



**2005**  
**Three Month Report**

## Sirit Inc.

### MANAGEMENT'S DISCUSSION AND ANALYSIS

*The following MD&A has been prepared to help investors understand the financial performance of the Company and provides information that management believes is relevant to an assessment and understanding of the Company's risks, opportunities and performance measures. Management has prepared this document in conjunction with its broader responsibilities for the accuracy and reliability of the financial statements and the development and maintenance of appropriate internal controls in its effort to ensure that the financial information is complete and reliable. The Audit Committee of the Board of Directors, consisting of three independent directors, has reviewed this document and all other publicly reported financial information, for integrity, usefulness, reliability and consistency.*

*This discussion, which has been prepared as of April 29, 2005 at which time 92,497,001 shares are outstanding, should be read in conjunction with the unaudited consolidated financial statements for the period ended March 31, 2005 and the audited consolidated financial statements, including the notes thereto included in the Company's December 31, 2004 annual report. This discussion contains forward-looking statements that involve inherent risks and uncertainties. The Company's actual results and the results of its investees may differ materially from those anticipated in these forward-looking statements. All amounts presented in this MD&A are in accordance with Canadian GAAP and presented in thousands of Canadian dollars unless otherwise specifically noted.*

#### GENERAL

Sirit Inc. ("Sirit" or "the Company") is a Radio Frequency Identification ("RFID") company that designs, develops, manufactures and sells RFID products and solutions. For over 12 years, Sirit Technologies, Inc., the Company's wholly owned operating subsidiary, has been providing RFID products and solutions to customers based primarily in the United States and throughout the Americas, Europe and Asia. More information on the Company can be found at [www.SEDAR.com](http://www.SEDAR.com).

On March 1, 2005, Sirit and Dynasys Technologies, Inc. ([www.rfidusa.com](http://www.rfidusa.com)), a provider of RFID hardware engineering solutions and distribution services, announced a strategic partnership and alliance. Dynasys will serve as a value added integrator and distributor of Sirit's embedded OEM RFID reader offerings to service RFID upgrade and retrofit markets as well as address EPCglobal™ and "closed loop" RFID applications.

On March 2, 2005, LXE Inc. announced a collaboration with Sirit and Intel Corporation to produce the first robust, forklift-mounted RFID data collection solutions for use in warehousing and distribution. This effort will produce solutions that will enable customers to garner the benefits of RFID throughout their warehouse, beyond simple compliance.

On March 15, 2005, the Company filed three new patent applications with the U.S. Patent and Trademark Office related to UHF radio frequency identification technology; two of the patents are in the area of RFID reader architecture and the third addresses high-efficiency RFID antenna technology.

On March 29, 2005, Sirit announced the completion of a multi-year supplier agreement totaling approximately US\$12.9 (CDN \$16.0) million with the E-470 Public Highway Authority in Colorado. The agreement calls for Sirit to deliver its UHF RFID toll transponder technology over a 60 month period, the longest supply commitment ever made by a Sirit tolling customer. Sirit commenced deliveries in accordance with this agreement in the first quarter of 2005.

#### RESOURCES

##### Cash Flows, Liquidity and Capital Resources

As at March 31, 2005, Sirit's cash resources were \$9.4 million, a decrease of \$0.6 million from a cash balance of \$10.0 million at December 31, 2004. Cash was utilized to fund on-going development efforts and operations.

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There were neither significant purchases nor any commitments to purchase capital assets during the first quarter of 2005.

#### Operating Activities

In the first quarter of 2005, Sirit utilized cash to fund operating activities of \$734 compared to cash generated from operating activities in the first quarter of 2004 of \$535. Included in the first quarter 2004 operating activities is other income of \$524 comprised of \$294 from the sale of intellectual property from an investment written-off in 2001 by Sirit Technologies Inc. and \$230 from the sale of a portion of a long-term investment.

Sirit's working capital position, (which includes all current assets and current liabilities), at March 31, 2005 is \$10.8 million compared to \$11.5 million at December 31, 2004. The change in working capital was impacted primarily by the decrease in cash during the quarter. Further details regarding the fluctuations of certain amounts which comprise working capital are noted below.

The decrease in accounts receivable of \$531 from December 31, 2004 results from lower sales volumes during the quarter. The increase in accounts payable and accruals of \$462 from December 31, 2004 is associated to the timing of payroll obligations as well as the inventory costs described below.

The increase in inventory of \$623 from December 31, 2004 is the result of a temporary build-up of transponders associated with the timing of Toll tag shipments, as well as an increase in SCM inventory in anticipation of future orders.

#### Investing Activities

There was minimal cash utilized during the quarter for investing activities compared to the first quarter of 2004 when the Company generated cash from investing activities through the sale of one of its long-term investments for cash of \$335.

#### Financing Activities

Minimal financing activities occurred during the first quarter of 2005. During the first quarter of 2004, the Company closed the second tranche of its financing with J L Albright for net cash proceeds of \$5.0 million.

#### Commitments

The Company gave notice to terminate its lease in Mississauga, Ontario effective December 31, 2005. The above is the only change in commitments when compared to December 31, 2004 and the financial impact of this change is noted below.

	<b>Payments due by Period</b>				
Contractual Obligations	<b>Total</b>	<b>Up to 1 year</b>	<b>2 to 3 years</b>	<b>4 to 5 years</b>	<b>Over 5 years</b>
Premises Leases	\$ 902	\$ 225	\$ 389	\$ 288	-

#### Related Party Transactions

During the first quarter of 2005, the Company paid directors fees of \$83 for their services in the fourth quarter of 2004 and the first quarter of 2005.

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### MANAGEMENT'S DISCUSSION AND ANALYSIS

The Company paid \$21 to one of its directors for legal services and entered into a consulting contract with a second director commencing March 2005. No fees have been paid with respect to this consulting contract in the first quarter of 2005. There were no other related party transactions in the first quarter of 2005.

### RESULTS

**For the three months ended March 31, 2005 compared to the three months ended March 31, 2004**

	Three months ended March 31	
	2005	2004
Revenue	\$ 4,426	\$ 4,937
Cost of Sales	2,766	2,893
Gross margin	1,660	2,044
Expenses	2,738	2,009
Operating income/(loss)	(1,078)	35
<b>Net income/(loss)</b>	<b>(1,041)</b>	<b>\$ 590</b>
<b>Basic and diluted income/(loss) per share</b>	<b>\$ (0.01)</b>	<b>\$ 0.01</b>
<b>Total assets</b>	<b>\$ 24,345</b>	<b>\$ 23,308</b>
<b>Total long-term financial liabilities</b>	<b>\$ -</b>	<b>\$ -</b>

#### Revenue

The following highlights significant aspects of the 2005 first quarter revenue:

- Total revenue in the first quarter of 2005 decreased by approximately 10% when compared to the first quarter of 2004. The change in revenue is best understood based on the Company's two revenue generating RFID verticals.

#### AVI

Total AVI revenue was down approximately \$0.5 million when compared to the first quarter of 2004. The quarter to quarter fluctuation was principally due to the timing of two shipments of AVI products totaling \$0.4 million with terms FOB destination shipped in March but not received by the customers until April 1; hence, that revenue was recognized in Q2 rather than Q1.

- Toll solutions represented approximately 64% of total Q1 2005 revenue compared to 69% in Q1 2004. Parking and Access Control revenues were 12% of total revenues compared to 8% in Q1 2004.

#### SCM

- Revenue from SCM sales remained stable in the first quarter of 2005 when compared to the same period in 2004 at \$1.1 million. SCM sales represented 24% of Q1 2005 sales compared to 23% in Q1 2004.

#### Gross Margin

Gross Margin for the first quarter of 2005 was 37.5% compared to a 41.4% gross margin reported in the first quarter of 2004. In dollar terms, fixed overhead cost components of gross margin do not fluctuate materially on a quarter by quarter basis. These costs will reflect a greater or smaller percentage of revenue as total revenues fluctuate quarterly. This impact is reflected in the lower gross margin in the

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### MANAGEMENT'S DISCUSSION AND ANALYSIS

first quarter of 2005 when compared to the first quarter of 2004. The mix of products, primarily within AVI, has also resulted in quarterly fluctuations in margins.

#### Selling, General and Administrative Expenses

- Total SG&A expenses for Q1 2005 were \$2.0 million compared to \$1.7 million in Q1 2004. The components of first quarter 2005 SG&A expenses of compared to the same period in 2004 include:
- Salaries and benefits of \$1,102 (2004 - \$913) are higher than the prior year due to overall higher staff levels during the first quarter of 2005 compared to 2004 as well as stock compensation costs of \$159 compared to \$36 in 2004.
- The remaining SG&A expenses have remained relatively stable year over year and in 2005 include directors fees of \$83 compared to nil in the prior year.

#### Development Expenses

- Development costs were \$645 during the first quarter of 2005, an increase of \$444 from the same period in the prior year and are in-line with expectations for the remainder of 2005. Development efforts continue to be focused primarily on SCM products as the Company expects to introduce new SCM products late in the second quarter and early in the third quarter of 2005.

#### Quarterly Results

	2005 1st Q	2004 4th Q	2004 3rd Q	2004 2nd Q	2004 1st Q	2003 4th Q	2003 3rd Q	2003 2nd Q
Revenue	\$ 4,426	\$ 4,876	\$ 5,162	\$ 5,525	\$ 4,937	\$ 4,089	\$ 4,535	\$ 4,554
Net income/(loss) from continuing operations	(1,041)	(913)	(642)	1,889	590	(526)	(1,534)	(1,151)
Net income/(loss) for the period	(1,041)	(913)	(642)	1,889	590	(526)	(1,534)	(1,158)
Net income/(loss) per share, from continuing operations, basic and diluted	\$ (0.01)	\$ (0.01)	\$ (0.01)	\$ 0.02	\$ 0.01	\$ (0.01)	\$ (0.03)	\$ (0.03)
Net income/(loss) per share, basic and diluted	\$ (0.01)	\$ (0.01)	\$ (0.01)	\$ 0.02	\$ 0.01	\$ (0.01)	\$ (0.03)	\$ (0.03)

The first quarter sales were impacted by the timing of shipments of Toll transponders which were lower when compared to the first quarter of 2004. The net loss results from on-going development efforts and normal operations with a lower revenue base.

During the third and fourth quarters of 2004, the Company significantly increased its development efforts totaling \$1.3 million and was negatively impacted by foreign exchange costs of \$0.6 million.

The decline in fourth quarter revenue in both 2003 and 2004 is due to reduced sales and available shipping times over the holiday seasons in Canada and the US.

The gain on sale of one of the Company's long-term investments totaling \$2.0 million was included in the Q1 and Q2 2004 net income. Included in the Q1 2004 net income was the one-time sale of an intangible asset of \$294.

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### **MANAGEMENT'S DISCUSSION AND ANALYSIS**

Due to rapidly changing market conditions during the second half of 2003, management had changed its strategy with respect to one of its AVI applications. As a result, in Q4 2003, the Company wrote-off \$245 of deferred development costs and \$260 of deposits associated with this development effort.

Included in the 2003 third quarter net loss is \$1.3 million of internal restructuring costs. This effort resulted in termination costs associated with an overall 30% staff reduction, streamlining inventory into a single location in Carrollton, Texas, refocusing efforts in the UK to development activities with limited sales activities and centralizing head office functions in the Mississauga, Ontario location. Additional costs incurred in completing the restructuring efforts were primarily travel, moving and salary related.

The 2003 second quarter results were negatively impacted by \$276 of fees associated with the bridge financing during the private placement and over \$1.4 million of revenue from the toll integration project which carries a lower gross margin as compared to the other AVI sales.

### **SIGNIFICANT ACCOUNTING POLICIES AND MANAGEMENT ESTIMATES**

There have been no material changes to the significant accounting policies and management estimates presented in the annual report of the Company as at December 31, 2004 and the Annual Information Form dated March 22, 2005. Please refer to these reports for a detailed analysis of the significant accounting policies and estimates made by management at that time.

### **RISKS**

Sirit's management team has the responsibility for the daily evaluation and management of risk factors affecting the Company. Management's assessment of the most significant potential risks which would have the greatest impact on the Company over the ensuing 12 to 24 months given currently available information, and except as noted below have not changed significantly from those presented in the 2004 Annual Report. This analysis contains forward looking statements that may differ materially from future actual results.

#### **RFID Adoption Rate**

Sirit has been an active participant in the most prominent trade shows and conferences in the first quarter of 2005, including the RFID World and RFID Journal Live conferences. The Company viewed several key themes emerging from these conferences. First, RFID is clearly gaining greater mindshare with organizations looking to improve efficiencies within their supply chains. Second, the technology is continuing to improve, specifically with respect to tag sensitivity, a key to improving read rates, is getting better with each new generation of chip technology. Third, major organizations other than Wal-Mart and the U.S. Department of Defense are moving somewhat slower than expected in their adoption of RFID. The Company believes that while RFID will achieve the prominence expected within the supply chain, adoption rates will be somewhat slower overall than 2004 research might have indicated. Sirit is financially positioned to manage any potential slowdowns in the adoption rate or rapid technological changes that may result given its strong cash and working capital balances, as well as, the recurring revenues earned from its AVI vertical.

#### **Long-Term Investments**

Sirit currently owns three minority interest investments recorded at approximately \$5.2 million. There is a risk that these organizations will face operating or market risks not currently foreseen by local

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management. Sirit faces the risk that it will not be able to liquidate these investments and realize the reported carrying values. Sirit reviews the valuation of these investments on a regular basis.

**Sirit Inc.**  
**Interim Consolidated Balance Sheets**  
(expressed in thousands of Canadian dollars)  
Unaudited

	<b>As at March 31 2005</b>	<b>As at December 31 2004</b>
<b>Assets</b>		
<i>Current Assets</i>		
Cash and cash equivalents	\$ 9,419	\$ 10,021
Accounts receivable	2,788	3,319
Inventory	1,919	1,296
Prepays and deposits	690	716
	<u>14,816</u>	<u>15,352</u>
Long-term investments (note 2)	5,191	5,191
Property, plant and equipment, net	880	896
Intangible asset, net	522	573
Deferred development costs, net	107	123
Goodwill	2,829	2,829
	<u>\$ 24,345</u>	<u>\$ 24,964</u>
<b>Liabilities</b>		
<i>Current Liabilities</i>		
Accounts payable and accrued liabilities	\$ 3,058	\$ 2,596
Deferred revenue	736	913
Warranty obligations	195	310
	<u>3,989</u>	<u>3,819</u>
<b>Shareholders' equity</b>		
Share capital (note 3)	34,856	34,763
Contributed surplus	559	400
Deficit	(15,059)	(14,018)
	<u>20,356</u>	<u>21,145</u>
	<u>\$ 24,345</u>	<u>\$ 24,964</u>

**Commitments and guarantees (note 6)**

Approved by the Directors:

"W. W. Staudt"  
Director

" G. C. McKinnis "  
Director

See accompanying notes

**Sirit Inc.**  
**Interim Consolidated Statements of Operations**  
(expressed in thousands of Canadian dollars except per share amounts)  
Unaudited

	<b>Three Months Ended</b>	
	<b>March 31</b>	
	<b>2005</b>	<b>2004</b>
<b>Revenue</b>	\$ 4,426	\$ 4,937
Cost of Sales	2,766	2,893
<b>Gross margin</b>	<u>1,660</u>	<u>2,044</u>
<b>Expenses</b>		
Selling, general and administrative	1,983	1,683
Development	645	201
Amortization	148	131
Foreign exchange	(38)	(6)
	<u>2,738</u>	<u>2,009</u>
<b>Operating income/(loss)</b>	(1,078)	35
Gain on disposal of long-term investment (note 2)	-	230
Other income	-	294
Interest income, net	37	31
<b>Net income/(loss) for the period</b>	<u>\$ (1,041)</u>	<u>\$ 590</u>
Deficit, beginning of period	<u>(14,018)</u>	<u>(14,942)</u>
<b>Deficit, end of period</b>	<u>\$ (15,059)</u>	<u>\$ (14,352)</u>
<b>Basic and diluted income/(loss) per share</b>	<u>\$ (0.01)</u>	<u>\$ 0.01</u>

See accompanying notes

**Sirit Inc.****Interim Consolidated Statements of Cash Flows**

(expressed in thousands of Canadian dollars)

Unaudited

	<b>Three Months Ended March 31</b>	
	<b>2005</b>	<b>2004</b>
<b>Cash provided by/(used in):</b>		
<b>Operating Activities</b>		
Income/(loss) from continuing operations	\$ (1,041)	\$ 590
Items not involving cash and cash equivalents (note 5a)	307	(55)
	<u>(734)</u>	<u>535</u>
Net change in non-cash working capital items (note 5b)	104	181
	<u>(630)</u>	<u>716</u>
<b>Investing Activities</b>		
Additions to property, plant and equipment	(65)	(23)
Proceeds on sale of long-term investment	-	335
	<u>(65)</u>	<u>312</u>
<b>Financing Activities</b>		
Issuance of common shares, net of associated expenses	93	5,012
	<u>93</u>	<u>5,012</u>
<b>Exchange rate impact on cash and cash equivalents</b>	<u>-</u>	<u>(7)</u>
<b>Increase/(decrease) in cash and cash equivalents</b>	(602)	6,033
Cash and cash equivalents, beginning of period	10,021	2,604
	<u>10,021</u>	<u>2,604</u>
<b>Cash and cash equivalents, end of period</b>	<b>\$ 9,419</b>	<b>\$ 8,637</b>
<b>Cash and cash equivalents consist of:</b>		
Cash and deposit accounts with banks	\$ 2,316	\$ 2,137
Short-term commercial paper	7,103	6,500
	<u>\$ 9,419</u>	<u>\$ 8,637</u>

See accompanying notes

**Sirit Inc.****Notes to the Financial Statements (unaudited)****(expressed in thousands of Canadian Dollars except per share info)****1. BASIS OF PREPARATION**

The accompanying unaudited consolidated financial statements have been prepared in accordance with Canadian generally accepted accounting principles for interim financial statements. Accordingly, certain disclosure normally included in annual financial statements prepared in accordance with generally accepted accounting principles are not provided. These interim financial statements have been prepared based on the accounting principles consistent with those used in the annual audited consolidated financial statements and should be read in conjunction with the annual audited financial statements of the Company for the year ended December 31, 2004. The results of the operations for the interim period are not necessarily indicative of the results of operations for any other interim period or for a full fiscal year.

**2. LONG-TERM INVESTMENTS**

Investments are recorded at the lower of cost and estimated net realizable value and include:

	<b>March 31</b>	<b>December 31</b>
	<b>2005</b>	<b>2004</b>
Medsite, Inc.	\$ 3,933	\$ 3,933
Applied Data Systems, Inc.	739	739
Horizon Wimba, Inc.	519	519
	<b>\$ 5,191</b>	<b>\$ 5,191</b>

As at March 31, 2004, the Company held an investment in Loma de Niquel Holdings Ltd. for a book value of \$916. In March 2004, the ultimate parent of Loma de Niquel Holdings Ltd. distributed cash from earnings through the repurchase and cancellation of shares. The Company retained its proportionate share of its investment and reported a gain of \$230 on the sale of 2,531 shares.

**3. SHARE CAPITAL**

(a) Common shares issued and outstanding:

	<b>Shares</b>	<b>Amount</b>
<b>Balance at December 31, 2004</b>	<b>92,147,001</b>	<b>\$ 34,763</b>
Issued on exercise of stock options	100,000	93
<b>Balance at March 31, 2005</b>	<b>92,247,001</b>	<b>\$ 34,856</b>

(b) During the period January 1, 2005 to March 31, 2005, the Company granted stock options to 11 employees and an outside consultant totalling 1,238,400 common shares. The Company determined compensation costs on these options granted based on the fair value at the grant date consistent with the fair value method of accounting for stock-based compensation. Stock-based compensation expense of \$159 is included in selling, general and administrative expenses and in contributed surplus in the first quarter of 2005.

(c) Basic net income/(loss) per common share is computed by dividing net income/(loss) for the period by the weighted average number of common shares outstanding during the period. Diluted net income/(loss) per common share is computed using the treasury stock method whereby the weighted average number of common shares used in the basic net income/(loss) per common share calculation is increased to include the number of additional common shares that would have been outstanding if the dilutive potential common shares had been

**Sirit Inc.****Notes to the Financial Statements (unaudited)  
(expressed in thousands of Canadian Dollars except per share info)**

issued at the beginning of the period or at time of issuance, if later. Potential common shares are excluded from the calculation if their effect is anti-dilutive.

The following table reconciles the basic weighted average number of common shares outstanding to the diluted weighted average number of common shares outstanding:

	<b>Three months ended March 31</b>	
	<b>2005</b>	<b>2004</b>
Weighted average number of shares outstanding - basic	92,190,334	84,691,528
Dilutive effect of stock options	-	3,026,856
Dilutive effect of warrants	-	2,048,611
	<b>92,190,334</b>	<b>89,766,995</b>

At March 31, 2005, as a result of losses applicable to the common shares, the outstanding options are excluded in the diluted loss per share calculation as their inclusion would be anti-dilutive.

**4. SEGMENTED INFORMATION**

The Company and its subsidiaries operate in the technology sector in two reportable business segments. The Company's assets by business segment are as follows:

	<b>March 31</b>	<b>December 31</b>
	<b>2005</b>	<b>2004</b>
Radio Frequency Identification Business	\$ 19,154	\$ 19,773
Portfolio Investments Business	5,191	5,191
	<b>\$ 24,345</b>	<b>\$ 24,964</b>

For the three months ended March 31, the Company's revenue and expenses by reportable business segment are as follows:

	<b>2005</b>		
	<b>RFID</b>	<b>Portfolio</b>	
	<b>Business</b>	<b>Investments</b>	<b>Total</b>
Revenue	\$ 4,426	\$ -	\$ 4,426
Expenses	5,504	-	5,504
Operating (loss)	(1,078)	-	(1,078)
Interest income, net	37	-	37
<b>LOSS FOR THE PERIOD</b>	<b>\$ (1,041)</b>	<b>\$ -</b>	<b>\$ (1,041)</b>

**Sirit Inc.****Notes to the Financial Statements (unaudited)****(expressed in thousands of Canadian Dollars except per share info)**

	<b>2004</b>		
	<b>RFID Business</b>	<b>Portfolio Investments</b>	<b>Total</b>
Revenue	\$ 4,937	\$ -	\$ 4,937
Expenses	4,901	1	4,902
Operating income/(loss)	36	(1)	35
Other income	294	-	294
Gain on sale of long-term investments	-	230	230
Interest income, net	31	-	31
<b>NET INCOME FOR THE PERIOD</b>	<b>\$ 361</b>	<b>\$ 229</b>	<b>\$ 590</b>

**5. SUPPLEMENTARY DISCLOSURES RELATED TO CASH FLOWS**

(a) Items not involving cash and cash equivalents:

	<b>Three months ended March 31</b>	
	<b>2005</b>	<b>2004</b>
Amortization	\$ 148	\$ 131
(Gain) on disposal of long-term investment	-	(230)
Loss on disposal of assets	-	8
Stock compensation costs	159	36
	<b>\$ 307</b>	<b>\$ (55)</b>

(b) Non-cash and non-cash equivalent working capital:

	<b>Three months ended March 31</b>	
	<b>2005</b>	<b>2004</b>
Accounts receivable	\$ 531	\$ 1,109
Inventory	(623)	(306)
Prepays and deposits	26	(120)
Accounts payable and accrued liabilities	462	(416)
Deferred revenue	(177)	40
Warranty obligations	(115)	(126)
	<b>\$ 104</b>	<b>\$ 181</b>

**6. COMMITMENTS AND GUARANTEES**

(a) As at March 31, 2005, certain accounts receivable and inventory are pledged as security in connection with accounts payable in the amount of \$1,106 (March 31, 2004 - \$613).

(b) The Company's total leased premises commitments are summarized as follows:

**Sirit Inc.****Notes to the Financial Statements (unaudited)****(expressed in thousands of Canadian Dollars except per share info)**

	<u>Amount</u>
2005 (9 months)	\$ 225
2006	198
2007	191
2008	192
2009	96
Thereafter	-
	<u>\$ 902</u>

**7. RELATED PARTY TRANSACTIONS**

During the first quarter of 2005, the Company paid director fees of \$83 for their services, a portion of which related to services performed in 2004. The Company also paid \$21 to one of its directors for legal services.

In the first quarter of 2004, the Company entered into a 3 month consulting contract with one of its directors commencing January 2004 and ending in March 2004. The fees paid under this consulting contract during the first quarter of 2004 totalled \$30.