent with industry practice, we periodically offer promotional discounts or allowances to the existing customer base. Where product is sold into new markets, the Company recognizes revenue when the risk of return is substantially eliminated which is based on estimates of sell-through to the end consumer.

Customer discounts and allowances are typically a percentage of the current published list price or may be a fixed amount, and treated as off-invoice allowances. Accordingly, discounts reduce revenue in the period of offering the program. Shipments resulting from these programs generally are not in excess of ordinary levels, therefore, the Company recognizes the related revenue upon delivery and include the shipments in estimating various product related allowances. In the event the Company determines these shipments represent purchases of inventory in excess of ordinary levels for a given wholesaler, an

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evaluation of the potential effect of exposure of product returns and a reduction in revenue (and increase to inventory) occurs. Discounts and allowances vary by customer, marketing program and time of the year. Discounts in excess of recognized revenue are charged to advertising and marketing expense following a customer specific analysis.

Recognition of licensing revenues, which are comprised of initial up-front fees and milestone payments from licensing arrangements, is in accordance with EIC-141, Revenue Recognition and EIC-142, Revenue Arrangements with Multiple Deliverables. Recognition of fees at the inception of the agreement for prior research and technology rights occur when the Company has no further involvement or obligation to perform under the arrangement. Initial up-front and milestone payments, that require the Company's continuing involvement, are deferred and amortized into statement of earnings over the estimated period of the Company's participation. The Company's commitment varies by each arrangement based on the ratio of costs expended to total estimated costs required to complete the Company's obligations. Recognition of revenue from performance milestone payments occurs upon achievement of the milestones as specified in the arrangement, provided payment is proportionate to the effort expended as measured by the portion of costs expended to total estimated development costs. Review of the estimates of the period and development costs take place on a regular basis.

## Intangible assets and deferred development costs

Intangible assets are presented at cost less accumulated amortization, generally computed using the straight-line method based on estimated useful lives ranging from five to twenty years. The Company amortizes intangible assets on a systematic basis to reflect the pattern in which the economic benefits of the asset are consumed, if that basis can be reliably determined. The expected useful life is the period over which the intangible asset contributes directly or indirectly to future cash flows. Management determines the useful lives of intangible assets based on a number of factors, which include legal, regulatory or contractual limitations; known technological advances; anticipated demand; and the presence of competition. A significant change in these factors may require a revision of the expected remaining useful life of an intangible asset, which could have a material effect on results of operations.

Deferred research and development costs consist of direct and indirect expenditures related to the Company's research and development programs. Expensing of research and development costs takes place in the current period unless they meet generally accepted accounting criteria for deferral and amortization. The Company assesses whether these costs have met the relevant criteria for deferral and amortization at each reporting date. Development costs related to Parathyroid Hypertensive Factor have been deferred and are being amortized over a period of five years. Deferred development costs are subject to the same impairment testing as intangibles.

Typically, the original carrying value of intangible assets and deferred costs is cost less amortization. The recording of those intangible assets acquired through asset acquisitions or business combinations is at fair value based on an allocation of the purchase price.

The Company evaluates intangible assets annually for impairment, or more frequently if events or changes in circumstances indicate that the carrying amounts of these assets may not be recoverable. Impairment testing is an assessment of fair value based on potential indicators of impairment, such as obsolescence, plans to discontinue use or restructure, and poor financial performance compared with

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original plans. Impairment exists when the carrying amount of an asset is not recoverable and its carrying amount exceeds its estimated fair value.

For intangible assets, impairment testing uses an income approach. This approach involves a forecast of the estimated future cash flows, adjusted to present value by applying an appropriate discount rate that reflects the risk factors associated with the cash flow streams. Some of the more significant estimates and assumptions inherent in the income approach include the amount and timing of the future cash flows, and the discount rate used to reflect the risks inherent in the future cash flows. A change in any of these estimates and assumptions could produce a different fair value, which could have a material impact on results of operations. In cases of impairment, management will re-evaluate the remaining useful life of the intangible asset and modify it, as appropriate. This evaluation may include an immediate adjustment to the carrying value and materially affect the results of operations.

## Accrued liabilities

The Company engages a significant number of third party service providers, contract manufacturing and logistic organizations. The basis of accruals is estimated expenses and/or inventory production. Where possible, detective controls, such as confirmations, are used to verify significant accruals. For example, the Company requests and verifies the accruals with statements from known, significant vendors and reconciles invoices received subsequent to the period end against those accruals. This accrual depends on the issuance and accuracy of estimates in purchase orders and contracts, and the accuracy of estimates on the percentage of completion and costs incurred to the end of the reporting period.

## Contingencies

In the normal course of business, the Company may be subject to loss contingencies, such as claims and assessments arising from litigation and other legal proceedings, contractual commitments and indemnities, product liabilities, and tax matters. The Company is required to accrue for such loss contingencies or expense if it is probable that the outcome will be unfavourable or take place, and if there is a reasonable estimate of the amount of the loss or expense. Evaluation of the Company's exposure to a loss takes into consideration various factors, including the progress of each contingency, experience with similar contingencies, and consultation with specialists and external legal counsel. The Company re-evaluates contingencies as additional information becomes available. Given the uncertainties inherent in complex litigation, regulatory processes and other contingencies, these evaluations can involve significant judgment about future events. The ultimate outcome of any litigation or other contingency may be material to the results of operations, financial position and cash flows.

## Income taxes

The Company has operations in various countries that have differing tax laws and rates. Income tax reporting is subject to audit by both domestic and foreign tax authorities.

The provision for income taxes involves a number of estimates and assumptions made by management. The amount of income earned in the various operating jurisdictions and the rate of taxes payable in respect of that income has an effect on the Company's consolidated income tax rate. The Company also enters into many transactions and arrangements in the ordinary course of business in which the tax treatment is not entirely certain and involves many taxation jurisdictions. As a result, management must

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make estimates and judgments based on knowledge and understanding of domestic and international tax rules in determining the consolidated tax provision. For example, certain countries in which the Company operates could seek to tax a greater share of income than has been provided for by the Company. The outcome of any audits by taxation authorities may differ from the estimates and assumptions used in determining our consolidated income tax provisions and accruals. These assessments could have a material effect on the Company's consolidated income tax provision and results of operations, financial position and cash flows for the period in which the tax authorities make such a determination. The Company may make a valuation allowance on deferred tax assets primarily relating to operating losses, future tax depreciation and tax credit carry forwards. Management assumes that these deferred tax assets are more likely than not, to remain unrealized. Management must exercise significant judgment to determine the appropriate amount of valuation allowance to record. Changes in the valuation allowance could materially increase or decrease the provision for income taxes in a period and affect the results of operations.

## Inventory valuation

Inventories of finished goods and product shipped with right-of return are presented at the lower of cost or net realizable value. The cost of inventory includes direct materials and labour costs, on a weighted average basis for the production lot. The net realizable value of inventory is determined by the estimated selling price of the products in the normal course of business less the cost of the inventory and estimated costs necessary to complete a sale. Determination of net realizable value is also based on, but not limited to, internal forecasts, historical sales data, input from members of the sales, marketing and operations groups, expiry dates and planned promotional programs. If the costs exceeds estimated net realizable value, the Company records allowances and continues to assess these allowances on a quarterly basis. All inventory items are also reviewed with members of the operations group for obsolescence including products that are no longer sold or saleable, or materials that are no longer used in production. These products and materials are expensed as identified or required.

The Company utilizes information gathered from customers and external data providers, sales estimates and judgment to determine the volume of product shipped with right-of-return. This product is within the customer's possession but is included in the Company's inventory as the related revenue has not been recognized and the customer has the ability to return the product. Management estimates that display and packaging materials will not be recoverable in the event of a return and expenses these materials when the product is shipped.

## Stock-based compensation

The Company has adopted the fair value-based method for recognizing stock-based compensation. The Company uses the Black-Scholes option-pricing model to calculate stock option values, which requires certain assumptions related to the expected life of the option, forfeiture rate, future stock-price volatility, risk-free interest rate, and dividend yield. The expected life of an option is based on the maximum eight years vesting period of the stock option plan. The basis of future stock-price volatility is historical volatility of the Company's common shares over the expected life of the option. The basis of the risk-free interest rate is the zero-coupon Canadian government bond rate with a term equal to the expected life of the option. The basis of the dividend yield is on the option's exercise price and expected annual dividend rate at the time of grant. The Company has not paid dividends in the past three years, nor has any plans to pay dividends. Changes to any of these estimates or assumptions, or the use of a different option-pricing

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model could produce a different fair value for stock-based compensation expense, which could have a material effect on the results of operations.

## Capitalized interest

The Company has modified its capitalization policy to include interest incurred on the construction of the related asset. Interest costs were capitalized on the land lease in fiscal year 2006.

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## Recent Accounting Pronouncements

### Financial instruments

On October 1, 2006, the Company adopted the following Canadian Institute of Chartered Accountants (CICA) accounting recommendations for the recognition, presentation and disclosure of financial instruments:

- CICA Handbook Section 3855 "Financial Instruments – Recognition and Measurement"
- CICA Handbook Section 3862 "Financial Instruments – Disclosures"
- CICA Handbook Section 3863 "Financial Instruments – Presentation"
- CICA Handbook Section 1530 "Comprehensive Income"
- CICA Handbook Section 3251 "Equity"

Under the new standards, all financial assets on acquisition must be classified as held-to-maturity, loans and receivables, held-for-trading or available-for-sale, and all financial liabilities at inception, must be classified as held-for-trading or other. All financial instruments are initially recorded on the balance sheet at fair value and if classified as loans and receivables, or held for trading, changes in fair value are included in earnings. For those instruments classified as available-for-sale and for derivative financial instruments designated as hedges, changes in fair value will be included in other comprehensive income. Other comprehensive income and its components are presented in a separate financial statement that is displayed with the same prominence as other financial statements.

## Non-GAAP Financial Measures and Reconciliations

Generally, a non-generally accepted accounting principles (non-GAAP) financial measure is a numerical measure of a company's performance, financial position or cash flows that either excludes or includes amounts, not normally excluded or included in the most directly comparable measure calculated and presented in accordance with GAAP. EBITDA and cash flow prior to working capital changes are not measures of financial performance (nor do they have standardized meanings) under Canadian GAAP. In evaluating these measures, investors should consider that the methodology applied in calculating such measures may differ among companies and analysts.

The Company uses both GAAP and certain non-GAAP measures to assess performance. Management believes these non-GAAP measures provide useful supplemental information to investors in order that they may evaluate CV Technologies Inc.'s financial performance using the same measures as management. The Company's management believes that, as a result, information provided to the investor is more transparent in assessing the financial performance of the Company. Investors should not consider these non-GAAP financial measures as a substitute or superior to the measures of financial performance prepared in accordance with GAAP.

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## EBITDA

The definition of EBITDA is earnings before interest, income taxes, depreciation and amortization. The Company uses EBITDA as a supplemental financial measure of its operational performance. Management believes EBITDA to be an important measure as it excludes the effects of items, which primarily reflect the impact of long-term investment decisions, rather than the performance of the Company's day-to-day operations. As compared to net earnings according to GAAP, this measure is limited in that it does not reflect the periodic costs of certain capitalized tangible and intangible assets used in generating revenues in the Company's business. Management evaluates such items through other financial measures such as capital expenditures and cash flow provided by operating activities. The Company believes that this measurement is useful to assess a company's ability to service debt and to meet other payment obligations or as a valuation measurement.

The following is a reconciliation of EBITDA to net earnings, the most directly comparable financial measure calculated and presented in accordance with Canadian GAAP.

<b>EBITDA</b> (in thousands)	Quarter 2 Mar 31, 2007	Quarter 2 Mar 31, 2006	Year to Date Mar 31, 2007	Year to Date Mar 31, 2006	Fiscal Year Sep 30, 2006 Restated
Net earnings (loss)	(3,296)	987	(6,880)	5,403	639
Current income taxes	(56)	1,090	4,775	2,998	3,301
Future income taxes	1,229	10	(759)	1,149	200
Amortization of deferred costs	90	90	181	181	362
Amortization of patents, registered trademarks, property, plant and equipment	97	65	206	129	312
Interest expense	37	8	55	15	61
Interest revenue	(131)	(132)	(214)	(180)	(411)
EBITDA	(2,030)	2,118	(2,636)	9,695	4,464

## Working capital

The definition of Working Capital is current assets less current liabilities. The Company uses working capital as a supplemental financial measure of its liquidity and operational performance.

<b>Working Capital</b> (in thousands)	Year to Date Mar 31, 2007	Year to Date Mar 31, 2006	Fiscal Year Sep 30, 2006 Restated	Fiscal Year Sep 30, 2005
Current assets	38,052	31,231	35,247	20,734
Current liabilities	30,398	7,236	18,862	3,806
Working capital	7,654	23,995	16,385	16,928

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## Cash flow

Below is a reconciliation of "cash flow prior to working capital changes" to cash provided by operating activities, the most directly comparable financial measure calculated and presented in accordance with Canadian GAAP.

The Company uses cash flow prior to working capital changes as a supplemental financial measure in its evaluation of liquidity. Management believes that adjusting principally for the swings in non-cash working capital items due to seasonality assists management in making long-term liquidity assessments. The Company also believes that this measurement is useful as a liquidity or valuation measurement.

<b>Cash Flow Prior Working Capital Changes</b> (in thousands)	<b>Quarter 2</b> <b>Mar 31, 2007</b>	<b>Quarter 2</b> <b>Mar 31, 2006</b>	<b>Year to Date</b> <b>Mar 31, 2007</b>	<b>Fiscal Year</b> <b>Sep 30, 2006</b>
<b>Cash flow prior to working capital changes</b>	<b>(1,253)</b>	<b>2,091</b>	<b>(6,009)</b>	<b>4,226</b>
Accounts receivable	2,714	2,613	2,593	(414)
Inventory	450	(1,081)	(1,794)	(10,789)
Prepaid expenses	(109)	504	404	(1,149)
Prepaid intra-group tax asset	52		104	(2,644)
Accounts payable and accruals	(6,592)	(1,235)	(698)	7,822
Income taxes payable	(1,501)	1,086	(3,164)	5,234
Customer deposits	(73)		15,643	1,774
Deferred revenue		20	30	120
<b>Changes in non-cash working capital</b>	<b>(5,059)</b>	<b>1,907</b>	<b>13,118</b>	<b>(46)</b>
<b>Cash provided by operating activities</b>	<b>(6,312)</b>	<b>3,998</b>	<b>7,109</b>	<b>4,180</b>

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## Glossary

Term	Definition
ASC	Alberta Securities Commission
BCSC	British Columbia Securities Commission
CBP	See ChemBioPrint
ChemBioPrint	A discovery and standardization platform used by the Company's scientists to identify the chemical profile and biological activity of natural products
CICA	Canadian Institute of Chartered Accountants
Company	CV Technologies Inc. which is the reporting issuer
CTO	Cease Trade Order
CVT-E002	Active ingredient in COLD-fx <sup>®</sup>
CVQ	Trading symbol for CV Technologies Inc. which is the reporting issuer
DIN	Drug Identification Number
FDA	U.S. Food and Drug Administration; the U.S. government body responsible for food (Dietary Supplements) drugs, medical devices, biologics, animal feed and drugs, cosmetics, radiation-emitting products, and combination products. CDER, the Center for Drug Evaluation and Research, is the division of the FDA responsible for drug approvals and the clinical trials on drugs. CFSAN, Center for Food Safety and Applied Nutrition, is the division of the FDA responsible for dietary supplements.
HT1001	Active ingredient in REMEMBER-fx <sup>®</sup>
HUMC	Hackensack University Medical Centre, New Jersey
ICTO	Interim Cease Trade Order
MD&A	Management's Discussion and Analysis
NHPD	Natural Health Products Directorate
NIH	National Institutes of Health: The National Institutes of Health (NIH), a part of the U.S. Department of Health and Human Services, is the primary Federal agency for conducting and supporting medical research.

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NK	Natural Killer (cells)
NPN	Natural Product Number
OSC	Ontario Securities Commission
OTC	OTC drug/product: Over-The-Counter drug; a drug approved for sale by the FDA or Health Canada that does not require a Doctor's prescription to be purchased. It is available for self-care.
Phase I	Phase I of Clinical Development (as defined by the U.S. FDA for use in drug development): Phase I starts with the initial administration of an investigational new drug into humans. Studies in this phase of development usually have nontherapeutic objectives (no efficacy endpoints for the trial) and may be conducted in healthy volunteer subjects. Studies conducted in Phase I typically involve one or a combination of the following aspects: (a) safety and tolerability (b) pharmacokinetics including absorption, distribution, metabolism and excretion (c) early measurement of efficacy if performed in patients.
Phase II	Phase II of Clinical Development (as defined by the U.S. FDA for use in drug development): A therapeutic exploratory phase where efficacy in disease populations is determined. Phase II is usually considered to start with the initiation of studies in which the primary objective is to explore therapeutic efficacy in patients. An important goal for this phase is to determine the dose and regimen for Phase III trials. Additional objectives of clinical trials conducted in Phase II may include evaluation of potential study endpoints, therapeutic regimens (including concomitant medications), and target populations for further study in Phase II or III.
Phase III	Phase III of Clinical Development (as defined by the U.S. FDA for use in drug development): Studies in Phase III are designed to confirm the preliminary evidence accumulated in Phase II that a drug is safe and effective for use in the intended indication and recipient population. These studies are intended to provide an adequate basis for marketing approval in the U.S. for a drug. Studies in Phase III may also further explore the dose-response relationship, or explore the drug's use in wider populations, in different stages of disease, or in combination with another drug.
QA	Quality assurance: All the planned and systematic activities applied within the quality system to provide adequate confidence that the predetermined standards for quality and safety will be met.
QC	Quality control: The testing of the product to ensure it meets the standards established by quality assurance.
Sales	Product sales and revenues include reductions for sales discounts and allowances

# CV Technologies Inc.

Quarterly Report for the Three and Six Month Periods Ended

March 31, 2007

SEDAR	System for Electronic Data Access and Retrieval ( <a href="http://www.sedar.com">www.sedar.com</a> )
PHF	Parathyroid Hypertensive Factor
POS	Point of Sale refers to the retail sale of product to consumers or end user.
RSV	Respiratory Syncytial Virus