Pacific Safety Products Inc.

TSX VENTURE: PSP

PACIFIC SAFETY PRODUCTS INC. REPORTS FIRST QUARTER OF FISCAL 2011

KANATA, Ontario (November 29, 2010) /CNW/ -- Pacific Safety Products Inc. (TSX VENTURE: PSP) ("PSP" or the "Company"), today reported financial results for the three month period ended September 30, 2010.

Highlights:

- Sales for the first quarter were $4.3 million, approximately 43.6% lower than first quarter of the prior year of $7.6 million.
- The gross margin percentage for the first quarter was 22.1%, up 7.0% from 15.1% for the first quarter of the prior year, but on lower sales this represented a decrease of approximately $0.2 million or 17.3%.
- Operating expenses for the first quarter of $1.6 million decreased $0.1 million or 5.8% from the first quarter of the prior year.
- Adjusted Earnings Before Interest, Taxes, Depreciation and Amortization ("EBITDA")[1] was a loss of $0.4 million for the first quarter compared to a loss of $0.3 million in the first quarter of the prior year.
- Working capital improved from $0.3 million for the year ended June 30, 2010 to $0.7 million for the first quarter.
- On August 17, 2010, the Company issued $1.0 million of unsecured convertible debentures in favour of a group of investors.

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[1] Adjusted EBITDA consists of earnings before interest expense, income taxes, stock based compensation, amortization, and other one-time charges and gains. PSP believes EBITDA is a useful measure in the evaluation of performance. EBITDA is not a measure recognized under Generally Accepted Accounting Principles ("GAAP") and does not have a standardized meaning as prescribed by GAAP. Therefore, EBITDA may not be comparable to similar measures presented by other entities. Investors are cautioned that EBITDA should not be construed as an alternative to net loss determined in accordance with GAAP.

- On August 18, 2010, the Company sold certain of PSP's headborne system assets, in particular, the helmet liner capability, to Revision Eyewear Inc. ("Revision") for $275,000 and a 4% royalty on gross sales over a 5 year period. On September 14, 2010 Revision exercised an option to purchase the remainder of the headborne systems for an additional $100,000 and a 2.5% royalty on gross sales over a 5 year period.
- Subsequent Event: On October 20, 2010, the Company announced that it had signed a letter of intent to complete a business combination by way of a court approved plan of arrangement of Zuni Holdings Inc. ("Zuni"), an NEX listed company, subject to certain conditions. PSP and Zuni entered into an arrangement agreement as of November 17, 2010.

Chief Executive Officer, Doug Lucky, observed, "The Company is renewing its momentum. The PSP Zuni merger squarely addresses the path to achieve financial stability. Combine that with the launch of our new NIJ.06-certified body armour product lines and customer wins including the recent order worth over U.S. $2.0 million for tactical body armour, and you can see evidence the Company is asserting itself in the market in order to create shareholder value."

Financial Covenant Update:

The Company signed a forbearance agreement (the "Forbearance Agreement") with its principal Canadian Bank (the "Bank") on August 17, 2010. Under the terms of the Forbearance Agreement, additional general and financial covenants have been placed on the Company. The Bank has agreed, pursuant to the Forbearance Agreement, not to take steps to realize under the facility prior to February 28, 2011 (the "Forbearance Period") unless a terminating event as defined in the Forbearance Agreement occurs.

Subsequent Event

On October 20, 2010, the Company announced that it had signed a letter of intent (the "LOI") to complete a business combination ("Merger") by way of a court approved plan of arrangement of Zuni Holdings Inc., an NEX listed company. Under the LOI, PSP has agreed to acquire all of the outstanding common shares of Zuni in exchange for PSP common shares at an agreed exchange ratio of one PSP common share for each Zuni common share. Following completion of the Merger, PSP will be owned 45.8% by current PSP shareholders and 54.2% by current Zuni shareholders, based on the current shares issued and outstanding. On a partially diluted basis, assuming exercise or conversion of all outstanding warrants and debentures of PSP, PSP will be owned 55.7% by current PSP shareholders and 44.3% by current Zuni shareholders. On November 18, 2010 PSP and Zuni announced the signing of an arrangement agreement (the "Arrangement Agreement") to complete the Merger. The Ontario Superior Court of Justice issued an interim order authorizing Zuni to call a special meeting of Zuni shareholders (the "Zuni Meeting") for December 22, 2010 to approve the Plan of Arrangement. PSP will hold an annual and special meeting of PSP shareholders (the "PSP Meeting") on December 22, 2010 to approve the issuance of PSP common shares in connection with the Merger and the continuance of PSP under the Canada Business Corporations Act. Subject to certain closing conditions, and non-solicitation and termination provisions, the Merger is currently expected to close on or about December 31, 2010. PSP believes this transaction will solidify its capital position and allow it to take advantage of significant growth opportunities that are available to the Company.

About PSP

The mission statement of Pacific Safety Products Inc. is ***...we bring everyday heroes home safely™.*** PSP is an established industry leader in the production, distribution and sale of high-performance and high-quality safety products for the defence and security market. These products include body armour to protect against ballistic, stab and fragmentation threats, ballistic blankets to reduce blast effects, and protective products against chemical and biological hazards. PSP is the largest body armour manufacturer in Canada, directly supplying the Canadian Department of Defence, Federal Government Agencies and major Canadian law enforcement organizations. The Company also provides specialized law enforcement and safety products through APS Distributors, a division of PSP that services law enforcement and public safety agencies across the country. The Company, through its U.S. subsidiary Sentry Armor Systems Inc., provides body armour products to U.S. based law enforcement and private security firms. The Company also produces tactical clothing. Pacific Safety Products is a reporting issuer in British Columbia, Alberta and Ontario, Canada and publicly trades under the symbol PSP on the TSX Venture Exchange.

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For complete consolidated financial statements with notes and management discussion and analysis, refer to SEDAR (www.sedar.com).

Forward-Looking Statements: This news release contains forward-looking statements based on management's expectations, estimates and projections. All statements that address expectations or projections about the future, including statements about the Company's growth strategy, product development, market position, expected expenditures and financial results are forward-looking statements. Some of the forward-looking statements may be identified by words like "expects," "anticipates," "plans," "intends," "projects," "indicates," and similar expressions. These statements are not guarantees of future performance and involve a number of risks, uncertainties and assumptions. Many factors, including those discussed more fully elsewhere in this release and in documents which may be filed with the British Columbia Securities Commission, the Alberta Securities Commission, the Ontario Securities Commission, the TSX Venture Exchange, as well as others, could cause results to differ materially from those stated. These factors include, but are not limited to, the possible failure to successfully plan and execute business improvement strategies, restrictions on covenants contained in the Company's credit agreement and the existence of defaults under such covenants, failure to consummate the proposed merger, the potential impact of the current economic downturn on the Company's business, the unpredictability of purchasing patterns by governmental agencies, the possibility of a deterioration in the Company's working capital position, the impact that changes in supplier payment terms or slow payment of accounts receivable could have on the Company's liquidity, the unavailability of or increase in price of external capital to finance the Company's research, development and growth initiatives, changes in the laws, regulations, policies and economic conditions, including inflation, interest and foreign currency exchange rate fluctuations of countries in which the Company does business, competition in the Company's markets, successful integration of structural changes or downsizing initiatives, including restructuring plans, acquisitions, divestitures and alliances, cost of raw material, the uncertainty associated with the outcome of research and development of new products, including regulatory approval and market acceptance, and seasonality of sales in some products.

Pacific Safety Products Inc.

REPORT TO SHAREHOLDERS

MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2010 AND 2009

This Management's Discussion and Analysis ("MD&A") of the financial position and results of operations of Pacific Safety Products Inc. (the "Company" or "PSP") has been prepared as of November 29, 2010 and should be read together with the Company's unaudited interim consolidated financial statements for the three months ended September 30, 2010, the audited annual consolidated financial statements and the notes thereto for the year ended June 30, 2010, and the Joint Management Information Circular issued on November 24, 2010. Management is responsible for the preparation and integrity of the consolidated financial statements, including maintenance of appropriate information systems, procedures and internal controls, and to ensure that information used internally or disclosed externally, including the consolidated financial statements and management's discussion and analysis, is complete and reliable. All figures are in **Canadian dollars except as otherwise noted.**

The financial data has been prepared in accordance with Canadian generally accepted accounting principles ("GAAP") and the Company's reporting currency is the Canadian dollar. Pacific Safety Products Inc. is a reporting issuer in Canada in the provinces of British Columbia, Alberta and Ontario. The Company trades on the TSX Venture Exchange under the symbol PSP. Additional regulatory information relating to Pacific Safety Products Inc. can be found at the System for Electronic Document Analysis and Retrieval ("SEDAR") website at www.sedar.com.

FORWARD-LOOKING INFORMATION

A number of the matters discussed in the MD&A deal with potential future circumstances and developments and may constitute "forward-looking" information within the meaning of applicable securities laws. These forward-looking statements relate to anticipated or assumed events or results including, without limitation, projected costs and capital expenditures, future tax losses, plans with respect to internal controls and the Company's outlook, business strategy, direction, plans and objectives. Generally, forward-looking information can be identified as such because of the context of the statements and often include words or phrases such as "will", "believes", "anticipates", "predicts", "plans", "intends", "estimates", "expects", "continues", "is pursuing", "improving", "projects", "indicates", or words or phrases of a similar nature.

The forward-looking information is based on current expectations and assumptions regarding expected growth, results of operations, financial performance and business prospects and opportunities. Forward-looking information is subject to known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company, or general industry results, to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. These factors include, but are not limited to, the possible failure to successfully plan and execute business improvement strategies, restrictions and covenants contained in the Company's credit agreements and the existence of defaults under such covenants, failure to consummate the proposed merger, the potential impact of the current economic downturn on the Company's business, the unpredictability of purchasing patterns by governmental agencies, the possibility of a deterioration in the Company's working capital position, the impact that changes in supplier payment terms or slow payment of accounts receivable could have on the Company's liquidity, the unavailability of or increase in price of external capital to finance the Company's research, development and growth initiatives, changes in the laws, regulations, policies and economic conditions, including inflation, interest and foreign currency exchange rate fluctuations of countries in which the Company does business, competition in the Company's markets, successful integration of structural changes or downsizing initiatives, including restructuring plans, acquisitions, divestitures and alliances, cost of raw material, the uncertainty associated with the outcome of research and development of new products, including regulatory approval and market acceptance, and seasonality of sales in some products, as well as other factors described below under "Part VII: Risks and Uncertainties" and the Company's other filings with applicable securities regulatory authorities which are available at www.sedar.com. The impact of any one risk factor on a particular forward-looking statement is not determinable with certainty as such factors are interdependent upon other factors, and management's course of action would depend upon its assessment of the future, considering all information then available.

Although the Company believes that the expectations and assumptions conveyed by the forward-looking information are reasonable based on information available to it as of November 29, 2010, no assurances can be given as to future results, levels of activity and achievements. All subsequent forward-looking information, whether written or oral, attributable to the Company or persons acting on its behalf, are expressly qualified in their entirety by these cautionary statements and readers are cautioned not to place undue reliance or importance on this information. The Company assumes no obligation to update forward-looking statements should circumstances or management's estimates or opinions change, except as required by applicable law.

MANAGEMENT'S DISCUSSION AND ANALYSIS

Mission

...we bring everyday heroes home safely.™

This MD&A is organized into the following parts:

I. Business Overview and Strategy
II. Results
III. Cash Flow
IV. Liquidity and Capital Resources
V. Quarterly Results
VI. Critical Accounting Estimates, Changes to Accounting Policies
VII. Risks and Uncertainties
VIII. Other Information

Part I: BUSINESS OVERVIEW AND STRATEGY

PSP is an established industry leader in the defence and security market. The Company is engaged in the design, production, sale and distribution of protective and duty products for law enforcement, security and defence. PSP's products are worn or included in equipment used by officers, agents, guards and military personnel. The Company has a significant market position in Canada, where it is one of the largest soft body armour manufacturers. The Company also provides specialized law enforcement and safety products through APS Distributors ("APS"), a division of PSP that services law enforcement and public safety agencies across Canada. The Company, through its wholly-owned subsidiary, Sentry Armor Systems Inc. ("Sentry"), provides body armour products to U.S. based law enforcement and private security firms. The Company's business strategy is to maintain its core body armour market while growing its portfolio of products so that more of what a customer wears or carries to the front line is sold by PSP.

PSP has a significant recurring revenue stream from its Canadian customers in the form of long standing contracts with terms of up to five years. These contracts are with federal, provincial and municipal organizations and agencies. The Company also pursues long-term defence contracts. PSP has been successful in supplying the Canadian military with fragmentation protection products and chemical and biological protection suits. The Company's U.S. business is primarily supplying state, county and municipal law enforcement agencies with soft body armour. These products are sold primarily through a network of third party distributors.

PSP has a research and development program that works cooperatively with customers on new product design. The Company also conducts independent research in future technologies and products that will enhance user effectiveness, increase value and survivability. PSP's current research and development programs are focused on the certification of certain product lines as required by the U.S. Department of Justice.

PSP has manufacturing operations in Arnprior, Ontario and Dover, Tennessee, a distribution centre in Bedford, Nova Scotia and its head office is located in Ottawa, Ontario. Its design and production facilities are all ISO9001 compliant. Founded in 1984, PSP has grown to currently include more than 160 employees at its Canadian and U.S. facilities.

The Company did not achieve certain covenants as stipulated in its operating line credit facility with its principal Canadian lender (the "Bank") in certain prior periods. On May 12, 2010, the Company entered into an arrangement agreement (the "Arrangement Agreement") with Revision Eyewear Inc. ("Revision"). The Arrangement Agreement contemplated that all of the outstanding common shares of PSP would be purchased by Revision at a price of $0.18 per Common Share, payable in cash at closing. On May 25, 2010, the Company was notified by the Bank that it would continue to waive the covenant violations, subject to no further deterioration in the Company's financial position, confirmation of shareholder approval of the acquisition by Revision and the payment in full of all outstanding lines of credit by June 30, 2010.

On June 15, 2010, the Company announced that it agreed with Revision to terminate the Arrangement Agreement as several of PSP's larger shareholders had indicated that they would not support the Arrangement Agreement, and it was apparent that there was insufficient shareholder support to obtain the required two-thirds approval of the shareholders. On August 18, 2010, the Company sold certain of PSP's headborne systems, in particular, the helmet liner capability, to Revision for $275,000 and a 4% royalty on gross sales over a five-year period (the "Headborne Sale"). On September 14, 2010, Revision exercised an option to purchase the remainder of the headborne systems for an additional $100,000 and a 2.5% royalty on gross sales over a five-year period.

On June 24, 2010, the Company was notified by the Bank that the Company had not met the conditions stipulated in its letter of May 25, 2010 and, as a result, the Company was subjected to, among other things; (i) a reduction in the operating line to $3 million from $5 million, (ii) more stringent reporting requirements, and (iii) preparing detailed projections for the 2011 fiscal year, showing maintenance of the Bank's covenants at all times.

The Company signed a forbearance agreement (the "Forbearance Agreement") with the Bank on August 17, 2010. Under the terms of the Forbearance Agreement, additional general and financial covenants have been placed on the Company. The Bank has agreed, pursuant to the Forbearance Agreement, not to take steps to realize under the facility prior to February 28, 2011 (the "Forbearance Period") unless a terminating event as defined in the Forbearance Agreement occurs. In connection with the Forbearance Agreement, the Company notified the holder of long-term debt (the "Lender") and its U.S. operating lender.

A condition of the Company's Forbearance Agreement with its Bank required the Company to request from the Lender a six-month postponement of principal payments related to its long-term debt. The Lender has agreed to this request pursuant to a letter agreement dated August 4, 2010. All other terms and conditions of the debt facility remain unchanged.

On August 17, 2010, the Company issued $1.0 million of unsecured convertible debentures in favour of a group of investors.

On October 20, 2010, the Company announced that it had signed a letter of intent (the "LOI") to complete a business combination ("Merger") by way of a court approved plan of arrangement of Zuni Holdings Inc. ("Zuni"), an NEX listed company. Under the LOI, PSP has agreed to acquire all of the outstanding common shares of Zuni in exchange for PSP common shares at an agreed exchange ratio of one PSP common share for each Zuni common share. Following completion of the Merger, PSP will be owned 45.8% by current PSP shareholders and 54.2% by current Zuni shareholders, based on the current shares issued and outstanding. On a partially diluted basis, assuming exercise or conversion of all outstanding warrants and debentures of PSP, PSP will be owned 55.7% by current PSP shareholders and 44.3% by current Zuni shareholders. On November 18, 2010 PSP and Zuni announced the signing of an arrangement agreement (the "Arrangement Agreement") to complete the Merger. The Ontario Superior Court of Justice issued an interim order authorizing Zuni to call a special meeting of Zuni shareholders (the "Zuni Meeting") for December 22, 2010 to approve the Plan of Arrangement. PSP will hold an annual and special meeting of PSP shareholders (the "PSP Meeting") on December 22, 2010 to approve the issuance of PSP common shares in connection with the Merger and the continuance of PSP under the Canada Business Corporations Act. Subject to certain closing conditions, and non-solicitation and termination provisions, the Merger is currently expected to close on or before December 31, 2010.

PSP believes this transaction will solidify its capital position and allow it to take advantage of growth opportunities that are available to the Company.

There can be no assurance that the Bank will not exercise its rights and remedies during the continuance of any defaults. In addition, if the Bank exercises its rights and remedies, there can be no assurance that a replacement facility can be obtained in order to permit the repayment of indebtedness under the Company's existing operating line credit facilities, or that, if such a replacement facility is obtained, it will be obtained at costs, or on terms and conditions, comparable to those of the Company's current indebtedness.

The Company's ability to continue as a going concern and to realize the carrying value of its assets and discharge its liabilities when due is dependent upon the Company's ability to obtain the ongoing support of its lenders, restore profitable operations and to raise additional capital.

Market Conditions

The Company continues to operate in a challenging environment as evidenced by decreased revenue and a recent history of losses. The reduced sales volume reflects reduced customer buying activity and increased competition as both domestic and foreign suppliers pursue market opportunities. While there have been some signs of improvement, management continues to monitor market conditions closely. Many of PSP's major customers are government departments and agencies at the federal, provincial, state and municipal levels. These organizations continue to operate under budget pressures as governments attempt to reduce spending in light of the current economic environment.

The market for law enforcement and security products in Canada has slowed compared to the same period last year. This market accounted for approximately 56.7% of the Company's revenue during the three months ended September 30, 2010, up from 52.2% for the same period last year. The Company's U.S. market for soft body armour continues to be affected by the economic recession, partially offset by sales to international customers. Currently the U.S. market accounts for approximately 43.3% of total revenue during the three months ended September 30, 2010, down from 47.8% for the same period last year.

Despite challenges in the market, PSP has launched its new NIJ.06-certified body armour product lines, and has recently won contracts for its new LiteX IIIA and LiteX II products with major police forces in British Columbia and Ontario initially worth over $300,000 and with a follow on value of over $800,000 in fiscal 2011 and fiscal 2012. PSP's body armour is known for its comfort, fit, reliability, and quality. Its LiteX product line combines a high level of ballistic protection with a flexible, light weight, and durable design that passes the stringent environmental and ballistic tests required to meet NIJ.06 certification. PSP's products are the only NIJ.06-certified body armour designed and manufactured in Canada, made at PSP's facility in Arnprior, Ontario. Its NIJ.06 certification provides for manufacturing in both its Arnprior and Dover plants. Police forces throughout the U.S. and Canada are in the process of upgrading their body armour to the NIJ.06 standard.

The Company's U.S. subsidiary, Sentry, received an order of over U.S. $2M for its tactical body armor during the second quarter ending December 31, 2010. The body armour is sold under its GH Armor™ brand and will be manufactured at the Company's plant in Dover, Tennessee for delivery during the second and third quarters of fiscal 2011. This order is indicative of PSP's growth strategy for the U.S. market and represents customer confidence in PSP's ability to deliver a large volume of quality product over a tight time frame.

Part II: RESULTS

SUMMARY OF OPERATIONS	*THREE MONTHS ENDED SEPTEMBER 30, 2010*	*THREE MONTHS ENDED SEPTEMBER 30, 2009*
SALES	$ 4,301,951	$ 7,629,381
COST OF SALES	3,352,558	6,481,158
GROSS MARGIN	949,393	1,148,223
EXPENSES	1,597,320	1,695,998
LOSS BEFORE OTHER ITEMS AND TAXES	(647,927)	(547,775)
OTHER ITEMS	115,333	67,407
LOSS BEFORE INCOME TAXES	(763,260)	(615,182)
INCOME TAX EXPENSE (RECOVERY)	2,316	(251,399)
NET AND COMPREHENSIVE LOSS	$ (765,576)	$ (363,783)
BASIC AND DILUTED LOSS PER SHARE	$ (0.03)	$ (0.01)
WEIGHTED AVERAGE BASIC COMMON SHARES ISSUED AND OUTSTANDING – BASIC AND DILUTED	25,741,153	25,654,605

FINANCIAL POSITION	*SEPTEMBER 30, 2010*	*JUNE 30, 2010*
TOTAL ASSETS	$ 10,910,460	$ 12,140,618
TOTAL LONG-TERM FINANCIAL LIABILITIES	$ 1,652,109	$ 946,580

Sales

Sales for the three months ended September 30, 2010 were $4.3 million, a decrease of $3.3 million or 43.6% as compared to the same period in the prior year. The decrease is attributed to a decline in core law enforcement sales in both Canada and the United States primarily as a result of curtailed government spending in light of the current economic environment. Sales from Canadian operations for the three months ended September 30, 2010 were $2.4 million, a decline of $1.5 million or 38.8% as compared to the same period in the prior year. The decrease was primarily attributed to the decline in sales of law enforcement products and a decrease in contract sales. The Company witnessed a marked decline in order intake from its largest customers. Sales from U.S. operations for the three months ended September 30, 2010 were $1.9 million, a decrease of $1.8 million or 48.9% as compared to the same period in the prior year. The decrease is primarily related to significant sales to a U.S. federal government agency in the three months ended September 30, 2009 that were non-recurring.

Gross Margin

For the three months ended September 30, 2010, gross margin as a percentage of sales was 22.1%, which was a significant improvement over the gross margin of 15.1% during the same period in the prior year. The increase is primarily related to product mix and low margin contract sales in the three months ended September 30, 2009.

Expenses

For the three months ended September 30, 2010, expenses were $1.6 million, a decrease of $0.1 million or 5.8% as compared to the same period in the prior year.

For the three months ended September 30, 2010, sales and marketing expenses were $0.6 million as compared to $0.8 million during the same period in the prior year. The decrease is primarily related to cost reduction initiatives implemented over the past two fiscal years.

For the three months ended September 30, 2010, research and development expenses were $0.07 million as compared to $0.08 million during the same period in the prior year. The development costs expense is primarily related to the certification of certain product lines as required by the U.S. Department of Justice.

For the three months ended September 30, 2010, general and administrative expenses were $0.8 million as compared to $0.7 million during the same period in the prior year.

Other Items

For the three months ended September 30, 2010, interest expense on the operating lines of credit and long-term debt was $0.07 million consistent with the same period in the prior year. Accrued interest on convertible debentures for the three months ended September 30, 2010 was $0.01 million. For the three months ended September 30, 2010, the Company recorded an interest expense for accretion of the convertible debentures of $0.01 million.

The Company recorded a further loss of $0.02 million related to the sale of certain PSP headborne system assets during the three months ended September 30, 2010.

Income Taxes

Income tax expense varies from the amount that would be computed by applying the combined federal and provincial tax rate as a result of the tax effect of items not deductible for tax purposes, the tax benefit of losses not recognized and other items.

Net and Comprehensive Loss

For the three months ended September 30, 2010, the Company recorded a net and comprehensive loss of $0.8 million as compared to net and comprehensive loss of $0.4 million during the same period in the prior year. The increase in net and comprehensive loss is primarily due to the reduction in sales compared with the same period in the prior year, and a future income tax recovery recorded in the three months ended September 30, 2009.

Adjusted Earnings Before Interest, Taxes, Depreciation and Amortization ("Adjusted EBITDA")

Adjusted EBITDA is not a recognized performance measure under GAAP and does not have a standardized meaning prescribed by GAAP. The term EBITDA consists of net and comprehensive loss and excludes interest, income tax expense / (recovery), depreciation and amortization. Adjusted EBITDA excludes stock-based compensation and one-time costs. Adjusted EBITDA is included as a supplemental disclosure because management believes that such a measurement provides a better assessment of the Company's operations on a continuing basis by eliminating certain non-cash charges and charges that are nonrecurring. The most directly comparable measure to Adjusted EBITDA calculated in accordance with GAAP is net and comprehensive income (loss). The following is a reconciliation of the Company's Adjusted EBITDA to net and comprehensive loss.

For the three months ended September 30, 2010, Adjusted EBITDA was a loss of $0.4 million compared to an Adjusted EBITDA loss of $0.3 million during the same period in the prior year. The increase in the loss is primarily related to reduced sales volumes.

The following is a reconciliation of Net and Comprehensive Loss to Adjusted EBITDA:

	THREE MONTHS ENDED SEPTEMBER 30, 2010	*THREE MONTHS ENDED SEPTEMBER 30, 2009*
Net and comprehensive loss	$ (765,576)	$ (363,783)
Interest expense	80,773	67,407
Interest expense – accretion of convertible debentures	11,821	–
Income taxes (recovery)	2,316	(251,399)
Stock-based compensation	–	7,426
Amortization	206,460	242,939
Loss on assets held for sale	22,739	–
Adjusted EBITDA	$ (441,467)	$ (297,410)

Part III: CASH FLOW

Cash Flow From (Used In)	*THREE MONTHS ENDED SEPTEMBER 30, 2010*	*THREE MONTHS ENDED SEPTEMBER 30, 2009*
Operating activities	$ (199,993)	$ (1,774,930)
Investing activities	88,952	(408,235)
Financing activities	111,041	1,963,183
	$ –	$ (219,982)

Cash flow used in operating activities for the three months ended September 30, 2010 was $0.2 million as compared to $1.8 million during the same period in the prior year. The reduction in cash flow used in operating activities is primarily due to reduced investment in working capital related to the decline in sales volume.

Cash flow from investing activities for the three months ended September 30, 2010 was $0.1 million as compared to cash flow used in investing activities of $0.4 million during the same period in the prior year. The increase in cash flow was due to reduced spending on property and equipment and product development, and receipt of proceeds from the Headborne sale.

Cash flow from financing activities for the three months ended September 30, 2010 was $0.1 million as compared to $2.0 million during the same period in the prior year. The decrease is primarily due to proceeds from the issue of convertible debentures of $0.9 million being offset by a reduction in the operating lines of credit of $0.8 million during the three months ended September 30, 2010, compared to an increase of $2.0 million in the operating lines of credit during the same period in the prior year.

Part IV: LIQUIDITY AND CAPITAL RESOURCES

AS AT	*SEPTEMBER 30, 2010*	*JUNE 30, 2010*
Operating lines of credit	$ (1,604,292)	$ (2,410,390)
Working capital	699,848	348,704
Long-term debt (long-term portion only)	(1,000,160)	(946,580)
Convertible debenture	(651,949)	–
Shareholders' equity	(4,205,445)	(4,634,541)

The Company's objective when managing liquidity and capital resources is to ensure that it has sufficient liquidity to support its financial obligations and fund its operating and strategic objectives.

The Company's operations and capital expenditures are primarily financed through the use of its credit facilities and working capital. The Company cannot conclude that existing cash resources, together with cash expected to be generated by operations, will be sufficient to meet operational and capital expenditure requirements and meet working capital needs, for at least the next 12 months based on current projections. The Company anticipates minimal capital expenditures in 2011 primarily related to ongoing repairs and maintenance. In order to address the Company's cash requirements, it has signed an Arrangement Agreement to complete a Merger with Zuni.

The Company cannot predict the amount or timing of its need for additional funds under various circumstances, such as continuing operations, new product development, changes to capital structure, or the continued weakness in economic conditions affecting the sectors within which the Company operates. There can be no assurance that, if deemed necessary, additional credit facilities could be obtained in order to permit the repayment of indebtedness under the Company's existing credit facilities, or that, if such a replacement facility was obtained, it could be obtained at costs, or on terms and conditions comparable to those of the Company's current indebtedness.

Working Capital

At September 30, 2010, PSP's working capital was $0.7 million compared to $0.3 million as at June 30, 2010. The increase in working capital is primarily related to the reduction in operating lines of credit as a result of financing received through issue of convertible debentures and proceeds from the Headborne sale.

Accounts receivable as at September 30, 2010 was $3.2 million compared to $4.2 million as at June 30, 2010. The decrease in accounts receivable reflects the decrease in sales in the three months ended September 30, 2010 compared to the three months ended June 30, 2010.

Operating lines of credit

PSP has an agreement with the Bank to provide advances repayable on demand with interest payable monthly calculated at the bank prime lending rate plus 3.50% per annum. The loan is secured by a first priority general security agreement over Canadian accounts receivable and inventory. The maximum operating line is $3.0 million and is subject to margin requirements and covenants set by the Bank. At September 30, 2010, the amount drawn on the line of credit was $1.5 million.

PSP is required to meet certain covenants as outlined in its credit facility agreement with the Bank. In prior periods the Company did not meet certain covenants as stipulated in its credit facility. The Bank has agreed, pursuant to a Forbearance Agreement dated August 17, 2010, not to take steps to realize under the facility prior to February 28, 2011 unless a terminating event as defined in the Forbearance Agreement occurs. During this Forbearance Period, the Company will be subject to amended financial covenants.

Sentry has an agreement with a United States bank to provide advances repayable on demand with interest payable monthly, calculated at the bank prime lending rate plus 2.00% per annum. The loan is secured by a first priority general security agreement over U.S. accounts receivable, inventory and an assignment of insurance. The maximum operating line is $1.4 million USD and is subject to margin requirements and covenants set by the lenders. At September 30, 2010, the amount drawn on the line of credit was $0.1 million.

Long-term Debt

The Company has a $1.4 million secured term loan with the Business Development Bank of Canada ("BDC"). A condition of the Company's Forbearance Agreement with its Bank required the Company to request from BDC a six-month postponement of principal payments related to its long-term debt. BDC agreed, pursuant to a letter agreement dated August 4, 2010, to this request. All other terms and conditions of the debt facility remain unchanged. At September 30, 2010, the principal outstanding on the loan was $1.1 million.

Convertible Debentures

On August 17, 2010, the Company completed a private placement of $1,000,000 aggregate principal amount, consisting of 40 units (the "Units") at a purchase price of $25,000 per Unit. Each Unit consists of $25,000 in principal amount of unsecured convertible debentures (the "Debentures") and 62,500 detachable common share purchase warrants (the "Warrants").

The Debentures mature three years from the date of issuance and bear interest at a rate of 10% per annum, payable annually in cash or common shares at the option of the Company. The holder has the right to convert all (but not less than all), principal and accrued interest at any time to common shares at a rate of one common share per $0.10 of indebtedness (the "Conversion Option"). The Warrants have a one-year term with an exercise price of $0.10 per common share during the first six-months and an exercise price of $0.12 per common share during the second six-months of the term.

Certain Directors of the Company beneficially own, directly or indirectly, $750,000 aggregate principal amount of the Debentures and 1,875,000 Warrants.

The Debentures contain certain default provisions that would provide the holders the right to demand repayment. The Company was in compliance with these conditions at September 30, 2010. These provisions include certain breaches or covenant violations of other credit facilities. The Company believes it is unlikely it will be in compliance with these conditions unless sufficient financing is obtained prior to the expiry of the Forbearance Agreement. Although the Company expects to secure sufficient financing and be in compliance with these conditions in future periods, if they are not, it would result in the holders of the Debentures being able to demand repayment.

Future Income Taxes

At September 30, 2010, the Company had approximately $3.3 million in Canadian non-capital tax loss carry forwards and $2.9 million USD in U.S. tax loss carry forwards available. As at September 30, 2010, the Company increased its income tax valuation allowance by $0.2 million to $3.2 million from $3.0 million at June 30, 2010. The increase is primarily related to the lack of profitability of the Company in the past several years.

Equity Instruments and Other Paid-in Capital

At September 30, 2010 and June 30, 2010, the Company's issued and outstanding shares were 25,741,153. The Company's Contributed Surplus balance was $1.2 million at September 30, 2010 and June 30, 2010. Other paid-in capital of $0.3 million at September 30, 2010 reflects the allocation of the equity component of convertible debentures, net of issue costs.

Capital Management

The Company's capital management strategy is designed to maintain financial strength and flexibility to support profitable growth. The Company's capital consists of accumulated debt, which is comprised of long-term debt, debentures, operating lines of credit and shareholders' equity, excluding other comprehensive income (loss). The Company manages its capital structure and makes adjustments to it, based on the level of funds available to the Company to manage its operations. See "Operating Lines of Credit", "Long-term Debt" and "Convertible Debentures".

The Company has not established a quantitative return on capital criteria, but rather promotes year-over-year sustainable growth.

The Company must adhere to certain financial covenants related to debt. See "Operating Lines of Credit", "Convertible Debentures" and "Long-term Debt".

There have been no changes in the Company's approach to capital management during the period.

Part V: QUARTERLY RESULTS

Fiscal 2011

	September 30, 2010
Sales	**$ 4,301,951**
Net and comprehensive loss	**(765,576)**
Basic and diluted loss per share	**(0.03)**

Fiscal 2010

	September 30, 2009	December 31, 2009	March 31, 2010	June 30, 2010
Sales	$ 7,629,381	$ 7,437,348	$ 7,698,489	$ 7,077,862
Net and comprehensive loss	(363,783)	(158,984)	(87,378)	(2,439,037)
Basic and diluted loss per share	(0.01)	(0.01)	–	(0.09)

Fiscal 2009

	September 30, 2008	December 31, 2008	March 31, 2009	June 30, 2009
Sales	$ 7,706,366	$ 9,592,792	$ 10,548,654	$ 7,187,674
Loss and comprehensive loss	7,757	41,758	417,451	(9,677,628)
Basic and diluted loss per share	–	–	0.02	(0.38)

Significant Fluctuations in Quarterly Results

For the three months ended September 30, 2010, the Company recorded a loss from operations of $0.8 million or $0.03 per share. The decrease in the loss compared to the prior quarter is primarily due to a loss on sale of assets of $0.6 million and a write-down of investment tax credits recoverable of $0.6 million for the three months ended June 30, 2010.

For the three months ended June 30, 2010, the Company recorded a loss from operations of $2.4 million or $0.09 per share. The increase in the loss compared to the prior quarter is primarily due to the reduction in sales and gross margin, costs associated with the Arrangement Agreement and the Headborne Sale, and the write-down of investment tax credits.

Part VI: CRITICAL ACCOUNTING ESTIMATES, CHANGES TO ACCOUNTING POLICIES

Critical Accounting Estimates

In the MD&A for the year ended June 30, 2010, the Company disclosed the accounting policies which management believes are most subject to management's estimation and judgment. As at September 30, 2010, it is management's belief that there are no required changes to those accounting policies. During the current period the Company issued Convertible Debentures along with Warrants. As a result significant management estimates during the period include assumptions used in estimating the fair value of the Debentures, conversion feature and Warrants issued.

Future Changes in Accounting Standards

The Company formally commenced an IFRS conversion project in the fourth quarter of fiscal year 2008 and engaged the services of an external advisor with IFRS expertise to work with management. The Company has developed an IFRS changeover plan in preparation for the conversion to IFRS which addresses the following key elements:

(i) Accounting policy changes and the impact on financial reporting
(ii) Financial reporting expertise and training requirements
(iii) Data systems and information technology impact
(iv) Internal Control over financial reporting
(v) Impact on business activities

An assessment was completed to examine the extent of the impact that the conversion may have on financial reporting, business processes, internal controls and information systems. The Company's plan is aimed in particular at identifying the differences between IFRS and the Company's current accounting policies, as well as assessing the impact of various accounting alternatives offered pursuant to IFRS. PSP's assessment of key areas, including Income Taxes, Foreign Exchange, and Property and Equipment continued in the first quarter of fiscal year 2011.

The Company will continue to evaluate these and other key areas in the coming quarters. The financial impact of the transition to IFRS cannot be reasonably estimated at this time.

Part VII: RISKS AND UNCERTAINTIES

In the normal course of business, the Company's operations continue to be influenced by a number of internal and external factors, and are exposed to risks and uncertainties, that can affect its business, financial condition and operating results. The activities of the Company are subject to ongoing operational risks, including the performance of key suppliers, product performance, government and other industry regulations, and reliance on information systems, all of which may affect the ability of the Company to meet its obligations. The ongoing ability to meet the needs of the market place is dependent on the development and introduction of new products. While management believes its innovation and technology make it a leader in the industry, revenue and results may be affected if products are not accepted in the market place, are not approved by regulatory authorities, or if products are not brought to market in a timely manner.

PSP operates in markets subject to government purchasing patterns and large tenders that are at times unpredictable and create fluctuations in the production load throughout the year. Government purchasing is typically tender driven and subject to competitive bidding. These buying patterns create the necessity of being able to quickly increase and decrease production capacity. PSP has addressed this risk by using cell-based manufacturing in which production staff is grouped into cells. Cells can quickly be added or reduced in order to mitigate the impact of large contracts on regular production of core products. In addition, large contracts often create a situation where a significant portion of the Company's revenue and accounts receivable may be from a small number of customers increasing the risks of economic dependence and concentration of credit.

The Company's working capital position is dependent on the timely collection of accounts receivable, inventory management and scheduled supplier payments. A change in supplier payment terms or slow collection of accounts receivable could adversely affect the Company's liquidity. Management has implemented controls to ensure accounts receivable are current and suppliers payments are largely within terms. However, based on the current estimates, the Company cannot conclude that existing cash resources, together with cash expected to be generated by operations, will be sufficient to meet operating, capital and working capital requirements for at least the next twelve-month period.

Pacific Safety Products Inc. is required to meet certain covenants as outlined in its credit facility with its Bank. In prior periods the Company did not meet certain covenants as stipulated in its credit facility. Pursuant to the Forbearance Agreement, the Bank agreed not to take steps to realize under the facility during the Forbearance Period unless a terminating event as defined in the Forbearance Agreement occurs. During this Forbearance Period, the Company will be subject to amended financial covenants. Should the Company fail to meet any of the conditions imposed by its lender, it would in turn trigger events of default with the Company's other lenders. Management believes that this event would lead to significant uncertainty as the Company would be subject to the demands of its lenders.

Going Concern

There is significant doubt about the appropriateness of the use of the going concern assumption because the Company reported a net loss of $0.8 million for the three months ended September 30, 2010 and a deficit of $14.9 million as at September 30, 2010. In addition, the Company has recently had to seek waivers from its lenders related to covenant violations on borrowings and entered into a forbearance agreement with its lenders. The Company's ability to continue as a going concern and to realize the carrying value of its assets and discharge its liabilities when due is dependent upon the Company's ability to obtain the ongoing support of its lenders, restore profitable operations and raise additional capital.

No Record of Recent Profitability

The Company has incurred a loss of $0.8 million during the three months ended September 30, 2010, and cumulative losses of $12.4 million in the last three fiscal years, including $3.0 million in 2010, $9.2 million in 2009, and $0.2 million in 2008 and there can be no assurance that the future business activities of the Company will restore profitability. The Company's ability to operate profitably and generate positive cash flow in the future will be affected by a variety of factors (including its ability to further develop and test its technology on schedule and on budget, the pace at which it secures additional customers, the time and expense required for the roll-out of its products, its success in marketing such product to its customers, the intensity of the competition experienced by the Company and the availability of additional capital to pursue its business plan, including development of new products). An inability to generate sufficient funds from operations will have a materially adverse effect on the Company's business, results of operations and financial condition.

Limited Managerial and Operating Resources

The Company's operations continue to a generate significant burden on the Company's limited management and operating resources, and may require that the Company hire additional employees and procure additional technical resources, as well as support and administrative personnel. There is no guarantee that the Company will be able to attract and keep the required personnel to meet its requirements or that it will be able to promptly satisfy customers' needs. The Company's business and operating results could be materially and unfavourably affected if it is not able to manage its limited resources.

Defaults under Credit Agreements

Credit facilities with the Bank and the U.S. operating lender are demand facilities. In the event the Merger is not completed, or other liquidity is not created during the Forbearance Period, the Bank may thereafter demand repayment of all amounts owing under the bank indebtedness and by virtue of the inter-lender agreement, the Lender and the U.S. operating lender may also demand repayment. There is also a cross default under the terms of the convertible debenture agreements and the debenture holders have the right to demand repayment of their indebtedness should an event of default occur. Given its present resources, the Company would not be able to repay the indebtedness. In addition, if the Bank exercises its rights and remedies, there can be no assurance that a replacement facility can be obtained in order to permit the repayment of indebtedness under the Company's existing credit facilities, or that, if such a replacement facility is obtained, it will be obtained at costs, or on terms and conditions, comparable to those of the Company's current indebtedness. Consequently, the Bank and/or the Lender, U.S. operating lender, and convertible debenture holders would then be able to avail themselves of a number of remedies, including the court appointment of a receiver for the Company.

For further discussion with respect to defaults under the Company's credit agreements, refer to the Operating Lines of Credit, Long-term Debt, and Convertible Debentures sections in Part IV of this MD&A.

Risks Relating to the Merger

The following is a summary of certain risk factors relating to the proposed merger of the Company and Zuni.

There can be no certainty that all conditions precedent to the Merger will be satisfied.

The completion of the Merger is subject to a number of conditions precedent, certain of which are outside the control of the Company. There can be no certainty that these conditions will be satisfied or, if satisfied, when they will be satisfied. If the Merger is not completed, the market price of the Common Shares may decline to the extent that the market price reflects a market assumption that the Merger will be completed. If the Merger is not completed and the Board of Directors decides to seek another transaction, there can be no assurance that it will be able to find a party willing to pay or accept an equivalent or more attractive price than that reflected in the agreed exchange ratio under the LOI.

The termination fee provided under the LOI may discourage other parties from delivering a Superior Proposal.

Under the Merger LOI, the Company may be required to pay a termination fee. If the Merger is terminated and within six months of such termination the terminating party enters into an agreement relating to the acquisition of a material portion of the shares of such party, or such party's assets or business in whole or in substantial part, and such alternative transaction is consummated, then upon closing of such transaction the terminating party will pay to the non-terminating party: (i) $150,000 if no definitive agreement in respect of the Merger has been executed; or (ii) $150,000 plus expenses incurred by the non-terminating party in relation to the Merger up to a maximum of $100,000 if a definitive agreement in respect of the Merger has been executed. This termination fee may discourage other parties from delivering a superior proposal, even if those parties would otherwise be willing to offer greater value to shareholders than that offered under the LOI with Zuni.

Other Risks

Refer to the Company's June 30, 2010 consolidated financial statements note 15 for other risks including credit risk, interest risk, foreign exchange risk, liquidity risk, and fair value of financial instruments.

Part VIII: OTHER INFORMATION

The authorized share capital of the Company consists of an unlimited number of common shares. As of November 29, 2010, there were 25,741,153 common shares outstanding. As of November 29, 2010, there were 957,800 options outstanding. On August 6, 2010, the Board of Directors approved the grant of 2,100,000 stock options to certain executive officers and senior management, at an exercise price of $0.10. The options were to vest prior to August 31, 2010 and would expire five years following the vesting date. However, in view of the number of options being available to be issued at the date of the grant being less than the amount of the grant, the Company is evaluating steps necessary to fulfill the purported option grant.

Unaudited Interim Consolidated Financial Statements of

PACIFIC SAFETY PRODUCTS INC.

Three months ended September 30, 2010 and 2009

PACIFIC SAFETY PRODUCTS INC.
UNAUDITED INTERIM CONSOLIDATED BALANCE SHEETS

		As at September 30, 2010		As at June 30, 2010
ASSETS				
CURRENT ASSETS				
Accounts receivable	**$**	**3,151,651**	$	4,154,435
Inventory		**2,247,579**		2,258,874
Prepaid expenses and deposits		**313,524**		204,677
Investment tax credits recoverable		**40,000**		40,000
Assets held for sale (note 3)		**–**		250,215
Total current assets		**5,752,754**		6,908,201
PROPERTY AND EQUIPMENT		**1,341,505**		1,426,667
PRODUCT DEVELOPMENT COSTS		**1,131,234**		1,049,423
INTANGIBLE ASSETS		**2,684,967**		2,756,327
TOTAL ASSETS	**$**	**10,910,460**	$	12,140,618
LIABILITIES AND SHAREHOLDERS' EQUITY				
CURRENT LIABILITIES				
Operating lines of credit (note 4)	**$**	**1,604,292**	$	2,410,390
Accounts payable and accrued liabilities		**3,275,214**		3,841,698
Deferred revenue		**30,520**		93,089
Current portion of long-term debt (note 5)		**142,880**		214,320
Total current liabilities		**5,052,906**		6,559,497
LONG-TERM DEBT (note 5)		**1,000,160**		946,580
CONVERTIBLE DEBENTURES (note 6)		**651,949**		–
TOTAL LIABILITIES		**6,705,015**		7,506,077
SHAREHOLDERS' EQUITY				
Share capital (note 7)		**17,614,731**		17,614,731
Warrants (note 7)		**45,500**		–
Contributed surplus (note 8)		**1,194,176**		1,194,176
Other paid-in capital (note 6)		**290,980**		–
Deficit		**(14,939,942)**		(14,174,366)
Total shareholders' equity		**4,205,445**		4,634,541
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY	**$**	**10,910,460**	$	12,140,618

Going concern (note 1)
Subsequent event (note 13)

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

PACIFIC SAFETY PRODUCTS INC.
UNAUDITED INTERIM CONSOLIDATED STATEMENTS OF OPERATIONS, COMPREHENSIVE LOSS AND DEFICIT

	Three months ended September 30, 2010	Three months ended September 30, 2009
SALES	**$ 4,301,951**	$ 7,629,381
COST OF SALES	**3,352,558**	6,481,158
GROSS MARGIN	**949,393**	1,148,223
EXPENSES		
Sales and marketing	**586,684**	786,991
Research and development	**70,339**	81,849
General and administration	**765,470**	674,047
Foreign exchange loss (gain)	**14,193**	(27,255)
Amortization of property and equipment	**38,277**	42,110
Amortization of intangible assets and product development costs	**122,357**	138,256
Total expenses	**1,597,320**	1,695,998
LOSS BEFORE OTHER ITEMS	**(647,927)**	(547,775)
OTHER ITEMS		
Interest on operating lines of credit	**54,207**	50,171
Interest on long-term debt	**14,397**	17,236
Interest on convertible debentures	**12,169**	–
Interest expense - accretion of convertible debentures (note 6)	**11,821**	–
Loss on assets held for sale (note 3)	**22,739**	–
Total other items	**115,333**	67,407
LOSS BEFORE INCOME TAXES	**(763,260)**	(615,182)
INCOME TAXES		
Current income tax expense (recovery)	**2,316**	(6,803)
Future income tax recovery	**–**	(244,596)
Total income tax expense (recovery)	**2,316**	(251,399)
NET AND COMPREHENSIVE LOSS	**(765,576)**	(363,783)
DEFICIT, BEGINNING	**(14,174,366)**	(11,125,184)
DEFICIT, ENDING	**$ (14,939,942)**	$ (11,488,967)
LOSS PER SHARE (note 10) ***BASIC AND DILUTED***	**$ (0.03)**	$ (0.01)
WEIGHTED AVERAGE COMMON SHARES ISSUED AND OUTSTANDING BASIC AND DILUTED	**25,741,153**	25,654,605

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

PACIFIC SAFETY PRODUCTS INC.
UNAUDITED INTERIM CONSOLIDATED STATEMENTS OF CASH FLOW

	Three months ended September 30, 2010	Three months ended September 30, 2009
OPERATING ACTIVITIES		
Cash receipts from customers	**$ 5,242,166**	$ 5,756,172
Cash paid to suppliers and employees	**(5,371,239)**	(7,440,498)
Interest paid	**(68,604)**	(67,407)
Income taxes paid	**(2,316)**	–
Other	**–**	(23,197)
CASH FLOW USED IN OPERATING ACTIVITIES	**(199,993)**	(1,774,930)
INVESTING ACTIVITIES		
Purchase of property and equipment	**(2,820)**	(196,910)
Investment in new product development	**(133,079)**	(204,748)
Investment in intangible assets	**(2,625)**	(6,577)
Proceeds from sale of assets, net of selling costs	**227,476**	–
CASH FLOW FROM (USED IN) INVESTING ACTIVITIES	**88,952**	(408,235)
FINANCING ACTIVITIES		
Proceeds from the issue of convertible debentures, net of issue costs	**935,000**	–
Repayment of long-term debt	**(17,860)**	(53,580)
Increase (decrease) in operating lines of credit	**(806,099)**	2,016,763
CASH FLOW FROM FINANCING ACTIVITIES	**111,041**	1,963,183
DECREASE IN CASH	**–**	(219,982)
CASH, BEGINNING	**–**	219,982
CASH, ENDING	**$ –**	$ –

The accompanying notes are an integral part of these unaudited interim consolidated financial statements.

Pacific Safety Products Inc. ("PSP"), incorporated under the British Columbia Business Corporations Act, manufactures, distributes and sells a complete line of protective products and accessories for the defence and security market. Nexus Armour Inc. ("Nexus") is a wholly-owned subsidiary of PSP and is the parent company of Sentry Armor Systems Inc. ("Sentry"). Sentry is incorporated in the State of Delaware, USA and commenced operations in Dover, Tennessee on July 5, 2006. APS Distributors ("APS") is a division of PSP located in Bedford, Nova Scotia and was acquired by PSP on October 31, 2007.

1. GOING CONCERN

These unaudited consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles ("Canadian GAAP") on a going concern basis, which assumes that the future operations will allow for the realization of assets and discharge of liabilities and commitments in the normal course of business. Should the Company be unable to continue as a going concern, it may be unable to realize the carrying value of its assets and to meet its liabilities as they become due. There is significant doubt about the appropriateness of the use of the going concern assumption because the Company reported a net loss of $0.8 million for the three months ended September 30, 2010 and a deficit of $14.9 million as at September 30, 2010. In addition, as described below, the Company in certain prior periods sought waivers from its lenders related to debt to tangible net worth covenant violations on borrowings and entered into a forbearance agreement with its lenders.

The Company signed a forbearance agreement (the "Forbearance Agreement") with the Bank on August 17, 2010. Under the terms of the Forbearance Agreement, additional general and financial covenants have been placed on the Company. The Bank has agreed, pursuant to the Forbearance Agreement, not to take steps to realize under the facility prior to February 28, 2011 (the "Forbearance Period") unless a terminating event as defined in the Forbearance Agreement occurs. In connection with the Forbearance Agreement, the Company notified the holder of long-term debt (the "Lender") and its U.S. operating lender.

A condition of the Company's Forbearance Agreement with its Bank required the Company to request from the Lender a six-month postponement of principal payments related to its long-term debt. The Lender agreed to this request pursuant to a letter agreement dated August 4, 2010. All other terms and conditions of the debt facility remain unchanged (note 5).

On August 17, 2010, the Company issued $1.0 million of unsecured convertible debentures in favour of a group of investors (note 6).

On October 20, 2010, the Company announced that it had signed a letter of intent (the "LOI") to complete a business combination ("Merger") by way of a court approved plan of arrangement of Zuni Holdings Inc. ("Zuni"), an NEX listed company. On November 18, 2010 PSP and Zuni announced the signing of an arrangement agreement (the "Arrangement Agreement") to complete the Merger. The Ontario Superior Court of Justice issued an interim order authorizing Zuni to call a special meeting of Zuni shareholders (the "Zuni Meeting") for December 22, 2010 to approve the Plan of Arrangement. PSP will hold an annual and special meeting of PSP shareholders (the "PSP Meeting") on December 22, 2010 to approve the issuance of PSP common shares in connection with the Merger and the continuance of PSP under the Canada Business Corporations Act.

There can be no assurance that the Bank will not exercise its rights and remedies during the continuance of any defaults. In addition, if the Bank exercises its rights and remedies, there can be no assurance that a replacement facility can be obtained in order to permit the repayment of indebtedness under the Company's existing credit facilities, or that, if such a replacement facility is obtained, it will be obtained at costs, or on terms and conditions, comparable to those of the Company's current indebtedness.

The Company's ability to continue as a going concern and to realize the carrying value of its assets and discharge its liabilities when due is dependent upon the Company's ability to obtain the ongoing support of its lenders, restore profitable operations and to raise additional capital. These consolidated financial statements do not include any adjustments to the carrying value and classification of assets and liabilities that would be necessary should the Company be unable to continue as a going concern, and such adjustments could be material.

2. SIGNIFICANT ACCOUNTING POLICIES

The unaudited interim consolidated financial statements have been prepared by the Company in accordance with Canadian generally accepted accounting principles ("Canadian GAAP") applicable to interim financial statements. In the opinion of management, the unaudited interim consolidated financial statements fairly present the financial position of the Company as at September 30, 2010. The results of operations are not indicative of operating results for the full year. The unaudited interim consolidated financial statements have been prepared utilizing the same accounting policies and methods of their application as the most recent audited consolidated annual financial statements as at and for the year ended June 30, 2010. The unaudited interim consolidated financial statements do not include all disclosures required according to Canadian GAAP for annual consolidated financial statements and should therefore be read in conjunction with the audited annual consolidated financial statements and notes thereto for the year ended June 30, 2010.

3. *ASSETS HELD FOR SALE*

On August 18, 2010, the Company sold certain PSP headborne system assets, in particular, the helmet liner capability, for $275,000 and a 4% royalty on gross sales over a five-year period. On September 14, 2010, the purchaser exercised an option to acquire the remainder of the headborne systems for an additional $100,000 and a 2.5% royalty on gross sales over a five-year period. The Company recorded a loss of $609,422 related to this transaction in the year ended June 30, 2010 based on the fair value of the assets, less estimated costs to complete the sale. The Company recorded a further loss of $22,739 related to this transaction in the three months ended September 30, 2010.

Proceeds from the sale, net of transaction costs, have been used to reduce the amount drawn on the line of credit.

4. *OPERATING LINES OF CREDIT*

PSP has an agreement with the Bank to provide advances repayable on demand with interest payable monthly calculated at the bank prime lending rate plus 3.50% per annum. The loan is secured by a first priority general security agreement over Canadian accounts receivable and inventory. The maximum operating line is $3.0 million and is subject to margin requirements and covenants set by the Bank. At September 30, 2010, the amount drawn on the line of credit was $1,520,024 (June 30, 2010 - $1,875,094).

PSP is required to meet certain covenants as outlined in its credit facility agreement with the Bank. In prior periods the Company did not meet certain covenants as stipulated in its credit facility. The Bank has agreed, pursuant to a letter agreement dated August 17, 2010 (the "Forbearance Agreement"), not to take steps to realize under the facility prior to February 28, 2011 (the "Forbearance Period") unless a terminating event as defined in the Forbearance Agreement occurs. During this Forbearance Period, the Company will be subject to amended financial covenants.

Sentry has an agreement with a United States bank to provide advances repayable on demand with interest payable monthly calculated at the bank prime lending rate plus 2.00% per annum. The loan is secured by a first priority general security agreement over U.S. accounts receivable, inventory and an assignment of insurance. The maximum operating line is $1.4 million USD and is subject to margin requirements and covenants set by the lenders. At September 30, 2010, the amount drawn on the line of credit was $84,268 (June 30, 2010 - $535,296).

5. *LONG-TERM DEBT*

	As at September 30, 2010	As at June 30, 2010
Secured term loan with interest payable monthly calculated at the Lender's floating base rate of 5.25% at September 30, 2010 plus a variance of 0.75% per annum on the principal outstanding. The principal is repayable by one installment of $17,620 on December 23, 2008, 83 consecutive monthly payments of $17,860 commencing January 23, 2009 with the final payment on May 23, 2016. This loan is secured by a first security interest in all present and after-acquired personal property, subject only to a prior charge with respect to receivables and inventory in favour of the bank providing a Canadian line of credit. A condition of the Company's Forbearance Agreement with its Canadian Chartered bank required the Company to request from its Lender a six-month postponement of principal payments related to its long-term debt. The Lender has agreed, pursuant to a letter agreement dated August 4, 2010, to this request. All other terms and conditions of the debt facility remain unchanged.	**$ 1,143,040**	$ 1,160,900
Less current portion	**(142,880)**	(214,320)
	$ 1,000,160	$ 946,580

5. LONG-TERM DEBT (continued)

The principal instalments required to be paid over the next five years and thereafter are as follows:

Years ending September 30,		
2011	$	**142,880**
2012		**214,320**
2013		**214,320**
2014		**214,320**
2015		**214,320**
Thereafter		**142,880**
	$	**1,143,040**

6. CONVERTIBLE DEBENTURES

On August 17, 2010, the Company completed a private placement of $1,000,000 aggregate principal amount, consisting of 40 units (the "Units") at a purchase price of $25,000 per Unit. Each Unit consists of $25,000 in principal amount of unsecured convertible debentures (the "Debentures") and 62,500 detachable common share purchase warrants (the "Warrants").

The Debentures mature three years from the date of issuance and bear interest at a rate of 10% per annum, payable annually in cash or common shares at the option of the Company. The holder has the right to convert all (but not less than all) principal and accrued interest at any time to common shares at a rate of one common share per $0.10 of indebtedness (the "Conversion Option"). The Warrants have a one-year term with an exercise price of $0.10 per common share during the first six-months and an exercise price of $0.12 per common share during the second six-months of the term.

On the date of issuance, the gross proceeds in the amount of $1,000,000 have been allocated based on the relative fair values of the Debentures ($640,128), the Conversion Option ($314,372) and the Warrants ($45,500). The relative fair value of the Debentures is classified as a liability, while the relative fair values of the Conversion Option and Warrants have been classified as separate components of shareholders' equity.

Over the three-year term, the Debentures are accreted to their principal amount through a periodic charge to accretion expense with a corresponding credit to the liability component. The accretion expense is based on the effective interest method. For the three months ended September 30, 2010, the Company recorded accretion expense of $11,821 related to the Debentures.

The Company incurred transaction costs of $65,000. These costs were allocated to Debenture issuance costs ($41,608) and to equity issuance costs ($23,392) based on the relative fair values of the debt and equity components. The Company has elected a policy to expense Debenture financing costs as incurred.

The fair value of the Conversion Option was estimated using the Black-Scholes option pricing model assuming no expected dividends, a volatility of the Company's share price of 89%, a risk-free interest rate of 1.75%, and an expected life of three years.

The fair value of the Warrants was estimated using the Black-Scholes option pricing model assuming no expected dividends, a volatility of the Company's share price of 101%, a risk-free interest rate of 1.4%, and an expected life of one year.

The fair value of the Debentures was estimated using the present value of future cash flows using a discount rate of 18%.

Certain Directors of the Company beneficially own, directly or indirectly, $750,000 aggregate principal amount of the Debentures and 1,875,000 Warrants.

The Debentures contain certain default provisions that would provide the holders the right to demand repayment. The Company was in compliance with these conditions at September 30, 2010. These provisions include certain breaches or covenant violations of other credit facilities. The Company believes it is unlikely it will be in compliance with these conditions unless sufficient financing is obtained prior to the expiry of the Forbearance Agreement. Although the Company expects to secure sufficient financing and be in compliance with these conditions in future periods, if they are not, it would result in the holders of the Debentures being able to demand repayment.

7. *EQUITY INSTRUMENTS*

(a) Share capital

Authorized
The authorized share capital of the Company consists of unlimited voting common shares without par value.

Issued		**September 30, 2010**		June 30, 2010
	Number of Shares	**Amount**	Number of Shares	Amount
Beginning balance	**25,741,153**	**$ 17,614,731**	25,654,605	$ 17,600,017
Employee Ownership Plan	**–**	**–**	86,548	14,714
Ending balance	**25,741,153**	**$ 17,614,731**	25,741,153	$ 17,614,731

In fiscal 2010, the Company issued 86,548 common shares under the employee ownership plan for proceeds of $14,714.

(b) Warrants

		September 30, 2010		June 30, 2010
	Number of Warrants	**Amount**	Number of Warrants	Amount
Private placement – August 17, 2010 (note 6)	**2,500,000**	**$ 45,500**	–	$ –
Balance, end of period	**2,500,000**	**$ 45,500**	–	$ –

(c) Restricted Shares

Effective March 13, 2007, the Company entered into a Restricted Share Agreement with an Employee. Subject to the terms and conditions of this Agreement, the Company agreed to grant Restricted Shares to the Employee on each of November 26, 2007, 2008 and 2009. The Restricted Shares granted in any year vest one year after the grant date and will be issued to the Employee on the second anniversary of the vesting date. The Company granted 62,206 and 100,000 Restricted Shares on November 26, 2007 and November 26, 2008, respectively, and issued the shares on June 16, 2009. The restricted shares related to fiscal 2010 are expected to be issued in fiscal 2011.

(d) Stock Options

The Company has a stock option plan that provides options to purchase common shares of the Company for its management, executive officers and members of the Board of Directors. These options expire five years after the issue date or, in the event the employee's service ceases, at a date determined by the Board of Directors. Board members' options expire 90 days after termination or resignation, subject to certain exceptions whereby specific board members' options expire one year after resignation. The exercise price for these stock options is set at the average closing price over the previous 20 day trading period. Vesting periods are determined by the Board of Directors upon issuance. At September 30, 2010, the Company had 957,800 stock options outstanding with exercise prices ranging from $0.14 to $1.95.

7. EQUITY INSTRUMENTS (continued)

	Senior Management	*Executive Officers*	*Board of Directors*	*Total*	*Weighted Average Exercise Price*
Balance, June 30, 2010	15,300	355,000	617,500	987,800	$ 0.59
Expired	–	–	(30,000)	(30,000)	0.71
Balance, September 30, 2010	15,300	355,000	587,500	957,800	$ 0.59

	Senior Management	*Executive Officers*	*Board of Directors*	*Weighted Average Exercise Price*	*Total*
Weighted Average Exercise Price	**$ 0.74**	**$ 0.31**	**$ 0.76**	**$ 0.59**	
Weighted Average Remaining Contractual Life (years)	**0.72**	**1.86**	**0.16**		**0.80**
Total Stock Option Pool Authorized					**3,000,000**
Total Stock Option Pool Remaining					**540,170**

The following table summarizes information regarding the Company's outstanding stock options at September 30, 2010:

Options Outstanding				*Options Exercisable*	
Range of Exercise Prices	Number Outstanding	Weighted Average Remaining Life (Years)	Weighted Average Exercise Price	Number Exercisable	Weighted Average Exercise Price
$0.14 to $0.43	530,000	1.55	$ 0.31	530,000	$ 0.31
$0.46 to $0.68	112,800	0.47	0.63	112,800	0.63
$0.71 to $1.03	285,000	0.41	0.96	285,000	0.96
$1.49 to $1.95	30,000	0.01	1.95	30,000	1.95
	957,800		$ 0.59	957,800	$ 0.59

On August 6, 2010, the Board of Directors approved the grant of 2,100,000 stock options to certain executive officers and senior management, at an exercise price of $0.10. The options were to vest prior to August 31, 2010 and would expire five years following the vesting date. However, in view of the number of options being available to be issued at the date of the grant being less than the amount of the grant, the Company is evaluating steps necessary to fulfill the purported option grant.

8. CONTRIBUTED SURPLUS

	Three months ended September 30, 2010	Three months ended September 30, 2009
Balance, beginning of period	**$ 1,194,176**	$ 1,176,991
Stock-based compensation expense	–	17,010
Balance, end of period	**$ 1,194,176**	**$** 1,194,001

9. CAPITAL DISCLOSURES

The Company's objectives when managing capital are: i) to ensure sufficient liquidity to support its financial obligations and execute its operating and strategic plans, ii) to minimize the cost of capital while taking into consideration current and future industry, market and economic risks and conditions, and iii) to maintain an optimal capital structure that provides necessary financial flexibility while also maintaining compliance with financial covenants.

The Company monitors its capital structure, when necessary, in light of changes in economic conditions, the objectives of its shareholders, the cash requirements of the business and the condition of capital markets.

The Company considers its total capitalization to include all interest-bearing debt, including operating lines of credit, long-term debt (including the current portion thereof), convertible debentures and shareholders' equity, net of cash. The calculation is set out in the following table:

	As at September 30, 2010	As at June 30, 2010
Operating lines of credit	**$ 1,604,292**	$ 2,410,390
Current portion of long-term debt	**142,880**	214,320
Long-term debt	**1,000,160**	946,580
Convertible debentures	**651,949**	–
Funded debt	**3,399,281**	3,571,290
Shareholders' equity	**4,205,445**	4,634,541
Capital under management	**$ 7,604,726**	$ 8,205,831

There have been no changes in the Company's approach to capital management during the three months ended September 30, 2010.

10. LOSS PER SHARE

As the Company incurred a net loss during the three months ended September 30, 2010 and 2009, the loss and diluted loss per common share are based on the weighted-average common shares outstanding during the period. The following outstanding instruments could have a dilutive effect in the future:

	As at September 30, 2010	As at June 30, 2010
Shares issuable on conversion of convertible debentures	**10,000,000**	–
Stock options	**957,800**	987,800
Warrants	**2,500,000**	–
	13,457,800	987,800

11. SEGMENTED INFORMATION

The Company's principal business activity is the manufacture, distribution and sale of a complete line of protective products and accessories for the defence and security market. The Company operates in Canada through its PSP and APS Distributors segments with operations based in Arnprior, Ontario and Bedford, Nova Scotia respectively, and in the U.S. through its Sentry subsidiary located in Dover, Tennessee.

These segments represent the Company's reportable segments, which are used to manage the business. The Company analyzes the performance of its operating segments based on revenue growth and operating profitability.

	Canadian Operations	U.S. Operations	Consolidated Total
For the three months ended September 30, 2010			
Revenue	**$ 2,490,971**	**$ 1,884,706**	**$ 4,375,677**
Elimination of inter-segment revenue	**(51,476)**	**(22,250)**	**(73,726)**
Total revenue	**2,439,495**	**1,862,456**	**4,301,951**
Gross margin	**423,933**	**525,460**	**949,393**
Expenses	**1,217,578**	**219,108**	**1,436,686**
Amortization	**114,543**	**46,091**	**160,634**
Other items	**95,049**	**20,284**	**115,333**
Income tax expense	**–**	**2,316**	**2,316**
Net income (loss)	**$ (1,003,237)**	**$ 237,661**	**$ (765,576)**

	Canadian Operations	U.S. Operations	Consolidated Total
For the three months ended September 30, 2009			
Revenue	$ 4,007,751	$ 3,800,969	$ 7,808,720
Elimination of inter-segment revenue	(22,499)	(156,840)	(179,339)
Total revenue	3,985,252	3,644,129	7,629,381
Gross margin	885,612	262,611	1,148,223
Expenses	999,311	516,321	1,515,632
Amortization	114,148	66,218	180,366
Other items	67,407	–	67,407
Income tax recovery	(251,399)	–	(251,399)
Net loss	$ (43,855)	$ (319,928)	$ (363,783)

	Canadian Operations	U.S. Operations	Consolidated Total
***A*S AT SEPTEMBER 30, 2010**			
Assets			
Current assets	**$ 4,248,268**	**$ 1,504,486**	**$ 5,752,754**
Property and equipment	**827,660**	**513,845**	**1,341,505**
Intangible, other assets	**2,496,578**	**1,319,623**	**3,816,201**
	$ 7,572,506	**$ 3,337,954**	**$ 10,910,460**

11. SEGMENTED INFORMATION (continued)

	Canadian Operations	U.S. Operations	Consolidated Total
AS AT JUNE 30, 2010			
Assets			
Current assets	$ 5,309,408	$ 1,598,793	$ 6,908,201
Property and equipment	880,079	546,588	1,426,667
Intangible, other assets	2,442,789	1,362,961	3,805,750
	$ 8,632,276	$ 3,508,342	$ 12,140,618

Sales for the three months ended September 30	**2010**	2009
Domestic	**$ 2,403,619**	$ 4,210,722
United States	**1,661,606**	3,187,532
International	**236,726**	231,127
	$ 4,301,951	$ 7,629,381

The Company had no significant sales (over 10% of revenue) to any one customer during the three months ended September 30, 2010. Included in revenue for the three months ended September 30, 2009 were sales of $1.0 million to the Canadian Federal Government and sales of $2.4 million to a U.S. federal government agency.

The Company experiences sales cycles that can be dependent on the award of contracts by major police agencies and federal government departments. These cycles are, at times, unpredictable and may cause variations in revenue and profitability.

12. COMPARATIVE FIGURES

In certain instances the information presented for comparative purposes have been reclassified to conform to the financial statement presentation adopted for the current period.

13. SUBSEQUENT EVENT

On October 20, 2010, the Company announced that it had signed a LOI to complete a Merger by way of a court approved plan of arrangement of Zuni Holdings Inc., an NEX listed company. Under the LOI, PSP has agreed to acquire all of the outstanding common shares of Zuni in exchange for PSP common shares at an agreed exchange ratio of one PSP common share for each Zuni common share. Following completion of the Merger, PSP will be owned 45.8% by current PSP shareholders and 54.2% by current Zuni shareholders, based on the current shares issued and outstanding. On a partially diluted basis, assuming exercise or conversion of all outstanding warrants and debentures of PSP, PSP will be owned 55.7% by current PSP shareholders and 44.3% by current Zuni shareholders. On November 18, 2010 PSP and Zuni announced the signing of an Arrangement Agreement to complete the Merger. The Ontario Superior Court of Justice issued an interim order authorizing Zuni to call a special meeting of Zuni shareholders for December 22, 2010 to approve the Plan of Arrangement. PSP will hold an annual and special meeting of PSP shareholders on December 22, 2010 to approve the issuance of PSP common shares in connection with the Merger and the continuance of PSP under the Canada Business Corporations Act. Subject to certain closing conditions, and non-solicitation and termination provisions, the Merger is currently expected to close on or before December 31, 2010.