Pacific Safety Products Inc.

REPORT TO SHAREHOLDERS

MANAGEMENT'S DISCUSSION AND ANALYSIS FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2013 and 2012

Management's Discussion and Analysis
September 30, 2013 and 2012
(in Canadian dollars)

This Management's Discussion and Analysis ("MD&A") of the financial position and financial performance of Pacific Safety Products Inc. (the "Company" or "PSP") has been prepared as of November 22, 2013 and should be read together with the Company's unaudited condensed consolidated interim financial statements for the three months ended September 30, 2013, the audited annual consolidated financial statements and the notes thereto for the year ended June 30, 2013, and the Management Information Circular dated November 08, 2013. 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 IAS 34 *Interim Financial Reporting* and International Financial Reporting Standards ("IFRS"), except where otherwise stated, 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 and capital management strategy, direction, plans, growth opportunities 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, 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, including resizing 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 22, 2013, 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 Recent Events
II. Results
III. Cash Flow
IV. Liquidity and Capital Resources
V. Quarterly Results
VI. Significant Accounting Policies and Estimates
VII. Risks and Uncertainties
VIII. Other Information

Part I: BUSINESS OVERVIEW AND RECENT EVENTS

Business Overview

PSP is an established industry leader in the defence and security market. The Company is engaged in the design, production and sale 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, 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 be a preferred supplier of body armour and other personal protection solutions throughout North America.

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, and 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 and its head office is located in Arnprior, Ontario. Its design and production facilities are all ISO9001:2008 registered and compliant to BA9000 (National Institute of Justice Body Armor Quality Management Requirements).

Recent Events

On April 24, 2013 an Arbitrator was formally appointed to settle a lease dispute between PSP and its Arnprior landlord, Arnprior Bay Property Limited, a member of the Huntington Properties Ottawa Inc. group of companies led by Alan Whitten. PSP maintains that it has been overcharged by the landlord over several years. The value of PSP's claim is estimated to be $0.1 million to $0.6 million depending on the outcome of Arbitration.

On June 14, 2013, the Company received certification for a new ballistic panel called the HeliXIIIA. It is one of the lightest, most flexible an most comfortable NIJ 0101.06 level IIIA certified armours available. This new product has been well received by the US, Canadian and international markets adding $0.3 million to revenues in the 3 months ended Sept 30, 2013.

On August 17, 2013, the Company replaced certain unsecured convertible debentures on maturity. The Company repaid $200,000 principal amount of the original debentures plus accrued interest. The remaining $800,000 aggregate principal of the original debentures issued August 17, 2010, plus $40,000 of accrued interest was settled with the issuance of secured debentures ("new debentures"). An additional secured debenture with a principal amount of $50,000 was issued on August 17, 2013.

The company has taken the necessary steps to align and size its operations to current North American business, while maintaining the ability to respond to new North American and international opportunities as they arise. The Company continues to focus on adding value for its customers in conjunction with revenue stability and growth.

Part II: RESULTS

SUMMARY OF OPERATIONS	***THREE MONTHS ENDED SEPTEMBER 30, 2013***	*THREE MONTHS ENDED SEPTEMBER 30, 2012*
REVENUES	**$ 3,823,488**	$ 2,817,538
COST OF SALES	**2,737,979**	2,250,777
GROSS MARGIN	**1,085,509**	566,761
EXPENSES	**867,039**	1,018,681
INCOME (LOSS) BEFORE OTHER ITEMS	**218,470**	(451,920)
OTHER ITEMS	**40,402**	49,591
INCOME (LOSS) BEFORE INCOME TAXES	**178,068**	(501,511)
INCOME TAXES	**–**	–
NET INCOME (LOSS) FOR THE PERIOD	**$ 178,068**	$ (501,511)
OTHER COMPREHENSIVE LOSS	**(41,120)**	(43,426)
TOTAL COMPREHENSIVE INCOME (LOSS) FOR THE PERIOD	**136,948**	(544,937)
EARNINGS (LOSS) PER SHARE -		
BASIC	**$ 0.002**	$ (0.009)
DILLUTED	**$ 0.002**	$ (0.009)

FINANCIAL POSITION	***AS AT SEPTEMBER 30, 2013***	*AS ATJUNE 30, 2013*
TOTAL ASSETS	**$ 5,437,086**	$ 4,469,214
TOTAL LONG-TERM FINANCIAL LIABILITIES	**$ 1,205,211**	$ 510,858

Revenues

Revenues for the three months ended September 30, 2013 were $3.8 million, an increase of $1.0 million or 35.7% as compared to $2.8 million for the same period in the prior year. Revenues from Canadian customers for the three months ended September 30, 2013 were $2.0 million, an increase of $0.4 million or 27.4% compared to the same period in the prior year. The increase relates primarily to the timing of orders from key contracts. Revenues from U.S. and International customers for the three months ended September 30, 2013 were $1.9 million, a increase of $0.6 million or 45.7% compared to the prior year. The increase is primarily related to the launch of the HeliXlllA and an increase in international sales.

Gross Margin

For the three months ended September 30, 2013, gross margin as a percentage of revenues was 28.4%, which was an increase from gross margin of 20.1% during the same period in the prior year. The increase is primarily related to efficiencies from increased sales volumes.

Expenses

For the three months ended September 30, 2013, expenses were $0.87 million, a decrease of $0.15 million or 14.9% as compared to the same period in the prior year. The decrease in expenses is primarily related to cost reduction initiatives implemented over the last two years, including a reduction in headcount.

For the three months ended September 30, 2013, sales and marketing expenses were $0.35 million as compared to $0.30 million during the same period in the prior year. An increase in US sales commissions and travel expenses were partially offset by the reduction in head count.

For the three months ended September 30, 2013, research and development expenses were $0.11 million which is consistent with the same period in the prior year.

For the three months ended September 30, 2013, general and administration expenses were $0.41 million as compared to $0.61 million during the same period in the prior year. The decrease is primarily related to the reduction in headcount and the reduction in non-reocurring consulting fees.

Foreign exchange gains

For the three months ended September 30, 2013, foreign exchange gains were $0.02 million as compared to gains of $0.01 million during the same period in the prior year. The gain is primarily related to the impact of fluctuations in of the Canadian dollar against the U.S. dollar with respect to purchases of materials in U.S. funds.

Finance costs

For the three months ended September 30, 2013, finance costs were $0.06 which is consistent with the same period in the prior year.

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 income (loss) for the period

For the three months ended September 30, 2013, the Company recorded a net income of $0.2 million compared to a net loss of $0.5 million during the same period in the prior year. The increase in income is primarily due to increased sales, improved gross margin and the reduction in expenses.

Other comprehensive income (loss)

For the three months ended September 30, 2013, the Company recorded other comprehensive loss of $0.04 million which is consistent with to the same period in the prior year.

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

Adjusted EBITDA is not a recognized performance measure under IFRS and does not have a standardized meaning prescribed by IFRS. The term EBITDA consists of net income and excludes interest, income tax expense (recovery), depreciation and amortization. Adjusted EBITDA excludes share-based compensation, foreign exchange and one-time charges and gains. 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 non-recurring. The most directly comparable measure to Adjusted EBITDA calculated in accordance with IFRS is net income for the period.

For the three months ended September 30, 2013 Adjusted EBITDA was $0.2 million compared with an Adjusted EBITDA loss of $0.4 million during the same period in the prior year.

The following is a reconciliation of net income for the period to Adjusted EBITDA:

	THREE MONTHS ENDED SEPTEMBER 30, 2013	*THREE MONTHS ENDED SEPTEMBER 30, 2012*
Net Income (loss) for the period	**$ 178,068**	$ (501,511)
Finance costs, net	**60,019**	59,021
Depreciation and amortization	**30,078**	34,118
EBITDA	**$ 268,165**	$ (408,372)
Foreign exchange gains	**(19,617)**	(9,430)
Adjusted EBITDA	**$ 248,548**	$ (417,802)

Part III: CASH FLOW

CASH FLOW FROM (USED IN)	***THREE MONTHS ENDED SEPTEMBER 30, 2013***	*THREE MONTHS ENDED SEPTEMBER 30, 2012*
Operating activities	**$ (330,265)**	$ 538,291
Investing activities	**(8,806)**	(4,061)
Financing activities	**(203,580)**	(53,580)
Increase (decrease) in cash and cash equivalents, net of bank overdraft used for cash management purposes	**$ (542,651)**	$ 480,650

Cash flow used in operating activities for the three months ended September 30, 2013 was $0.3 million as compared to cash flows from operating activities of $0.5 million during the same period in the prior year. The increase in cash used in operating activities is primarily due to the timing of revenues in the quarter and the timing receipts compared to the prior year.

Cash flow used in investing activities for the three months ended September 30, 2013 was minimal due to curtailed spending on capital assets.

Cash flow used in financing activities for the three months ended September 30, 2013 relates to repayments of long-term debt which is consistent with the same period in the prior year and the net repayment of the convertible debentures.

Part IV: LIQUIDITY AND CAPITAL RESOURCES

AS AT	***SEPTEMBER 30, 2013***	*JUNE 30, 2013*
Cash and cash equivalents	**$ 1,157,919**	$ 1,333,784
Bank indebtedness	**(537,337)**	(152,875)
Working capital	**2,575,396**	1,584,245
Long-term debt (long-term portion only)	**(357,200)**	(410,780)
Debentures	**(752,885)**	–
Shareholders' equity	**(1,835,024)**	(1,563,676)

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.

In order to further strengthen the Company's financial position and address its liquidity requirements, the Company continues to consider and evaluate on an ongoing basis, all alternatives available to it. These alternatives include, without limitation, seeking additional sources of financing, identifying and pursuing strategic partnerships, raising additional equity, working closely with the financial institution to obtain favourable borrowing terms and other value enhancing opportunities. The Company receives continued support from its bank and lender. There was a decrease of $1.6 million in expenses in fiscal year 2013 compared to fiscal year 2012 and there has been a decrease of $0.2 million in expenses for the three months ended September 30, 2013 compared to the same period in the prior year.

Working Capital

At September 30, 2013, PSP’s working capital was $2.6 million compared to $1.6 million as at June 30, 2013. The increase in working capital reflects an increase in trade and other receivables of $0.8 million, an increase in inventory of $0.4 million, a net decrease in cash and bank indebtedness of $0.5 million, an increase in trade and other payables of $0.7 million and the repayment/replacement of the convertible debenture of $1.0 million.

Trade and other receivables increased due to increase revenues compared to the three months ended June 30, 2013 and the timing of collection of those revenues.

Inventories as at September 30, 2013 were $1.5 million as compared to $1.1 million as at June 30, 2013. The increase in inventory reflects the higher sales and order volumes during the three months ended September 30, 2013.

Trade and other payables as at September 30, 2013 were $1.6 million as compared to $0.9 million as at June 30, 2013. The increase is primarily related to the increase in trade payables reflecting higher sales volumes and increased purchasing during the three months ended September 30, 2013.

Bank Indebtedness

PSP has an Agreement with a Canadian bank (the "Bank") for a credit facility in the amount of $1.0 million. The facility is a revolving demand facility available by way of overdraft with interest payable monthly calculated at the bank prime lending rate plus 1.95% per annum. The facility is secured by cash collateral of $1.0 million and a general security agreement over all personal property of PSP and its subsidiaries. The Agreement has no financial covenants and is subject to certain general covenants as outlined in the Agreement. At September 30, 2013, the amount drawn on the overdraft facility was $0.5 million. Cash collateral held in a GIC with the Bank in the amount of $1.0 million is included in cash and cash equivalents.

Long-term Debt

The Company has a secured term loan with the Business Development Bank of Canada ("BDC" or the "Lender"). At September 30, 2013, the principal outstanding on the loan was $0.6 million.

Convertible Debentures, New 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 "Convertible Debentures") and 62,500 detachable common share purchase warrants (the "Warrants").
The Warrants expired unexercised on August 17, 2011. The Convertible Debentures had an interest rate of 10% per annum payable in cash or common shares at the option of the company and a maturity date of August 17, 2013.

On August 17, 2013, the Company repaid $200,000 principal amount of the original Convertible Debentures plus accrued interest. The remaining $800,000 aggregate principal of the original Convertible Debentures issued, plus $40,000 of accrued interest was settled with the issuance of secured debentures (the "Debentures"). A Debenture with a principal amount of $50,000 was issued on August 17, 2013.

The terms of the Debentures issued August 17, 2013 are as follows (i) cash interest is payable annually at a rate of 12%; (ii) the term of the debentures are 18 months with a maturity date of February 17, 2015; (iii) the Debentures are secured by way of a general security agreement over all of the assets and property of the company; (iv) the Company issued 3,360,000 Bonus Shares to the Debenture holders at a deemed price of $0.05, such number of common shares representing 20% of the principal amount. The Bonus Shares are subject to a four month and one day hold period from date of issuance.

On the date of issuance, the gross proceeds of the Debenture in the amount of $890,000 were allocated based on the fair values of the Debentures ($755,600) and Bonus Shares ($134,400). On the date of issuance, the fair value of the Debentures was classified as a liability, while the fair values Bonus Shares were classified as part of shareholders' equity.

The terms of the new debentures issued August 17, 2013 are as follows (i) cash interest is payable annually at a rate of 12%; (ii) the term of the debentures are 18 months with a maturity date of February 17, 2015; (iii) the new debentures are secured by way of a general security agreement over all of the assets and property of the company; (iv) the Company issue 3,360,000 Bonus Shares to the debenture holders at a deemed price of $0.05, such number of common shares representing 20% of the principal amount. The Bonus Shares are subject to a four month and one day hold period from date of issuance. Certain directors and a former director of the Company beneficially own or control, directly or indirectly, $665,000 aggregate principal amount of the debentures.

Over the 18 month 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 September 30, 2013, the Company recorded accretion expense of $10,309 related to the Debentures and $16,588 (three months ended September 30, 2012 - $26,301) related to the Convertible Debentures.

The company incurred transaction costs of $14,107 in connection with the issuance of the Debentures. The transaction costs have been capitalized and are being amortized over the term of the Debenture.

Certain directors and a former director of the Company beneficially own or control, directly or indirectly, $665,000 aggregate principal amount of the Debentures.

Deferred Income Taxes

At September 30, 2013, the Company had approximately $4.1 million in Canadian tax non-capital loss carryforwards and $5.0 million in U.S. tax loss carryforwards available, excluding loss carryforwards of Zuni and its subsidiaries which have no operating business activities.

Capital and Other Components of Equity

At September 30, 2013 the Company's issued and outstanding shares were 64,114,895. At June 30, 2013, the Company's issued and outstanding shares were 60,554,895.

On August 17, 2013, the Company issued 3,360,000 Bonus Shares to the debenture holders at a deemed price of $0.05, such number of common shares representing 20% of the principal amount of $890,000 (the replacement debentures). The closing price on the date of issuance was $0.04 per share which was used to determine the value of the share capital.

The Company's contributed surplus balance was $1.9 million at September 30, 2013 and June 30, 2013.

Other paid-in capital of $0.2 million at September 30, 2013 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, convertible debentures, bank indebtedness 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 "Bank Indebtedness", "Long-term Debt" and "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 "Bank Indebtedness", "Long-term Debt" and "Debentures".

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

Part V: QUARTERLY RESULTS

Fiscal 2014	**September 30, 2013**
Sales	**$ 3,823,488**
Net income for the period	**178,068**
Basic and diluted earnings per share	**0.002**

Fiscal 2013	June 30, 2013	March 31, 2013	December 31, 2012	September 30, 2012
Revenues	$ 2,715,543	$ 3,354,535	$ 2,808,904	$ 2,817,538
Net loss for the period	(23,743)	(85,491)	(55,888)	(501,511)
Basic and diluted loss per share	(0.001)	(0.001)	(0.001)	(0.009)

Fiscal 2012	June 30, 2012	March 31, 2012	December 31, 2011	September 30, 2011
Revenues	$ 4,456,155	$ 5,153,175	$ 3,638,271	$ 3,486,062
Net income (loss) for the period	320,894	138,001	(1,397,389)	(297,377)
Basic and diluted earnings (loss) per share	0.006	0.002	(0.024)	(0.005)

Significant Fluctuations in Quarterly Results

For the three months ended September 30, 2013, the Company recorded a net income from operations of $0.2 million or $0.002 per share. The increase in income compared to the prior quarter is due to an increase in revenues and gross margin.

For the three months ended June 30, 2013, the Company recorded net loss from operations of $0.02 million or $0.001 per share. The decrease in loss compared to the prior quarter is primarily due to a decrease in expenses and 1 time adjustments despite lower sales and gross margin.

For the three months ended March 31, 2013, the Company recorded a net loss from operations of $0.09 million or $0.001 per share. The increase in loss compared to the prior quarter is due to lower gross margin despite the increase in revenues.

For the three months ended December 31, 2012, the Company recorded a net loss from operations of $0.06 million or $0.001 per share. The decrease in loss compared to the prior quarter is due to improved gross margin and reductions in expenses.

For the three months ended September 30, 2012, the Company recorded a net loss from operations of $0.5 million or $0.009 per share. The increase in loss compared to the prior quarter is due to the decline in revenues and gross margin.

For the three months ended June 30, 2012, the Company recorded net income from operations of $0.3 million or $0.006 per share. The increase in income compared to the prior quarter is primarily due to increased gross margin and a decrease in expenses.

For the three months ended March 31, 2012, the Company recorded net income from operations of $0.1 million or $0.002 per share. The increase in income compared to the prior quarter is primarily due to increased revenues and gross margin and the long-lived asset impairment charge of $1.2 million at December 31, 2011.

For the three months ended December 31, 2011, the Company recorded a net loss from operations of $1.4 million or $0.024 per share. The increase in the loss compared to the prior quarter is primarily due to the long-lived asset impairment charge of $1.2 million.

Part VI: SIGNIFICANT ACCOUNTING POLICIES AND ESTIMATES

The Company's accounting policies are provided in note 3 to the consolidated financial statements for the year ended June 30, 2013.

Use of estimates and judgments

The preparation of the condensed consolidated interim financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.
Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

In the process of applying the Company's accounting policies, management has made the following estimates and judgments, which have the most significant effect on the amounts recognized in the condensed consolidated interim financial statements:

Impairment of non-financial assets
Impairment exists when the carrying value of a non-financial asset or cash-generating unit exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use. The value in use calculation is based on a discounted cash flow model. The recoverable amount is most sensitive to the discount rate used for the discounted cash flow model as well as the expected future cash flows and the growth rates used.

Depreciation and amortization rates
In calculating the depreciation and amortization expense, management is required to make estimates of the expected useful lives of property and equipment and intangible assets.

Taxes
Deferred tax assets, if any, are recognized for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilized. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and the level of future taxable profits together with future tax planning strategies.

Trade and other receivables
Allowance for doubtful accounts

The Company uses historical trends and performs specific account assessments when determining the allowance for doubtful accounts. These accounting estimates are in respect to the trade and other receivables line on the Company's condensed consolidated interim statement of financial position.

The estimate of the Company's allowance for doubtful accounts could change from period to period due to the allowance being a function of the balance and composition of accounts receivable. If the future were to adversely differ from management's expectations of allowance for doubtful accounts, the Company could experience an additional bad debt charge in the future.

Inventories
Allowance for inventory obsolescence

The Company determines its allowance for inventory obsolescence based upon expected inventory turnover, inventory aging and current and future expectations with respect to product offerings. The Company reviews future revenue trends and forecasts, expected inventory requirements and inventory composition necessary to support future revenues. These accounting estimates are with respect to inventories on the Company's condensed consolidated interim statement of financial position.

The estimate for the Company's allowance for inventory obsolescence could change from period to period due to changes in product offerings and consumer acceptance of those products. If the inventory obsolescence was inadequate it would result in a charge to operations expense in the future.

Provisions
The Company estimates provisions for warranties and onerous contracts. A provision will be recognized if the Company has a legal or constructive obligation due to a prior event. Warranties are based on historical trends. Onerous contracts are based on an

unavoidable cost in excess of any future benefit. The onerous contract provision is calculated at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing the contract.

Share-based compensation

The Company uses the Black-Scholes option-pricing model to determine the grant date fair value of share-based compensation. The following assumptions are used in the model: dividend yield; expected volatility; risk-free interest rate; expected option life; and fair value.

The estimate for the Company's provisions could change from period to period due to changes in historical trends, revenue or the business environment.

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 upon 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 a casual pool of staff and 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.

Dependence on Key Personnel

The success of the Company's operations depends on its senior management team and other key employees, as well as the ability to retain and attract skilled and qualified management and employees. The loss of the services of key personnel could have a material adverse effect on the business, financial condition, results of operations or future prospects of the Company.

Defaults under Credit Agreements

The credit facility with the Canadian bank is a demand facility. In the event that the Company was in default under the terms of the agreement, the bank may thereafter demand repayment of all amounts owing under the bank indebtedness and by virtue of the inter-lender agreement, the Lender may also demand repayment.

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

Other Risks

Refer to the Company's June 30, 2013 consolidated financial statements note 21 for other risks including credit risk, interest rate risk, currency risk, liquidity risk, and fair value of financial instruments.

Part VIII: OTHER INFORMATION

On October 21, 2013, 50,000 stock options were exercised. The authorized share capital of the Company consists of an unlimited number of common shares. As of November 22, 2013, there were 64,164,895 common shares outstanding. As of November 22, 2013, there were 2,950,000 options outstanding.

Condensed Consolidated Interim Financial Statements of

PACIFIC SAFETY PRODUCTS INC.

Three months ended September 30, 2013 and 2012

(in Canadian Dollars)

(Unaudited)

PACIFIC SAFETY PRODUCTS INC.
CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS
(Unaudited)

Notice to Reader

The accompanying condensed consolidated interim financial statements have been prepared by and are the responsibility of the Company's management. The Company's independent auditor has not performed a review of these condensed consolidated interim financial statements in accordance with the standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

Terry Vaudry
Chief Executive Officer

November 22, 2013

PACIFIC SAFETY PRODUCTS INC.
CONDENSED CONSOLIDATED INTERIM STATEMENT OF FINANCIAL POSITION
(Unaudited)

	September 30, 2013	June 30, 2013
ASSETS		
CURRENT ASSETS		
Cash and cash equivalents (note 4)	**$ 1,157,919**	$ 1,333,784
Trade and other receivables	**2,250,935**	1,437,536
Inventories	**1,481,048**	1,100,872
Prepaid expenses	**82,345**	106,733
Total current assets	**4,972,247**	3,978,925
NON-CURRENT ASSETS		
Property and equipment (note 5)	**407,766**	433,216
Prepaid deposits	**57,073**	57,073
Total non-current assets	**464,839**	490,289
TOTAL ASSETS	**$ 5,437,086**	$ 4,469,214
LIABILITIES AND EQUITY		
CURRENT LIABILITIES		
Bank indebtedness (note 7)	**$ 537,338**	$ 152,875
Trade and other payables	**1,570,868**	898,653
Short-term provisions (note 10)	**29,677**	30,270
Deferred revenue	**44,648**	116,747
Current portion of long-term debt (note 8)	**214,320**	214,320
Convertible debentures (note 9)	–	981,815
Total current liabilities	**2,396,851**	2,394,680
NON-CURRENT LIABILITIES		
Long-term debt (note 8)	**357,200**	410,780
Long-term provisions (note 10)	**95,126**	100,078
Debentures (note 9)	**752,885**	-
Total non-current liabilities	**1,205,211**	510,858
TOTAL LIABILITIES	**3,602,062**	2,905,538
EQUITY		
Share capital (note 11)	**20,428,373**	20,293,973
Contributed surplus	**1,852,702**	1,852,702
Other paid-in capital	**234,953**	234,953
Deficit	**(20,521,183)**	(20,699,251)
Accumulated other comprehensive income	**(159,821)**	(118,701)
Total equity	**1,835,024**	1,563,676
TOTAL LIABILITIES AND EQUITY	**$ 5,437,086**	$ 4,469,214

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

PACIFIC SAFETY PRODUCTS INC.
CONDENSED CONSOLIDATED INTERIM STATEMENT OF COMPREHENSIVE INCOME
(Unaudited)

FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2013 and 2012

		2013		2012
REVENUES	**$**	**3,823,488**	$	2,817,538
COST OF SALES		**2,737,979**		2,250,777
GROSS MARGIN		**1,085,509**		566,761
EXPENSES				
Sales and marketing		**347,313**		299,993
Research and development		**108,103**		110,343
General and administration		**411,623**		608,345
Total expenses		**867,039**		1,018,681
INCOME (LOSS) BEFORE OTHER ITEMS		**218,470**		(451,920)
OTHER ITEMS				
Foreign exchange gains		**(19,617)**		(9,430)
Finance income (note 13)		**(9,452)**		(7,946)
Finance costs (note 13)		**69,471**		66,967
Total other items		**40,402**		49,591
INCOME (LOSS) BEFORE INCOME TAXES		**178,068**		(501,511)
INCOME TAXES				
Current income taxes		–		–
NET INCOME (LOSS) FOR THE PERIOD		**178,068**		(501,511)
OTHER COMPREHENSIVE LOSS				
Foreign currency translation differences – foreign operations		**(41,120)**		(43,426)
TOTAL COMPREHENSIVE INCOME (LOSS) FOR THE PERIOD	**$**	**136,948**	**$**	(544,937)
EARNINGS (LOSS) PER SHARE *(note 14)*				
BASIC	***$***	***0.002***	*$*	*(0.009)*
DILUTED	***$***	***0.002***	*$*	*(0.009)*

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

PACIFIC SAFETY PRODUCTS INC.
CONDENSED CONSOLIDATED INTERIM STATEMENT OF CHANGES IN EQUITY
(Unaudited)

FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2013 and 2012

	Share capital	Contributed surplus	Other paid-in capital	Deficit	Cumulative translation account	Total
Balance, June 30, 2012	$ 20,180,223	$ 1,849,202	$ 234,953	$(20,032,618)	$ (181,791)	$ 2,049,969
Net loss for the period	–	–	–	(501,511)	–	(501,511)
Other comprehensive loss:						
Foreign currency translation differences	–	–	–	–	(43,426)	(43,426)
Total comprehensive loss for the period	–	–	–	(501,511)	(43,426)	(544,937)
Total amounts attributable to owners	–	–	–	–	–	–
Balance, September 30, 2012	$ 20,180,223	$ 1,849,202	$ 234,953	$(20,534,129)	$ (225,217)	$ 1,505,032
Balance, June 30, 2013	**$ 20,293,973**	**$ 1,852,702**	**$ 234,953**	**$(20,699,251)**	**$ (118,701)**	**$ 1,563,676**
Net income for the period	**–**	**–**	**–**	**178,068**	**–**	**178,068**
Other comprehensive loss:						
Foreign currency translation differences	**–**	**–**	**–**	**–**	**(41,120)**	**(42,120)**
Total comprehensive income (loss) for the period	**–**	**–**	**–**	**178,068**	**(41,120)**	**136,948**
Shares issued to debentures holders	**134,400**	**–**	**–**	**–**	**–**	**134,400**
Total amounts attributable to owners	**134,400**	**–**	**–**	**–**	**–**	**134,400**
Balance, September 30, 2013	**$ 20,428,373**	**$ 1,852,702**	**$ 234,953**	**$ (20,521,183)**	**$ (159,821)**	**$ 1,833,024**

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

PACIFIC SAFETY PRODUCTS INC.
CONDENSED CONSOLIDATED INTERIM STATEMENT OF CASH FLOWS
(Unaudited)

FOR THE THREE MONTHS ENDED SEPTEMBER 30, 2013 and 2012

	2013	2012
CASH FLOW FROM OPERATING ACTIVITIES		
Cash receipts from customers	**$ 2,923,851**	$ 4,588,213
Cash paid to suppliers and employees	**(3,175,677)**	(3,979,242)
Interest paid	**(73,784)**	(78,626)
Interest received	**9,452**	7,946
CASH FLOW FROM (USED IN) OPERATING ACTIVITIES	**(316,158)**	538,291
CASH FLOW FROM INVESTING ACTIVITIES		
Purchase of property and equipment	**(8,806)**	(4,061)
CASH FLOW USED IN INVESTING ACTIVITIES	**(8,806)**	(4,061)
CASH FLOW FROM FINANCING ACTIVITIES		
Repayment of long-term debt	**(53,580)**	(53,580)
Cost of issuance of Debentures	**(14,107)**	
Repayment of Convertible Debentures	**(1,000,000)**	–
Proceeds from issued Debentures	**850,000**	–
CASH FLOW USED IN FINANCING ACTIVITIES	**(217,687)**	(53,580)
INCREASE (DECREASE) IN CASH AND CASH EQUIVALENTS	**(542,651)**	480,650
CASH AND CASH EQUIVALENTS, NET OF BANK INDEBTEDNESS, BEGINNING	**1,180,909**	1,087,219
Effect of exchange rate fluctuations on cash held	**(17,677)**	(3,687)
CASH AND CASH EQUIVALENTS, NET OF BANK INDEBTEDNESS, ENDING (note 4)	**$ 620,581**	$ 1,564,182

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

1. REPORTING ENTITY

Pacific Safety Products Inc. ("PSP" or the "Company") is a company domiciled in Canada and incorporated under the Canada Business Corporation Act. The address of the Company's head office is 124 Fourth Avenue, Arnprior, Ontario K7S 0A9. The Company manufactures and sells a comprehensive line of protective products for the defence and security markets.

The condensed consolidated interim financial statements of the Company as at and for the year ended June 30, 2013 comprise the Company and its subsidiaries. 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. In accordance with the terms of a Plan of Arrangement, Zuni Holdings Inc. ("Zuni") became a wholly-owned subsidiary of PSP effective December 31, 2010. Zuni is the parent company of MTI Leewood GmbH, MTI Groendyk Inc. and MTI Specialty Silicones Inc. Zuni and its subsidiaries have no operating business activities. MTI Leewood GmbH was deregistered effective June 27, 2012.

2. BASIS OF PREPARATION

(a) Statement of compliance
These condensed consolidated interim financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS"). These condensed consolidated interim financial statements do not include all of the information required for full 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, 2013.

The condensed consolidated interim financial statements were authorized for issue by the Board of Directors on November 22, 2013.

(b) Basis of measurement
These condensed consolidated interim financial statements have been prepared on the historical cost basis except as permitted by IFRS and as otherwise indicated within these notes.

(c) Functional and presentation currency
These condensed consolidated interim financial statements are presented in Canadian dollars, which is the Company's functional currency.

(d) Use of estimates and judgments
The preparation of the condensed consolidated interim financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

In the process of applying the Company's accounting policies, management has made the following estimates and judgments, which have the most significant effect on the amounts recognized in the condensed consolidated interim financial statements:

Impairment of non-financial assets
Impairment exists when the carrying value of a non-financial asset or cash-generating unit exceeds its recoverable amount, which is the higher of its fair value less costs to sell and its value in use. The value in use calculation is based on a discounted cash flow model. The recoverable amount is most sensitive to the discount rate used for the discounted cash flow model as well as the expected future cash flows and the growth rates used.

Depreciation and amortization rates
In calculating the depreciation and amortization expense, management is required to make estimates of the expected useful lives of property and equipment and intangible assets.

d) Use of estimates and judgments (continued):

Taxes
Deferred tax assets, if any, are recognized for all unused tax losses to the extent that it is probable that taxable profit will be available against which the losses can be utilized. Significant management judgment is required to determine the amount of deferred tax assets that can be recognized, based upon the likely timing and the level of future taxable profits together with future tax planning strategies.

Trade and other receivables

Allowance for doubtful accounts

The Company uses historical trends and performs specific account assessments when determining the allowance for doubtful accounts. These accounting estimates are in respect to the trade and other receivables line on the Company's condensed consolidated interim statement of financial position.

The estimate of the Company's allowance for doubtful accounts could change from period to period due to the allowance being a function of the balance and composition of accounts receivable. If the future were to adversely differ from management's expectations of allowance for doubtful accounts, the Company could experience an additional bad debt charge in the future.

Inventories

Allowance for inventory obsolescence

The Company determines its allowance for inventory obsolescence based upon expected inventory turnover, inventory aging and current and future expectations with respect to product offerings. The Company reviews future revenue trends and forecasts, expected inventory requirements and inventory composition necessary to support future revenues. These accounting estimates are with respect to inventories on the Company's condensed consolidated interim statement of financial position.

The estimate for the Company's allowance for inventory obsolescence could change from period to period due to changes in product offerings and consumer acceptance of those products. If the inventory obsolescence was inadequate it would result in a charge to operations expense in the future.

Provisions
The Company estimates provisions for warranties and onerous contracts. A provision will be recognized if the Company has a legal or constructive obligation due to a prior event. Warranties are based on historical trends. Onerous contracts are based on an unavoidable cost in excess of any future benefit. The onerous contract provision is calculated at the present value of the lower of the expected cost of terminating the contract and the expected net cost of continuing the contract.

The estimate for the Company's provisions could change from period to period due to changes in historical trends, revenue or the business environment

Share-based compensation
The Company uses the Black-Scholes option-pricing model to determine the grant date fair value of share-based compensation. The following assumptions are used in the model: dividend yield; expected volatility; risk-free interest rate; expected option life; and fair value.

The estimate for the Company's provisions could change from period to period due to changes in historical trends, revenue or the business environment.

(e) Basis of consolidation

The consolidated financial statements comprise the accounts of the Company and its wholly-owned subsidiaries.

Subsidiaries are consolidated from the date of acquisition, being the date on which the Company obtains control, and continue to be consolidated until the date that such control ceases. The financial statements of the subsidiaries are prepared for the same reporting period as the Company using consistent accounting policies. Intra-group balances and transactions, and any unrealized income and expenses arising from intra-group transactions, are eliminated in preparing the consolidated financial statements

3. SIGNIFICANT ACCOUNTING POLICIES

The accounting policies set out in note 3 to the consolidated financial statements for the year ended June 30, 2013 have been applied consistently to all periods presented in these condensed consolidated interim financial statements.

4. CASH AND CASH EQUIVALENTS

	September 30, 2013	June 30, 2013
Bank balances	**$ 117,919**	$ 293,784
Guaranteed investment certificates	**1,040,000**	1,040,000
Cash and cash equivalents	**1,157,919**	1,333,784
Bank overdraft used for cash management purposes	**(537,338)**	(152,875)
Cash and cash equivalents in the statement of cash flows	**$ 620,581**	$ 1,180,909

Cash held in guaranteed investment certificates (“GIC”) includes $1,040,000 held by the Canadian Bank as cash collateral for the overdraft facility.

5. PROPERTY AND EQUIPMENT

	Manufacturing equipment	Office equipment	Leasehold improvements	Computer equipment	Total
Cost or deemed cost					
As at June 30, 2012	$ 601,660	$ 49,532	$ 236,439	$ 35,920	$ 923,551
Additions	13,379	–	19,111	11,529	44,019
Effect of movements in exchange rates	10,222	263	3,524	349	14,358
As at June 30, 2013	625,261	49,795	259,074	47,798	981,928
Additions	1,999	–	–	6,807	8,806
Effect of movements in exchange rates	(6,415)	(168)	(1,989)	(185)	(8,757)
As at September 30, 2013	$ 620,845	$ 49,627	$ 257,085	$ 54,420	$ 981,977
Depreciation and impairment losses					
As at June 30, 2012	$ 298,487	$ 22,173	$ 64,010	$ 15,718	$ 400,388
Depreciation	86,295	7,005	38,842	8,483	140,625
Effect of movements in exchange rates	5,970	158	1,358	213	7,699
As at June 30, 2013	390,752	29,336	104,210	24,414	548,712
Depreciation	16,011	1,306	10,507	2,254	30,078
Effect of movements in exchange rates	(3,589)	(96)	(771)	(123)	(4,579)
As at September 30, 2013	$ 403,174	$ 30,546	$ 113,946	$ 26,545	$ 574,211
Net book value					
As at June 30, 2013	$ 234,509	$ 20,459	$ 154,864	$ 23,384	$ 433,216
As at September 30, 2013	**$ 217,671**	**$ 19,081**	**$ 143,139**	**$ 27,875**	**$ 407,766**

6. INTANGIBLE ASSETS

At December 31, 2011, it was determined that the remaining intangible assets of both the Canada CGU and the US CGU were fully impaired and an impairment loss was recognized.

Impairment
At September 30, 2013, management determined that there has not been any change to the assets' value in use, fair value less costs to sell, or resulting recoverable amount

7. BANK INDEBTEDNESS

PSP has an Agreement with a Canadian bank (the "Bank") for a credit facility in the amount of $1.0 million. The facility is a revolving demand facility available by way of overdraft with interest payable monthly calculated at the bank prime lending rate plus 1.95% per annum. The facility is secured by cash collateral of $1.0 million and a general security agreement over all personal property of PSP and its subsidiaries. The Agreement has no financial covenants and is subject to certain general covenants as outlined in the Agreement. At September 30, 2013 and June 30, 2013, the amounts drawn on the overdraft facility were $537,338 and $152,875, respectively. Cash collateral held in a GIC with the Bank in the amount of $1,040,000 is included in cash and cash equivalents at September 30, 2013 and June 30, 2013.

8. LONG-TERM DEBT

	September 30, 2013	June 30, 2013
Secured term loan with interest payable monthly calculated at the Lender's floating base rate of 5% at September 30, 2013 plus a variance of 0.75% per annum on the principal outstanding. The variance rate will move to 2.3% if (i) financial statements are not submitted within 6 months of year end or (ii) available funds less non-financed capital expenditures in the most recent fiscal year are at least 1.5 times the current portion of long-term debt or (iii) the debt to equity ratio does not exceed 1.0:1. Debt being defined as long-term debt plus capital leases plus book value of preferred shares subject to a formal redemption agreement. The principal is repayable by one installment of $17,620 on December 23, 2008, 83 consecutive monthly payments of $17,860 commencing January 23, 2009 with the final payment on May 23, 2016. This loan is secured by a first security interest in all present and after-acquired personal property, subject only to a prior charge with respect to receivables and inventory in favour of the bank providing a Canadian credit facility.	**$ 571,520**	$ 625,100
Less current portion	**(214,320)**	(214,320)
	$ 357,200	$ 410,780

The principal installments are required to be paid as follows:

Years ending September 30,	
2014	$ 214,320
2015	214,320
2016	142,880
	$ 571,520

9. 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 "Convertible Debentures") and 62,500 detachable common share purchase warrants (the "Warrants"). The Warrants expired unexercised on August 17, 2011. The Convertible Debentures had an interest rate of 10% per annum payable in cash or common shares at the option of the company and a maturity date of August 17, 2013.

On August 17, 2013, the Company repaid $200,000 principal amount of the original Convertible Debentures plus accrued interest. The remaining $800,000 aggregate principal of the original Convertible Debentures issued, plus $40,000 of accrued interest was settled with the issuance of secured debentures (the "Debentures"). A Debenture with a principal amount of $50,000 was issued on August 17, 2013.

The terms of the Debentures issued August 17, 2013 are as follows (i) cash interest is payable annually at a rate of 12%; (ii) the term of the debentures are 18 months with a maturity date of February 17, 2015; (iii) the Debentures are secured by way of a general security agreement over all of the assets and property of the company; (iv) the Company issued 3,360,000 Bonus Shares to the Debenture holders at a deemed price of $0.05, such number of common shares representing 20% of the principal amount. The Bonus Shares are subject to a four month and one day hold period from date of issuance.

On the date of issuance, the gross proceeds of the Debenture in the amount of $890,000 were allocated based on the fair values of the Debentures ($755,600) and Bonus Shares ($134,400). On the date of issuance, the fair value of the Debentures was classified as a liability, while the fair values Bonus Shares were classified as part of shareholders' equity.

The terms of the new debentures issued August 17, 2013 are as follows (i) cash interest is payable annually at a rate of 12%; (ii) the term of the debentures are 18 months with a maturity date of February 17, 2015; (iii) the new debentures are secured by way of a general security agreement over all of the assets and property of the company; (iv) the Company issue 3,360,000 Bonus Shares to the debenture holders at a deemed price of $0.05, such number of common shares representing 20% of the principal amount. The Bonus Shares are subject to a four month and one day hold period from date of issuance. Certain directors and a former director of the Company beneficially own or control, directly or indirectly, $665,000 aggregate principal amount of the debentures.

Over the 18 month 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 September 30, 2013, the Company recorded accretion expense of $10,309 related to the Debentures and $16,588 (three months ended September 30, 2012 - $26,301) related to the Convertible Debentures.

The company incurred transaction costs of $14,107 in connection with the issuance of the Debentures. The transaction costs have been capitalized and are being amortized over the term of the Debenture.

Certain directors and a former director of the Company beneficially own or control, directly or indirectly, $665,000 aggregate principal amount of the Debentures.

10. PROVISIONS

The provision for warranties is based on estimates made from historical data associated with similar products. At September 30, 2013 the warranty liability was $43,849 (June 30, 2013 - $44,323).

On August 16, 2011 the Company signed a sublease for the remaining lease term for its former head office premises in Kanata, Ontario. The Company recognized a provision for the discounted future lease payments to which the Company is committed less expected future sublease income in the amount of $122,308. The balance in the provision for onerous contracts at September 30, 2013 was $80,954 (June 30, 2013 - $86,025).

11. CAPITAL AND OTHER COMPONENTS OF EQUITY

(a) Share capital

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

		September 30, 2013		June 30, 2013
	Number of Shares	**Amount**	Number of Shares	Amount
Balance, beginning of period	**60,554,895**	**$ 20,293,973**	57,454,894	$ 20,180,023
Shares issued to Debenture holders	**3,560,000**	**134,400**	–	–
Shares issued	–	–	3,100,000	113,950
Balance, end of period	**64,114,895**	**$ 20,428,373**	60,554,895	$ 20,293,973

On August 19, 2013 the company issues 3,560,000 Common Shares at a deemed value of $0.05 in conjunction with the issuance of replacement debentures with an aggregate principal of $890,000. The closing price on the date of issuance was $0.04 per share which was used to determine the value of the share capital.

On June 23, 2013, the Company issued 1,050,000 common shares at a deemed price of $0.05 per share in settlement of $30,000 of accrued directors fees and $22,500 of accrued executive compensation. The difference between the closing price on the date of issuance of $0.04 and the deemed price of $0.05 has been allocated to general and administrative expense.

On October 10, 2012, the Company issued 800,000 common shares at a deemed price of $0.05 per share in settlement of $40,000 of interest payable on the Convertible Debentures and 1,250,000 common shares at a deemed price of $0.05 per share in settlement of $55,000 of accrued directors fees and $7,500 of accrued compensation. The difference between the closing price on the date of issuance of $0.035 and the deemed price of $0.05 has been allocated to general and administrative expense.

(b) Stock Options

The PSP Stock Option Plan provides options to purchase common shares of the Company for its management, executive officers and members of the Board of Directors. Under the PSP Stock Option Plan, the PSP Board determines the term of any options granted, which shall not exceed ten years from the date of grant. The exercise price and vesting periods will be determined by the Board of Directors upon issuance. The expiration of any PSP option will be accelerated if the participant's employment or other relationship with PSP terminates.

On April 5, 2013, the Board approved a new Fixed Stock Option Plan ("2013 Plan") which will replaced the existing stock option plan of the Company, adopted December 22, 2010. The number of shares reserved for issuance under the 2013 Plan is fixed at 5,950,489 shares. All other terms of the plan remain in accordance with the PSP Stock Option Plan.

Recently the Toronto Stock Exchange allowed companies to apply to have the strike price of options previously issued lowered from a minimum of 10 cents to a minimum of 5 cents. PSP applied to have their options reduced and received permission on September 26, 2013. The approval applied to 1,250,000 of previously granted stock. None of the option holders who are subject to the re-pricing are insiders of the Company.

11. CAPITAL AND OTHER COMPONENTS OF EQUITY (CONTINUED)

At September 30, 2013 the Company had 3,000,000 stock options outstanding with an weighted-average exercise price of $0.08 compared with 3,075,000 stock options outstanding with an exercise price of $0.10 at June 30, 2013.
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	Total		***Weighted Average Exercise Price***
Balance, June 30, 2013	3,075,000	$	0.10
Expired	75,000		0.10
Balance, September 30, 2013	**3,000,000**	**$**	**0.08**

The following table summarizes information regarding the Company's stock options as at September 30, 2013:

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
$0.10	1,750,000	1.52	$	0.10	1,750,000	$	0.10
$0.05	1,250,000	2.71	$	0.05	1,250,000	$	0.05
Options outstanding, end of period	3,000,000	2.65	$	0.08	3,000,000	$	0.08

Total Stock Option Pool Authorized	5,950,489
Total Stock Option Pool Remaining	2,950,489

12. OPERATING SEGMENTS

The Company's principal business activity is the manufacture and sale of a comprehensive line of protective products and accessories for the defence and security market. The Company operates in Canada through PSP with operations based in Arnprior, Ontario, and in the U.S. through its Sentry subsidiary located in Dover, Tennessee. Head office expenses, including the office of the CEO and public company costs, are reported as Corporate.

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. Assets acquired pursuant to a Plan of Arrangement (note 1) are reported as Corporate assets.

Transfer prices between operating segments are on an arm’s length basis in a manner similar to transactions with third parties.

12. OPERATING SEGMENTS (CONTINUED)

	Canadian Operations	U.S. Operations	Corporate	Consolidated Total
For the three months ended September 30, 2013				
Revenue	**$ 2,042,225**	**$ 1,861,892**	**$ –**	**$ 3,904,117**
Elimination of inter-segment revenue	**(79,244)**	**(1,385)**	**–**	**(80,629)**
Total revenue	**1,962,981**	**1,860,507**	**–**	**3,823,488**
Gross margin	**563,019**	**522,490**	**–**	**1,085,509**
Expenses	**464,340**	**207,944**	**194,755**	**867,039**
Other items	**40,402**	**–**	**–**	**40,402**
Net income (loss) after taxes	**$ 58,277**	**$ 314,546**	**$ (194,755)**	**$ 178,068**

	Canadian Operations	U.S. Operations	Corporate	Consolidated Total
For the three months ended September 30, 2012				
Revenue	$ 1,619,447	$ 1,281,504	$ –	$ 2,900,951
Elimination of inter-segment revenue	(78,477)	(4,936)	–	(83,413)
Total revenue	1,540,970	1,276,568	–	2,817,538
Gross margin	302,702	264,059	–	566,761
Expenses	510,969	152,607	355,105	1,018,681
Other items	49,266	–	325	49,591
Net income (loss) after taxes	$ (257,533)	$ 111,452	$ (355,430)	$ (501,511)

	Canadian Operations	U.S. Operations	Corporate	Consolidated Total
AS AT SEPTEMBER 30, 2013				
Assets				
Current assets	**$ 3,456,742**	**$ 1,512,636**	**$ 2,869**	**$ 4,972,247**
Property and equipment	**212,541**	**195,225**	**–**	**407,766**
Prepaid deposits	**57,073**	**–**	**–**	**57,073**
	$ 3,726,356	**$ 1,707,861**	**$ 2,869**	**$ 5,437,086**
Liabilities				
Current liabilities	**$ 1,541,791**	**$ 498,815**	**$ 356,245**	**$ 2,396,851**
Long-term debt	**–**	**–**	**1,110,085**	**1,110,085**
Long-term provisions	**76,953**	**18,173**	**–**	**95,126**
	$ 1,618,744	**$ 516,988**	**$ 182,869**	**$ 3,602,062**

12. OPERATING SEGMENTS (CONTINUED)

	Canadian Operations	U.S. Operations	Corporate	Consolidated Total
AS AT JUNE 30, 2013				
Assets				
Current assets	$ 2,525,152	$ 1,270,904	$ 182,869	$ 3,978,925
Property and equipment	221,581	211,635	–	433,216
Prepaid deposits	57,073	–	–	57,073
	$ 2,803,806	$ 1,482,539	$ 182,869	$ 4,469,214
Liabilities				
Current liabilities	$ 699,059	$ 352,081	$ 1,343,540	$ 2,394,680
Long-term debt	–	–	410,780	410,780
Long-term provisions	81,525	18,553	–	100,078
	$ 777,624	$ 370,634	$ 1,760,067	$ 2,905,538

Revenue for the three months ended September 30,	**2013**	2012
Canada	**$ 1,962,981**	$ 1,540,970
United States	**1,135,576**	1,189,035
International	**724,931**	87,533
	$ 3,823,488	$ 2,817,538

Revenues for the three months ended September 30, 2013 include $0.8 million from a Canadian Provincial Government (three months ended September 30, 2012 - $0.4 million), which represents 22.6% (three months ended September 30, 2012 – 14.1%).

Revenues from one U.S. distributor for the three months ended September 30, 2013 were $0.6 million, representing 15.8% of total revenues. The Company had no other significant sales (over 10% of revenue) to any one customer.

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.

13. FINANCE INCOME AND FINANCE COSTS

Recognized in profit or loss:

For the three months ended September 30,	**2013**	2012
Interest income on bank deposits	**$ 9,452**	$ 7,946
Finance income	**$ 9,452**	$ 7,946
Interest on bank indebtedness	**$ 4,986**	$ 3,795
Interest on long-term debt	**8,738**	11,872
Interest on debentures and convertible debentures	**28,790**	24,999
Accretion of debentures and convertible debentures	**26,987**	26,301
Finance costs	**$ 69,471**	$ 66,967

14. EARNINGS PER SHARE

Basic earnings per share amounts are calculated by dividing the net income for the period by the weighted-average common shares outstanding during the period. Diluted earnings per share amounts are calculated by dividing the net income for the period by the weighted-average common shares outstanding plus the weight-average number of common shares that would be issued on conversion of all the dilutive potential common shares into common shares.

The following outstanding instruments had a dilutive effect for the three months ended September 30, 2013 and could have a dilutive effect in the future:

	September 30, 2013
Stock options	**3,000,000**
	3,000,000

15. RELATED PARTY TRANSACTIONS

Trade and other payables as of September 30, 2013 includes interest payable and directors fees payable to the directors and a former director of $19,492 (June 30, 2013 - $63,155).

On August 17, 2013 interest of $35,000 was settled in cash and interest of $40,000 by the settlement of replacement Debentures to debentures holders who are directors or former directors. Certain directors and a former director of the Company beneficially own or control, directly or indirectly, $665,000 aggregate principal amount of the Debentures.

Consulting expenses for services performed by a former director of the Company during the three months ended September 30, 2013 were $Nil (three months ended September 30, 2012 - $31,250). These expenses are included in general and administrative expenses.