KITS EYECARE LTD.
Condensed Interim Consolidated Financial Statements
For the Three Months ended March 31, 2023 and March 31, 2022
(in thousands of Canadian Dollars, except share and per share data)
(Unaudited)

KITS EYECARE LTD.
CONDENSED INTERIM CONSOLIDATED STATEMENTS OF LOSS
(in thousands of Canadian Dollars, except share and per share data)
(Unaudited)

	Three months ended March 31,	
	2023	**2022**
Revenue (Note 3)	$ 27,667	$ 20,052
Cost of sales	18,540	13,939
Gross profit	9,127	6,113
Fulfillment	3,465	2,770
Marketing	3,998	2,694
General and administrative	1,935	2,183
Exchange (gain)/loss	39	485
Depreciation and amortization	603	555
Operating income (loss)	(913)	(2,574)
Finance costs - net	381	404
Income (Loss) before income taxes	$ (1,294)	$ (2,978)
Income taxes (Note 11)	(274)	(714)
Net income (loss) for the period	$ (1,020)	$ (2,264)
Income (Loss) per share (Note 12)		
Basic	$ (0.03)	$ (0.07)
Diluted	$ (0.03)	$ (0.07)

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

KITS EYECARE LTD.
CONDENSED INTERIM CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS
(in thousands of Canadian Dollars, except share and per share data)
(Unaudited)

	Three months ended March 31,	
	2023	**2022**
Net income (loss) for the period	$ (1,020)	$ (2,264)
Other comprehensive income for the period:		
Items that may be reclassified to profit or loss		
Currency translation differences	(38)	(474)
Total comprehensive income (loss) for the period	$ (1,058)	$ (2,738)

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

KITS EYECARE LTD.
CONDENSED INTERIM CONSOLIDATED STATEMENTS OF FINANCIAL POSITION
(in thousands of Canadian Dollars, except share and per share data)
(Unaudited)

	March 31, 2023	December 31, 2022 Audited
Assets		
Current assets		
Cash and cash equivalents	$ 19,574	$ 18,790
Accounts and other receivables	712	897
Inventory (Note 6)	14,483	16,414
Tax receivable	9	20
Prepaids, deposits and other assets	609	877
Total current assets	35,387	36,998
Property and equipment	2,612	2,828
Right-of-use asset (Note 7)	7,001	7,209
Deferred tax asset (Note 11)	5,378	5,122
Intangible assets (Note 13)	2,493	2,939
Goodwill (Note 13)	38,738	38,769
Total assets	$ 91,609	$ 93,865
Liabilities and shareholders' equity		
Current liabilities		
Accounts payable and accrued liabilities	$ 15,952	$ 16,809
Tax payable	422	422
Deferred revenue (Note 3)	3,737	3,487
Loan (Note 4(a))	3,085	3,099
Lease liability (Note 7)	639	623
Total current liabilities	23,835	24,440
Loan (Note 4(a))	7,390	8,158
Promissory note (Note 4(b))	1,920	1,884
Lease liability (Note 7)	5,505	5,674
Total liabilities	38,650	40,156
Shareholders' equity		
Share capital (Note 8)	77,116	76,985
Contributed surplus (Note 9)	3,040	2,863
Retained deficit	(26,719)	(25,699)
Accumulated other comprehensive loss	(478)	(440)
Total shareholders' equity	52,959	53,709
Total liabilities and shareholders' equity	$ 91,609	$ 93,865

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

Contingencies – Note 14

KITS EYECARE LTD.

CONDENSED INTERIM CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

(in thousands of Canadian Dollars, except share and per share data)

(Unaudited)

	Share Capital		Contributed surplus	Retained earnings (deficit)	Accumulated other comprehensive	Total
	Common shares					
	Shares	Amount				
Balance at December 31, 2021	31,156,380	$ 76,592	$ 1,937	$ (21,147)	$ (2,597)	$ 54,785
Share-based payments (Note 9)	-	-	306	-	-	306
RSR excerise (Note 8)	85,336	225	(225)	-	-	-
Net loss and comprehensive loss	-	-	-	(2,264)	(474)	(2,738)
Balance as at March 31, 2022	31,241,716	$ 76,817	$ 2,018	$ (23,411)	$ (3,071)	$ 52,353
Balance as at December 31, 2022	31,316,452	$ 76,985	$ 2,863	$ (25,699)	$ (440)	53,709
Share-based payments (Note 9)	-	-	308	-	-	308
RSR excerise (Note 8)	50,480	131	(131)	-	-	-
Net loss and comprehensive loss	-	-	-	(1,020)	(38)	(1,058)
Balance as at March 31, 2023	31,366,932	$ 77,116	$ 3,040	$ (26,719)	$ (478)	$ 52,959

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

KITS EYECARE LTD.
CONDENSED INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS
(in thousands of Canadian Dollars, except share and per share data)
(Unaudited)

	Three months ended March 31	
	2023	**2022**
Operating activities		
Net Income (Loss)	$ (1,020)	$ (2,264)
Items not affecting cash:		
Share-based payments (Note 9)	308	306
Depreciation of property and equipment and right-of-use assets	422	439
Amortization of intangible assets (Note 13)	444	412
Finance costs	409	411
Income taxes	(274)	(714)
Unrealized foreign exchange (gain) / loss	(58)	98
Changes in non-cash operating working capital:		
Accounts receivable	185	70
Inventory	1,931	(814)
Prepaid expenses and other assets	268	162
Accounts payable and accrued liabilities	(857)	1,383
Deferred revenue	250	(535)
Income tax refund received	11	-
Cash provided by / (used in) by operating activities	**2,019**	**(1,046)**
Financing activities		
Repayment of lease obligation (Note 7)	(207)	(264)
Repayment of loan (Note 4(a))	(1,040)	(1,000)
Cash used in financing activities	**(1,247)**	**(1,264)**
Investing activities		
Purchase of property and equipment	(6)	(34)
Cash used in investing activities	**(6)**	**(34)**
Increase / (decrease) in cash and cash equivalents	**766**	**(2,344)**
Foreign exchange effect on cash and cash equivalents	18	169
Cash and cash equivalents, beginning of period	18,790	20,505
Cash and cash equivalents, end of period	**$ 19,574**	**$ 18,330**

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

1. Nature of operations

Kits Eyecare Ltd. (the "Company" or ”KITS”) is vertically integrated, digitally native eyecare platform, with sales primarily in the United States and Canada. The Company was incorporated under the Business Corporations Act (British Columbia) on October 19, 2018 with its registered headquarters located at 1020 - 510 Seymour Street, Vancouver, BC, V6B 3J5.

The Company is listed on the Toronto Stock Exchange (the “TSX”) under the symbol “KITS”.

2. Basis of preparation and statement of compliance

The Company prepares its annual consolidated financial statements in accordance with International Financial Reporting Standards (IFRS) as issued by the International Accounting Standards Board (IASB). These condensed interim consolidated financial statements have been prepared in accordance with IAS 34, Interim Financial Reporting (IAS 34).

These condensed interim consolidated financial statements should be read in conjunction with the Company’s most recent annual consolidated financial statements for the year ended December 31, 2022, as some disclosures from the annual consolidated financial statements have been condensed or omitted. There are no IFRS or International Financial Reporting Interpretations Committee interpretations that are not yet effective that would be expected to have a material impact on the Company’s condensed interim consolidated financial statements.

From July 1, 2022 onwards, the Company had presented exchange gain/loss separately with its comparatives which was previously included within general and administrative expense. The Company is making this change in classification in order to align and better reflect these expenses within the operating results of the Company. There is no change to consolidated net income (loss) or cash flows as a result of this change in classification.

On May 9, 2023, the Board of Directors authorized these condensed interim consolidated financial statements for issuance.

Critical accounting estimates and judgements
In preparing these condensed interim consolidated financial statements management has made judgements and estimates that affect the application of accounting policies and the reported amounts of assets and liabilities, income and expense. Actual results may differ from these estimates.

The significant estimates and judgements made by management in applying the Company’s accounting policies and the key sources of estimation uncertainty were the same as those described in the most recent annual consolidated financial statements.

3. Segment information and deferred revenue

The Company operates in a single reportable operating segment, being the sale of eyewear products to consumers.

Geographic information
The Company determines the geographic location of revenue based on the location of its customers. For the three months ended March 31, 2023,the US/CDN exchange rate appreciated by 6.8% (2022: 0.0%).

	Three months ended March 31	
	2023	2022
United States	$ 20,018	$ 14,135
Canada and other	7,649	5,917
Total	$ 27,667	$ 20,052

All of the Company's non-current assets are located in Canada.

Deferred revenue

Deferred revenue consists of credit vouchers of $844 (December 31, 2022: $938), unfulfilled orders of $2,055 (December 31, 2022: $2,017) and allowance for estimated returns of $838 (December 31, 2022: $532). Credit vouchers relate to vouchers that have been issued or sold to customers. Revenue from credit vouchers is recognized when the vouchers are redeemed, when the likelihood of redemption becomes remote, or when the vouchers expire.

Revenue by product

	Three months ended March 31	
	2023	2022
Contact Lenses	$ 24,285	$ 17,498
Glasses	3,382	2,554
Total	$ 27,667	$ 20,052

4. Financial liabilities

(a) Loan

The Company entered into a secured loan agreement (the "BDC Loan") for $23.4 million with BDC Capital Inc. ("BDC") on March 26, 2019, with a repayment date of April 15, 2026 and a monthly contractual principal payment of $250. Effective as of January 15, 2021, this loan bears interest at BDC floating rate plus a variance of 4.45% per annum and is payable on a monthly basis. As at March 31, 2023, BDC floating rate was 7.80% (2022: 7.55%). The Company is required to make a one-time payment to BDC equal to 0.45% of the Company's annual gross sales at maturity. The BDC Loan is secured by a first ranking security interest in all present and after acquired personal property and all present and future intellectual property of the Company.

The Company is subject to various covenants under the BDC Loan, including requirements to maintain certain financial ratios. The BDC Loan is in good standing as of the date hereof.

As at March 31, 2023, the carrying amount of the loan is $10,475 (2022: $11,257). For the three months ended March 31, 2023, the Company made repayments of $1,040 (2022: $1,000) and recognized $257 (2022: $236) of interest expense in finance costs. Interest expense is calculated by applying the effective interest rate of 9.96% (2022: 9.83%).

(b) Promissory note

On January 18, 2021, the Company issued 15,314,709 common shares in connection with the conversion of all the Company's Class A, B and C preferred shares and a promissory note of $2,412 which are the accrued dividends payable to the holders of the preferred shares. The note bears no interest and matures on the earlier of January 31, 2026 or the date after the Company's current loan from BDC Capital has been repaid in full (the "Maturity Date"). Unpaid principal shall be payable in quarterly installments beginning on March 31, 2021 of

$121, subject to the consent of BDC Capital. Any unpaid principal shall be payable in full upon the Maturity Date.

As at March 31, 2023, the carrying value of the promissory note is $1,920 (2022: $1,884). During the three months ended March 31, 2023, no quarterly principal was paid to the promissory holders and the Company recorded accretion expense of $36 (2022: $34) in finance costs. Accretion expense is calculated by applying the effective interest rate of 8.00%.

5. Financial instruments and fair values

The Company characterizes fair value measurements using a hierarchy that prioritizes inputs depending on the degree to which they are observable. The three levels of the fair value hierarchy are as follows:

- Level 1: fair value measurements are quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: fair value measurements are those derived from inputs other than quoted prices included within level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3: fair value measurements are those derived from valuation techniques that include significant inputs for the asset or liability that are not based on observable market data (unobservable inputs).

The carrying value of cash and cash equivalents, account receivables, and accounts payable and accrued liabilities approximate their fair value because of the short-term nature of these financial instruments. These financial instruments are classified as financial assets and liabilities at amortized cost.

There are no financial liabilities that are measured at fair value. The following table shows the carrying amount and the fair values of financial liabilities, including their levels in the fair value hierarchy.

	March 31, 2023			December 31, 2022		
	Carrying value	Fair value measurement Level 2	Fair value measurement Level 3	Carrying value	Fair value measurement Level 2	Fair value measurement Level 3
Financial liabilities						
Loan	$ 10,475	$ 10,048	$ -	$ 11,257	$ 10,787	$ -
Promissory note	1,920	1,691	-	1,884	1,642	-
Total	$ 12,395	$ 11,739	$ -	$ 13,141	$ 12,429	$ -

During the three months ended March 31, 2023, there have been no transfers of amounts between Level 1, Level 2, and Level 3 of the fair value hierarchy.

The classification of the financial instruments as well as their carrying values as at March 31, 2023 and December 31, 2022 is shown in the table below.

	March 31, 2023			December 31, 2022		
	Amortized cost (Financial asset)	Amortized cost (Financial liabilities)	Total	Amortized cost (Financial asset)	Amortized cost (Financial liabilities)	Total
Financial assets						
Cash and cash equivalents	$ 19,574	$ -	$ 19,574	$ 18,790	$ -	$ 18,790
Accounts and other receivables	712	-	712	897	-	897
Total financial assets	$ 20,286	$ -	$ 20,286	$ 19,687	$ -	$ 19,687
Financial liabilities						
Account payable and accrued liabilities	$ -	$ 15,952	$ 15,952	$ -	$ 16,809	$ 16,809
Loan	-	10,475	10,475	-	11,257	11,257
Promissory note	-	1,920	1,920	-	1,884	1,884
Total financial liabilities	$ -	$ 28,347	$ 28,347	$ -	$ 29,950	$ 29,950

Valuation techniques and significant unobservable inputs

To determine the fair value of financial liabilities at initial recognition, the Company considered the present value of expected payments, discounted using a risk-adjusted discount rate. As at March 31, 2023, none of the Company's financial liabilities are subsequently measured at fair value after initial recognition.

Capital management

The Company manages its capital, which consists of equity and long-term debt with the objectives of safeguarding sufficient net working capital over the annual operating cycle and providing sufficient financial resources to grow operations to meet long-term consumer demand. The Company prepares and updates its annual operational results based on the Company's short and long term objectives and monitors actual operating results compared to the forecast to ensure that there is sufficient capital on hand to grow its operations. The Board of Directors of the Company monitors the Company's capital management on a regular basis. The Company will continually assess the adequacy of the Company's capital structure and capacity and make adjustments within the context of the Company's strategy, economic conditions, and risk characteristics of the business.

Market risk

Market risk is the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in market prices. Market prices comprise interest rate risk and foreign currency risk.

Interest rate risk

The Company is exposed to changes in interest rates on our cash and cash equivalents and loans. The Company's debt has a variable interest rate based on BDC's floating base rate plus a margin. As a result, the Company is exposed to interest rate risk due to fluctuations in the BDC's floating base rate. The principal amount outstanding under the loan was $9,150 as at March 31, 2023 (December 31, 2022: $9,900) which currently bears interest at 12.25% (December 31, 2022: 12.00%). For the three months ended March 31, 2023, a 1.00% increase in the floating interest rate would have increased interest paid by $26 (December 31, 2022: $300) and finance costs by $25 (December 31, 2022: $138).

Currency risk

The Company's and its subsidiary's functional currencies are the Canadian Dollar ("CAD") and the United States Dollar ("USD") respectively. The Company is exposed to fluctuations in the USD and the CAD relative to these functional currencies. The Company has not entered into any agreements or purchased any instruments to hedge possible currency risks at this time. The Company is exposed to the following currency risk as at March 31, 2023:

	March 31, 2023		December 31, 2022	
	USD	CAD	USD	CAD
Cash and cash equivalents	$ -	$ 1,680	$ 12	$ 804
Accounts and other receivables	-	208	-	190
Accounts payable and accrued liabilities	-	(6,041)	-	(6,786)
Total	$ -	$ (4,153)	$ 12	$ (5,792)

A 10% strengthening in the Canadian dollar against the U.S. dollar on net monetary accounts would, with all other variables being constant, have an approximately unfavorable impact of $378 (December 31, 2022: $527) on net loss.

Credit risk

Credit risk refers to the possibility that the Company can suffer financial losses due to the failure of the Company's counterparties to meet their payment obligations. The Company is exposed to minimal credit risk. The Company does not extend credit to customers, but do have some receivables exposure with respect to payment processors transferring customer funds to the Company and to rebates receivable from the Company's vendors. The majority of accounts receivables are settled in under 30 days. In order to reduce this risk, the Company uses industry leading payment processors, including Braintree Payment Gateway, Chase Paymentech, American Express, and PayPal. The Company deposits its cash and cash equivalents with major financial institutions that have been assigned high credit ratings by internationally recognized credit rating agencies. As such, exposure to customer credit risk is nominal.

Liquidity risk

Liquidity risk is the risk that we cannot meet a demand for cash or fund our obligations as they come due. The Company manage liquidity risk by continuously monitoring actual and projected cash flows, taking into account the seasonality of the Company's revenue, income and working capital needs. The following table summarizes the amount of contractual undiscounted future cash flow requirements as March 31, 2023.

Contractual obligations	Carrying amount	Contractual cash flows	Less than 1 year	1-3 years	4-5 years	After 5 years
Accounts payable and accrued liabilities	$ 15,952	$ 15,952	$ 15,952	$ -	$ -	$ -
Loan - Principal amount	10,475	10,457	3,000	6,000	1,457	-
Loan - Interest	-	1,759	951	793	15	-
Promissory note	1,920	2,412	-	-	2,412	-
	$ 28,347	$ 30,580	$ 19,903	$ 6,793	$ 3,884	$ -

6. Inventory

As at March 31, 2023, inventory comprised of $7,419 (2022: $9,094) of contact lenses, $5,581 (2022: $5,909) of frames, prescription lenses of $1,057 (2022: $868) and other miscellaneous inventory of $426 (2022: $543).

7. Leases

During the three months ended March 31, 2023, the Company had $nil (2022: $23) of lease liability additions, paid $207 (2022: $264) of lease payments, recognized $116 (2022: $142) of accretion expense, and $62 (2022: $100) of foreign exchange loss.

During the three months ended March 31, 2023, the Company had $nil (2022: $23) of right-of-use asset additions, recognized depreciation expense of $202 (2022: $189) and incurred $6 (2022: $134) of exchange differences.

8. Share capital

During the three months ended March 31, 2023, 50,480 (2022: 85,336) vested RSRs were delivered to its officers and directors.

9. Share-based compensation

During the three months ended March 31, 2023, the Company granted 15,284 restricted shares rights ("RSRs") to its directors which vest immediately upon grant. The RSRs have a weighted fair value of $3.68 which is the Company's average share price for the period the services were provided. As at March 31, 2023, the Company has a total 23,124 of outstanding RSRs, comprising of 7,840 of non-vested RSRs.

During the three months ended March 31, 2023, 3,500 stock options were forfeited at a weighted average exercise price of $6.26. As at March 31, 2023, the Company has a total of 2,866,808 of stock options outstanding with a weighted average exercise price of $3.15, comprising of 2,355,383 of exercisable stock options with a weighted average exercise price of $2.94.

Share-based compensation expense related to RSRs and options of $62 and $246 (2022: $64 and $242) was recorded for the three months ended March 31, 2023, respectively.

10. Related party transactions

During the three months ended March 31, 2023, the Company paid rent of $nil (2022: $19) to a company under common control of a significant shareholder of the Company and recorded rent of $nil (2022: $30) to a company under common control of another significant shareholder of the Company, of which $22 is unpaid as at March 31, 2023. These amounts have been included in other general and administrative expense and are part of the Company's ordinary course of business. The contract terms were based on market rates for these types of services and were terminated as of December 31, 2022.

During the three months ended March 31, 2023, the Company recorded $31 (2022: $20) of Board fees to its directors (the "Directors") and $56 (2022: $50) of share-based compensation. $31 of Board fees remain unpaid as at March 31, 2023.

Key management compensation
Key management consists of the Board of Directors, the Chief Executive Officer, and the executives who report directly to the Chief Executive Officer. Key management compensation comprises of wages and short-term employee benefits. For the three months ended March 31, 2023, the Company paid $434 (2022: $400) of wages and short-term employee benefits to key management and recorded $176 (2022: $188) of key management share-based compensation.

11. Income taxes

The Company calculates the period income tax expense using the tax rate that would be applicable to the expected total annual earnings. The major components of income tax expense in the condensed interim consolidated statements of loss for the three months ended March 31, 2023 comprises of current income tax expense of $nil (2022: $nil) and deferred income tax recovery of $274 (2022: $714).

As at March 31, 2023, deferred tax assets consist of available non-capital losses and other tax deductions of $6,915 (2022: $6,847), net of deferred tax liability arising from property and equipment, right of use assets and net of lease liability of $766 (2022: $823), intangible assets of $445 (2022: $565), promissory note of $133 (2022: $142), and foreign exchange of $193 (2022: $195). The Company has non-capital losses of approximately $21,733 (2022: $22,017) that can be applied against future years' taxable income for Canadian income tax purposes. The Company has recognized these losses as a deferred income tax asset as it expects to utilize these losses against future taxable income.

12. Loss per share

Weighted average number of ordinary shares used as the denominator in calculating basic and diluted earnings per share is 31,366,932 (2022: 31,241,716).

Common share equivalents that could potentially dilute net income per basic share in the future, but were not included in the computation of diluted earnings per share because the impact would have been anti-dilutive comprised of all issued stock options of the Company.

13. Goodwill and intangible assets

During the three months ended March 31, 2023, the Company recognized $444 (2022: $412) of amortization expenses, and $33 (2022:$566) of exchange differences. The Company exercises judgement to determine whether there is an impairment indicator requiring an impairment test for its goodwill and indefinite life intangible assets to be completed. As at March 31, 2023, no impairment indicators exist.

14. Contingencies

The Company is, from time to time, involved in various claims, legal proceedings and complaints arising in the ordinary course of business. The Company does not believe that adverse decisions in any pending or threatened proceedings, or any amount it may be required to pay by reason thereof, will have a material adverse effect on the financial condition or future results of operations of the Company.