

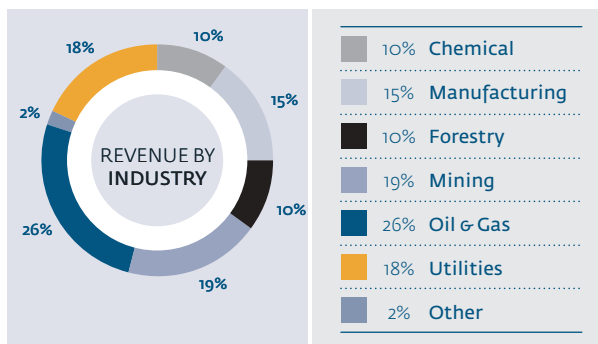
## MANAGEMENT'S DISCUSSION AND ANALYSIS

The following discussion of Matrikon's financial condition and results of operations should be read in conjunction with the consolidated financial statements and related notes for the year ended August 31, 2003. All dollar amounts in this discussion are in Canadian dollars unless otherwise specified.

### Company Overview

Matrikon is a growing international provider of industrial information technology (IT) solutions that enable plants to produce their goods more efficiently. Our solutions help clients to improve their operational performance by transforming plant data into actionable business information.

Matrikon is one of the largest process control system integrators in North America with a client base diversified across a number of vertical industries, including oil and gas, power and utilities, forestry, chemicals, mining and discrete manufacturing. With our diversified client base, no single client accounts for more than 5% of our business.



Matrikon's client base covers a variety of vertical industries.

Our products are arranged into four different suites:

### Connectivity Suite

We are the world's largest supplier of real-time industrial connectivity. Matrikon's Connectivity Suite includes a collection of over 500 drivers and related tools and serves over 30,000 users with a global install base of 100,000. Connectivity is vital to our other product suites as it enables communication between the myriad of plant data systems available on the market today.

### Process Suite

Solutions in the Process Suite include alarm management, equipment monitoring, condition-based maintenance, advanced control technologies, downtime reporting, optimization and data visualization. Process Suite solutions are designed for process industry environments where goods are produced continuously (oil and gas, chemicals and petrochemicals, utilities) and for batch industry environments where a recipe is

used to make a large quantity of material which is individually packaged for consumer consumption (pharmaceuticals, food and beverage).

### MxSuite

Solutions in the MxSuite include planning and scheduling, assembly line sequencing, plant floor monitoring and data visualization. MxSuite solutions are designed for the discrete manufacturing environment where goods are made one at a time, usually on an assembly line (automotive, equipment and component manufacturing).

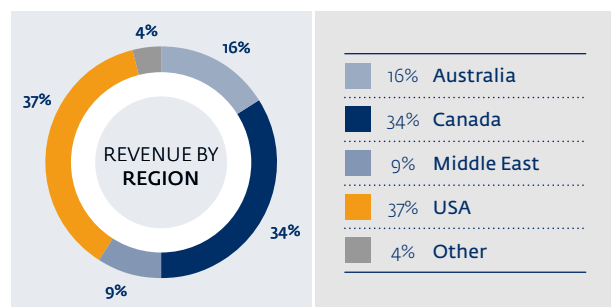
### Total-InSite

Total-InSite is a hosted solution delivered as an ASP (application service provider) to clients who do not have the infrastructure to support and maintain a solution internally. Total-InSite includes solutions from the Process Suite product line as well as applications that address industry-specific issues. Total-InSite was recently launched with an initial focus on the oil and gas industry.

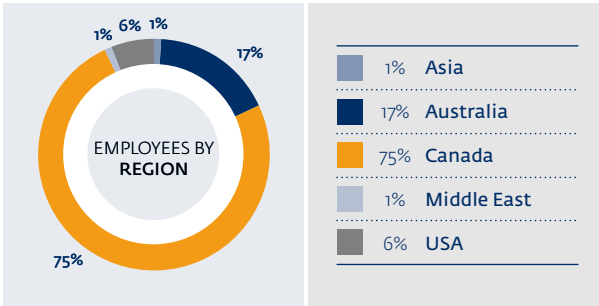
Revenue is derived from the licensing of our software, support and maintenance fees, equipment and third party software sales, and consulting and integration services, both related to our proprietary software and to third party software and hardware.

Our integration and consulting services deliver value by ensuring that the plant infrastructure is in place to achieve optimal performance, providing applications to meet specific needs through custom programming, and integrating various proprietary and third party products to create a customized solution. Our service expertise covers plant information technology services from plant design to asset management and audits of advanced control technologies.

To support our global customer base, Matrikon has 16 offices around the world, with six in Canada (including our head office in Edmonton), five in Australia, three in the United States and one each in the Middle East and Asia.



First international office opened in New York



Matrikon is listed on the Toronto Stock Exchange under the trading symbol "MTK". As at October 31, 2003 there were 28,813,165 common shares of the corporation issued and outstanding and 2,093,586 options granted.

We operate internationally, with a substantial portion of our business conducted in foreign currencies.

### Vision and Strategy

Our vision is to be one of the top 10 industrial solution firms. To achieve this vision, Matrikon has been transitioning from a system integrator (primarily integrating third party hardware and software) to a total solution provider using our proprietary technology to create high-end solutions for plant intelligence.

Management believes that the company has made significant progress in this transition as evidenced by the commercial success and continued development of our proprietary products emphasizing solutions for the total enterprise. In 2003, eight major clients signed corporate license agreements for specific Matrikon products or for entire product suites, compared to two in 2002. Global projects that comprise a solution incorporating proprietary products and professional services also continue to gain momentum. In 2003, 10 projects were worth over \$1.00 million compared to six in 2002. We believe this is the true measure of our success as the transition to total solution provider continues.

Matrikon's growth strategy focuses on four fundamentals: geographic expansion, innovative technology; complementary professional services; and vertical market diversification. These growth strategies will be achieved through both organic growth and strategic acquisitions. The following table outlines progress in fiscal year 2003 and key focus areas for 2004 and beyond.

Growth Strategy	2003 Progress	2004+ Objectives
<b>Geographic Expansion</b>	<p>Distributor program expanded. Excellent relationships established with distributors in the United Kingdom and Korea</p> <p>Sales office opened in Malaysia, additional team members deployed to the Middle East</p> <p>Acquisition of Hunter Control in September 2002 brought a notable presence in Australia and has grown from 60 to over 80 team members. Australian strength positions Matrikon for further expansion into Asia</p>	<p>Continue development of distributor program</p> <p>Europe holds great opportunity-gain market share through distributors</p> <p>Continue to expand in Australia</p>
<b>Innovative Technology and Products</b>	<p>New versions of every product in the Process Suite product line released</p> <p>Product advisory board meetings held in October 2003. Clients representing industry leaders from around the world share current and future needs</p> <p>Total-InSite for Oil and Gas, Matrikon's ASP delivered solution, was introduced. This is a new business model for Matrikon and will build a recurring revenue stream. With Total-InSite, Matrikon is able to deliver its solutions to a broader client base, including smaller producers</p> <p>The NSERC Synergy award recognized Matrikon's innovative research and development partnership with the University of Alberta</p>	<p>Ongoing product development based on industry feedback</p> <p>Develop Total-InSite solutions for additional industries</p> <p>Additional research chairs with leading industrial computing universities</p>
<b>Services and People Expertise</b>	<p>Service expertise has been constantly developed and extended - from Control and Automation when the company began, to the full range of professional services we offer today. Focus areas include enterprise resource planning integration, condition based maintenance, network management and maintenance and reliability. We acquired significant experience in maintenance and reliability through Hunter Control and plan to expand that capability in our North American operations</p>	<p>Continue to develop service expertise in asset management disciplines, such as asset monitoring, expert analysis, and automatic maintenance scheduling for condition-based maintenance.</p>
<b>Vertical Market Diversification</b>	<p>Over the past few years our focus has been on growing in the utilities, mining and discrete manufacturing industries. This focus has paid off, with 46 percent of revenue coming from these three industries in 2002 and 52 percent in 2003. Today, Matrikon is recognized as an expert in the power industry and we expect to see an increase in our revenue from this sector due to the Eastern Canada/US blackout in August of 2003</p> <p>MxPTACI, a focused, value-priced scheduling solution specifically developed to meet the needs of the plastics injection molding industry was launched</p> <p>Total-InSite released for the Oil and Gas industry</p>	<p>Continue focus on increasing presence in discrete manufacturing industries and on developing products that meet industry specific needs.</p>

Matrikon completes its first acquisition, a small system integrator in St. Louis, to establish second office in the United States.

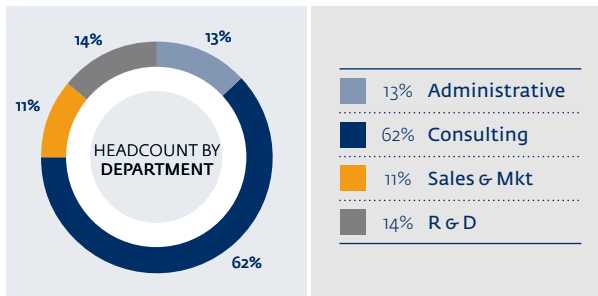
## Key Performance Drivers & Capability to Deliver Results

Several key performance drivers affect our ability to deliver value to our clients and therefore achieve our strategic vision and build long term value for our shareholders. These critical factors include our ability to attract and retain a highly skilled workforce, our ability to develop innovative products and continually increase their market share, our ability to operate efficiently and sustain growth, and our ability to attain the financial resources required to achieve our objectives.

### An exceptional team

Our people are our finest asset. They drive our ability to be successful by developing innovative technology, delivering value to our clients through our integration and consulting services, supporting our customer base, and developing long-term relationships with our clients. Matrikon recognizes that our ability to attract and retain quality people is fundamental to our success. Therefore, we emphasize the development of a sustainable corporate culture that values performance, leadership and innovation and provides exceptional opportunities for growth and career development.

Employee base growth and utilization are the primary performance measures used with respect to our workforce. Our team increased by 36% to approximately 450 staff at August 31, 2003 from 330 in 2002, with approximately half of the increase as a result of the Australia acquisition. Utilization, which measures billable time against the total available time for each employee, also improved throughout the year from 71% in September 2002 to 79% in August. Average utilization in 2003 was 76%.



Another indication of our success in shaping a sustainable corporate culture is our recognition as one of the Top 100 Employers in Canada by Maclean's magazine in both 2002 and 2003.

As we believe that 'what is measured is improved', we regularly seek the thoughts and opinions of our team members through

employee surveys in order to develop the programs they want. In 2003, 93% of survey respondents were proud to work at Matrikon.

We believe that we have the human capital in place today to achieve our objective of growing to \$100 million in revenue. The critical factor for continued growth is our ability to develop tomorrow's leaders to enable international expansion while ensuring that our culture and values are maintained. In 2003, 116 team members attended "The Art of Matrikon Leadership", a program designed to guide employees in achieving their leadership potential.

### Innovative technology

Our successful transition to a solutions company requires that we continue to develop innovative technology. Our commitment to innovation is achieved through continual research and development, award-winning collaboration with leading educational centers, and collaboration with our clients to ensure that our products meet their current and future needs.

A primary method for efficiently developing new technology is through consulting engagements. When technology is developed during a project, we maintain intellectual property rights and in many cases are encouraged to commercialize the technology to ensure future development and support. Each product that we sell today sprang out of a need that a client expressed or that we recognized through the course of consulting engagements.

Matrikon's product development is enhanced by our partnership with educational institutions. Through Matrikon sponsored research chairs, we collaborate with industrial clients and graduate students to commercialize leading edge technology.

To further ensure that our product development addresses the technology priorities of our clients, Matrikon established a Product Board of Direction for each product suite. Each advisory board is comprised of clients who have embraced our technology and meets annually to review product direction and discuss priority features and functionality. The advisory boards serve to keep our product development cycle in touch with the evolving needs of our clients. By giving our clients a voice in our technology direction, we develop an even deeper partnership with them while ensuring that our technology is heading in the right direction.

The primary measure of our success in technological innovation is the number of new product introductions and upgrades to existing products over the course of the year. In 2003, Matrikon launched four new products in the Mx and Process Suites (MxNet, MxPTACi, ProcessMORe, HistorianView), introduced Total-InSite, and developed approximately 30 drivers and related technology tools in the Connectivity Suite. We also released

Matrikon's management team decides to shift the business model to give higher priority to developing & marketing proprietary software - the beginning of our transition to a solution provider

new versions of six major products (ProcessNet, ProcessDoctor, ProcessGuard, ProcessMonitor, MxLine, MxAPS). Product development is ongoing, with new releases of major products occurring every 12 to 18 months.

### Improving operating efficiency

In order to enhance shareholder value, we must operate efficiently and thus we continually seek out ways to improve our efficiency.

The two measures used to determine operating efficiency are gross margin and factor reports. In 2003, our gross margin improved to 50% from 49% in 2002, but was on the low end of our target range of 50% to 55%. Three factors impacted gross margin for the year: Australian operations, the increased strength of the Canadian dollar relative to the United States dollar, and strong equipment and third party product sales, which carry a lower profit margin.

Australian operations significantly improved efficiency over the course of the year, from a gross margin of 28% in the first quarter to 45% in the fourth quarter. In spite of this improvement, the lower gross margin in the first part of the year reduced the combined gross margin by 4% for the year. We believe that the improvements made in the latter part of the year are sustainable.

We have reviewed our foreign currency policies and adjusted pricing to ensure that margins can be maintained going forward.

Equipment and third party sales carry a lower profit margin. They are ancillary to consulting engagements and fluctuate period by period.

The factor report is an internal measure of each group's operating efficiency and is calculated by subtracting expenses from total billings and dividing the result by payroll. The overall factor at the end of 2003 was 2.27, a 51% improvement over the start of the year when our current method of calculating factor was introduced.

Another essential element of our efficiency and our ability to sustain growth is our capability to deliver value to clients while maintaining profitability on large projects. To ensure that quality and profitability are maintained, our experienced project management team frequently performs project audits covering various aspects of the project, from budget to risk assessment to customer satisfaction to delivery of various project components. In addition, we recently implemented a confidential client survey at the conclusion of each project to ensure the delivery of value and overall client satisfaction.

As each project progresses, myMatrikon (our communication portal for employees, clients and partners) is used to keep all parties informed with instant access to progress reports, key

contacts, project documentation and other tools for enhanced collaboration.

We are currently implementing a Project Performance Indicator (PPI) to provide information on the health and profitability of each project based on financial measures.

### Sustained growth

Since 1999, Matrikon has enjoyed a compound annual growth rate of 41% for revenue and 50% for net income. Our long-term target is to sustain revenue and earnings growth at 20% to 40% per year, although we may not see growth in this range every year. Our ability to continue to grow at this rate is predicated upon several factors, the most significant current factor being the sales and marketing to support this growth target.

Over the past few years, we have increased our investment in sales and marketing activities and dramatically increased our sales team (from 35 at the end of 2002 to 50 at the end of 2003) to support our drive to increase product sales and win larger projects.

The tactical focus of the marketing team is developing collateral to support sales personnel, generating leads, generating general awareness, and developing tighter bonds within the Matrikon user community. As technology and the Internet evolve, so does Matrikon's marketing strategy. Our web site is our primary source of lead generation, and receives 80,000 user visits per month. We see the emphasis on print material decreasing and multimedia presentations increasing. Multimedia provides the ability to visually show viewers our products and services, provides better message retention and is able to quickly reach a much broader audience than traditional print media.

For example, Matrikon developed a comprehensive tutorial on OPC technology and how it is used to build a best-of-breed solution. This tutorial is available to anyone through Matrikon's web site. It is also available through the web sites of numerous trade magazines and Matrikon partners. It is quickly proliferating through industrial communities, generating both awareness of Matrikon's OPC expertise and leads for our products. Since its was made available in August, user visits to the OPC section of Matrikon's web site have doubled to 42,000 per month.

Another marketing tactic is road shows, which we use to educate existing and potential clients about specific industry issues (for example: alarm management, connectivity and

The products group is formed to handle product development and establish quality assurance mechanisms to ensure quality as well as innovation

redundancy). This provides an opportunity for Matrikon to showcase its products while achieving 'expert' status in the resolution of these issues.

Our sales strategies focus on developing the customer relationship and the 'Matrikon Experience' from initial contact to completed project. This is furthered through the Matrikon Value Partners (MVP) program, including the product and industry advisory boards and Matrikon user community conferences. Given the diversity of Matrikon's products and our professional engineering expertise, many clients are familiar with only one part of our business. The MVP program is an opportunity to further broaden our exposure within our existing client base.

The sales organization is placing greater emphasis on strategic account management to identify and close opportunities for large-scale projects and corporate license agreements within our existing customer base.

#### Financial resources

Matrikon's philosophy with respect to managing finances has always been to remain profitable and free of long-term debt. Our growth to date has been funded by internal cash flow, supplemented by a line of credit. Each month we focus on the bottom-line to ensure that costs remain in line with revenue, and that any divergence can be caught and corrected.

Matrikon raised \$10 million through a private placement subsequent to the end of the fiscal year, allowing institutional investors to obtain a larger position in the company. This cash infusion improved our financial flexibility and we are now better positioned to take advantage of accretive acquisition opportunities and otherwise fund growth initiatives. In addition, our strengthened balance sheet places us in a better position to bid on and win multi-million dollar contracts, as larger customers will have more confidence in our financial viability.

Our financial condition is healthy, with a strong balance sheet, no debt and unused capacity in our credit facilities. We believe our financial resources are sufficient to take advantage of market opportunities and do not anticipate the need to seek additional equity financing in 2004.

### Scorecard

	Target	Actual	Note
<b>Revenue Growth</b>	20%-40%	27%	Target set in Q402 earnings announcement
<b>Earnings per share</b>	0.11 – 0.15	0.11	Original target 10-30% growth (Q402 announcement)
<b>Earnings Growth</b>	57%-115%	69%	Revised target 0.11-0.15 EPS or 57%-115% growth (Q103 announcement)  Expected to achieve lower end of target due to foreign exchange impact (Q303 announcement)
<b>Software licenses and related support</b>	20-25% of revenue	24%	Original target 20% (Q402 announcement) Revised target 20-25% (Q103 announcement and 2002 annual report)
<b>International market</b>	20% of revenue	29%	2002 Annual Report
<b>Discrete industry</b>	20% of revenue	15%	2002 Annual Report. Penetration of the discrete market has been slower than anticipated. Matrikon's strategy for this area has been refocused and includes a broader emphasis (beyond planning and scheduling solutions). To this end, MxNet was recently released, as well as a focused solution for the plastics industry (MxPTACI)
<b>Gross margin</b>	50-55%	50%	Q303 earnings announcement

### Items of note in 2003

#### Acquisitions

In September 2002, Matrikon acquired Hunter Control, a system integrator and Matrikon distributor in Australia. We are pleased to report that the Australian division posted net income of \$0.58 million for fiscal year 2003, up from a loss of \$0.99 million in its fiscal year 2002.

The Australian division continues to increase efficiency, with a steady improvement in gross margin throughout the year from 28% in the first quarter to 45% in the fourth quarter. The Australian division achieved several major contract wins throughout the year, including a multi-year corporate contract for products, services and support with Santos (Australia's largest gas producer); a multi-plant, three-year corporate contract with CSR Sugar for process information management solutions; and a AUD\$1.93 million contract with BHP Billiton's Queensland Nickel facility. Based on these contracts and the improved operating efficiency, management is confident that

Office opened in Houston

2000

228 employees

2000

Australia will continue to grow in 2004 and beyond. The team in Australia has increased by 33% (to 80 employees) since September 2002.

While we expect to achieve our fiscal year 2004 growth targets through organic growth, we continue to actively seek acquisition candidates to complement our growth strategy. Of particular interest are acquisitions that will serve to fast track our geographic expansion (especially in Europe), add technology that is recognized as a leader within a specific vertical industry, and add to our employee base.

#### SR&ED credit

Matrikon's Scientific Research and Experimental Development (SR&ED) credit for the years ended August 31, 2002 and 2003 were filed and recognized in the fourth quarter, with the 2002 portion (\$0.37 million) as a credit to Other Income and the 2003 portion (\$0.48 million) as a credit to Research and Development expenses. The SR&ED credit is a tax credit offered by the Canadian government to be applied towards activities related to scientific advancement. Matrikon's SR&ED filing comprises both product development expenses and major projects where new technology is developed and Matrikon retains intellectual property rights.

#### Lawsuit

Management had been working to settle a dispute with OSISOFT, Inc., a competitor to Matrikon, for the past several months and an agreement in principle had been reached with respect to the dispute. Nonetheless, OSISOFT filed a lawsuit in the United States claiming violations of a data partner agreement and infringement of intellectual property rights.

It is management's view that the lawsuit was filed as a strategic attack in an attempt to impair Matrikon's business. Matrikon has commenced legal action against OSISOFT in Canada to confirm our legal right to continue to develop and provide interface technologies, which connect to data residing in OSISOFT's proprietary software, to our clients.

Approximately 30% of Matrikon's ProcessNet and ProcessDoctor install base accesses data from OSISOFT's historian product. That number continues to decline as the number of vendors in the historian space increases. As such, management does not believe that the lawsuit is material, but is monitoring the situation. The financial impact of defending the lawsuit may become material.

#### Canadian dollar appreciation negatively affected fiscal year results by \$0.02 per share

We operate internationally with approximately 65% of our business conducted in foreign currencies, predominantly US dollars. Accordingly, our results are affected by year-over-year

exchange rate fluctuations of various currencies relative to the Canadian dollar. The rapid rise of the Canadian dollar relative to the US dollar in the third quarter negatively affected third quarter and fiscal year results, causing a decline in fiscal year revenue of \$1.01 million, compared to a gain of \$0.24 million in fiscal year 2002. The tax-effected impact to net income for the fiscal year was \$0.61 million or \$0.02 per share.

The rapid rise of the Canadian dollar in relation to the US dollar, in combination with our typical sales cycle of three months to one year to close business, allowed little opportunity to align pricing strategies. We have now adjusted our pricing strategies to reflect the improved strength of the Canadian dollar for future contracts. In addition, currency fluctuations may affect profit margins on multi-year contracts.

It is management's belief that Matrikon's continued global expansion functions as an offset to currency fluctuations by diversifying the currencies used and thereby lessening the company's dependency on any one currency. Revenue from international business increased to 29% in 2003 from 14% in 2002 and is expected to continue to increase as we progress with our geographic expansion strategy. Approximately 16% of revenue in fiscal 2003 were in Australian dollars, which made gains compared to the Canadian dollar and helped to compensate for the weakened US dollar.

The current rise of the Canadian dollar may continue to impact results.

### Results of Operations

12 Months Ended August 31

(5 000s)	2003	%	2002	%	% Change
<b>Total Revenue</b>	47,868	100	37,576	100	27
<b>Consulting Fees</b>	32,662	68	27,780	74	18
<b>Equipment Sales</b>	3,737	8	3,372	9	11
<b>Total Service and Related</b>	<b>36,399</b>	<b>76</b>	<b>31,152</b>	<b>83</b>	<b>17</b>
<b>Software License Fees</b>	8,572	18	4,172	11	105
<b>Extended Support</b>	2,897	6	2,252	6	29
<b>Total Product and Related</b>	<b>11,469</b>	<b>24</b>	<b>6,424</b>	<b>17</b>	<b>79</b>

Matrikon's annual and quarterly results are primarily affected by the level and timing of customer orders, fluctuation in costs and the relative mix of products, services, support and equipment.

Matrikon completes the reverse takeover of TigrSoft and begins trading on the Toronto Stock Exchange

Historically, Matrikon has experienced some seasonal variation in revenue. The first quarter is typically strong, followed by a weaker second quarter due to a company-wide week-long shutdown in December. Management has noticed that as the portion of revenue from software licensing increases, second quarter results improve due to the second quarter falling at the end of the typical budget calendar for IT spending. Sales begin to pick up in the third quarter, with this increase being offset by increased hiring activity. The fourth quarter is historically Matrikon's strongest quarter. With the shifting dynamic in Matrikon's business model, we are uncertain if these trends will continue.

### Revenue growth target achieved (27%)

Matrikon achieved record revenue for fiscal year 2003. Software license fees continue to drive revenue growth, having increased by 105% in the fiscal year when compared to the equivalent period of 2002. Over the past four years, Matrikon has been transitioning from a services company to a total solutions company offering proprietary technology. This is reflected in the increasing portion of revenue from software licenses and extended support, which totaled 24% of revenue in 2003 compared to 17% of revenue in 2002. Management believes that while there is potential to grow revenue from software licenses, the transition is complete from an operational viewpoint. Product development procedures are well developed and are complemented by stringent quality assurance and customer support.

The momentum built over the course of the past year continues, with eight new corporate license agreements in fiscal 2003 compared to two in fiscal 2002. Corporate license agreements are contracts to deploy specific software at multiple sites across an enterprise.

Support revenue increased by 29% in fiscal year 2003 compared to 2002. Management expects continued growth in support revenue as software licenses continue to grow. As support revenue is divided over the year, there is a lag between increases in product licenses and the increase in support revenue.

Equipment sales, which include third party software and hardware, increased by 11% over fiscal year 2002. Equipment sales are ancillary to consulting engagements and will continue to fluctuate each period.

### Segment Revenues

Matrikon has five strategic business units: control and automation, industrial information systems (IS), advanced applications, product sales and implementation and multidisciplinary projects (see page 24 for a description of

each unit). Matrikon evaluates each business unit's performance and reports segmented information according to this structure. Revenue from product licensing and support was 24% of revenue for fiscal year 2003; revenue from implementation of Matrikon products was 21%, and consulting revenue (related to third party products or general consulting) was 55% of the total. Our long-term target is to achieve a breakdown of approximately 33% revenue from products, 33% revenue from implementation of our products, and 33% from consulting unrelated to our products.

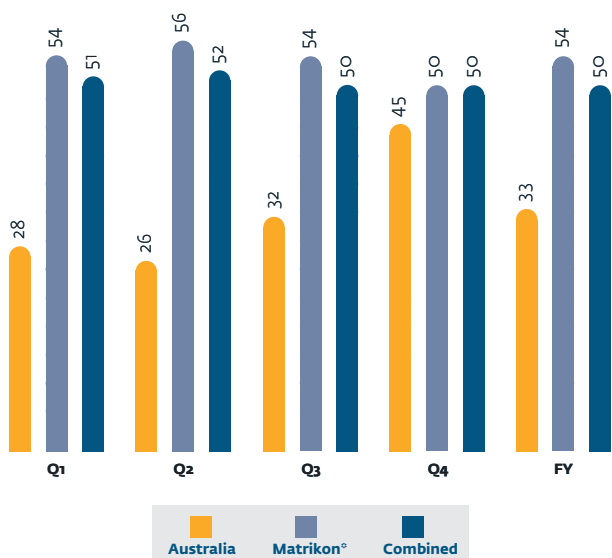
12 Months Ended August 31

(\$ 000s)	2003	2002	Change	% Change	2003 % of Revenue
<b>Control &amp; Automation</b>	10,699	8,159	2,540	31	22
<b>Industrial IS</b>	14,320	10,099	4,221	42	30
<b>Advanced Applications</b>	8,471	4,808	3,663	76	18
<b>Product Sales &amp; Implementation</b>	18,760	14,704	4,056	28	39
<b>Multidisciplinary Projects</b>	6,729	5,290	1,439	27	14
<b>Corporate &amp; Eliminations</b>	(11,111)	(5,484)	(5,627)	103	(23)
<b>Total</b>	47,868	37,576	10,292	27	100

While Control and Automation revenue increased by 31% over 2002, income before taxes decreased by 17%. This is due to the large number of competitors for this business, which results in downward pressure on rates. We expect to continue to see pressure on profit margins in this business unit. The Control and Automation service group provides a strategic advantage as work performed in this group often leads to new business for Matrikon's other service groups.

Revenue for the Multidisciplinary Projects group, which manages large projects that are a collaboration of other groups, increased by 27% while income before taxes decreased by 54%. This is not a reflection of the profitability of large projects, but rather a result of increasing use of intercompany labour resources. The Multidisciplinary Projects group uses employees from various other service groups on an as needed basis, with an hourly rate paid to the employee's permanent group (intercompany consulting revenue) and therefore transferring some of the profit to that group. In 2003, a large portion of loaned employees were members of the Advanced Applications group, which accounts for the significant increase in Advanced Applications income before taxes (306%).

## Gross Margin



\*Matrikon consolidated less Australian operations

### Gross Margin target achieved (50%)

While the Australian division has improved operating efficiencies significantly, it negatively impacted consolidated gross margin for the year. The chart above shows gross margin percentage broken down for Australia, Matrikon operations excluding Australia and the combined gross margin. Gross margin improved from 49% in fiscal year 2002 to 50% in 2003. Matrikon finished fiscal year 2003 at the lower end of its target of 50%-55% for gross margin.

In addition, the continued strength of the Canadian dollar in relation to various other currencies in which we do business and the increase in revenue from lower margin equipment sales impacted gross margin in the third and fourth quarters.

Management expects that gross margin will continue to improve as software sales increase and Australia's efficiency improvements continue.

Matrikon establishes research chair at University of Alberta. The research is then commercialized in Matrikon's ProcessDoctor and ProcessMonitor products.

## Quarterly results

The following table presents a summary of our unaudited consolidated operating results for the last eight quarters.

(\$ 000s except per share amounts)	Q1, 2002	Q2, 2002	Q3, 2002	Q4, 2002	Q1, 2003	Q2, 2003	Q3, 2003	Q4, 2003
<b>Revenue</b>	10,737	8,330	9,470	9,039	11,939	11,815	11,664	12,450
<b>Gross Profit</b>	4,950	4,262	4,949	4,412	6,052	6,094	5,851	6,170
<b>Gross Profit %</b>	46	51	52	48	51	52	50	50
<b>Net Income</b>	563	290	562	135	629	770	381	845
<b>Net Income %</b>	5	3	6	1	5	7	3	7
<b>Shares Outstanding</b>	22,735	22,738	22,742	23,722	24,210	24,209	24,215	24,224
<b>EPS - basic</b>	0.02	0.01	0.03	0.01	0.03	0.03	0.02	0.03
<b>EPS - diluted</b>	0.02	0.01	0.03	0.01	0.03	0.03	0.02	0.03

## Operating Expenses

12 Months Ended August 31

(\$ 000s)	2003	2002	Change	% Change
<b>Consulting G&amp;A</b>	7,537	5,727	1,810	32
% of Revenue	16	15	1	-
<b>Sales &amp; Marketing</b>	4,800	4,032	768	19
% of Revenue	10	11	(1)	-
<b>Research &amp; Development</b>	2,465	2,288	177	8
% of Revenue	5	6	(1)	-
<b>General &amp; Administrative</b>	4,442	3,135	1,307	42
% of Revenue	9	8	1	-
<b>Amortization</b>	1,368	1,062	306	29
% of Revenue	3	3	-	-
<b>Total Expenses</b>	20,612	16,244	4,368	27
% of Revenue	43	43	-	-

Combined operating expenses remained steady as a percentage of revenue at 43% (\$20.61 million in 2003 and \$16.24 million in 2002).

Consulting general and administrative (consulting G&A) expense represents the non-billable portion of project expenses, including all related infrastructure costs. Consulting G&A increased to 16% of revenue from 15% in 2002. For the fiscal year, general and administrative expenses increased slightly to 9% of revenue from 8% last year.

Matrikon recognizes that new product development is essential to our future growth and to our strategy for increasing profitability. Research and development costs decreased to 5% of revenue in 2003 compared to 6% of revenue in 2002. This is primarily a result of the SR&ED credit applied against fourth quarter research and development expenses (\$0.48 million). Matrikon controls R&D expenses through an efficient development process and through consulting engagements, which provide an opportunity to identify emerging industry trends and develop new technology while earning revenue. New versions of each product in the Process Suite and several products in the MxSuite were released in 2003 and product development is ongoing.

Matrikon held its first product advisory board meetings in October 2003. Through the product advisory board, major clients provide input into product technology and features to ensure that our products are aligned with the needs of our clients.

#### EPS target achieved (\$0.11)

<small>(\$ 000s except per share amounts)</small>	2003	2002	Change	% Change
<b>Net Income</b>	2,625	1,550	1,075	69
<b>% of Revenue</b>	5	4	1	-
<b>Earnings per Share</b>	0.11	0.07	0.04	57

Net income as a percentage of revenue increased to 5% for fiscal year 2003 from 4% in 2002. Management expects that profitability will continue to improve as revenue from higher margin software licenses increases.

#### Adjusted Net Income

As a private company prior to the reverse takeover of TigrSoft in 2001, Matrikon paid shareholder bonuses annually. This practice is common to private companies, however it makes it difficult to compare results with other publicly traded companies and does not provide for meaningful trend analysis. Therefore, management uses adjusted net income for the years prior to becoming a public company as a truer comparison of results to current presentation. Adjusted net income is net income plus shareholder bonuses net of related income taxes. Adjusted net income is not a measure of performance under generally accepted accounting principles (GAAP) and therefore does not have a standardized meaning prescribed by GAAP and is not necessarily comparable to similar measures presented by other companies. The following table reconciles net income to adjusted net income.

<small>(\$ 000s)</small>	1999	2000	2001	2002	2003
<b>GAAP Net income (loss)</b>	513	(449)	952	1,550	2,625
<b>Shareholder bonus</b>	1,025	1,805	700	-	-
<b>Income tax effect of above</b>	410	722	280	-	-
<b>Adjusted Net Income</b>	1,128	634	1,372	1,550	2,625

#### Liquidity and Capital Resources

At August 31, 2003, accounts receivable were \$13.90 million compared to \$11.67 million at August 31, 2002. Fiscal year 2003 includes accounts receivable of \$2.16 million for the Australian operations, which are not included in 2002 as the acquisition was completed on September 5, 2002. The average collection period at August 31, 2003 was 97 days compared to 89 days as at August 31, 2002. This increase is in part a result of increased international business, which typically has longer payment cycles. Matrikon's client base consists primarily of Fortune 500 companies with strong credit ratings; hence bad debt expense has been minimal at less than 0.5% per annum.

Current liabilities, excluding bank indebtedness, increased from \$6.19 million at August 31, 2002 to \$8.51 million at August 31, 2003. The increase in current liabilities includes an increase in commission accruals, which corresponds to the increase in revenues over fiscal 2002, and a general increase in trade accounts payable associated with the general increase in our business activity. In addition, the future income tax asset relating to the Canadian losses acquired with TigrSoft in 2001 has been fully utilized, therefore remaining Canadian tax timing differences result in a future tax liability on the financial statements.

Cash provided by operating activities was \$2.94 million for fiscal year 2003, up from a deficit of \$2.12 million in fiscal year 2002.

Matrikon has a \$7.00 million operating line of credit at a variable interest rate of the bank's prime plus 25 basis points. At August 31, 2003, Matrikon had \$nil outstanding on the line of credit, compared to bank indebtedness of \$2.27 million at August 31, 2002. Except as disclosed in Note 13 to the consolidated financial statements, Matrikon is not party to any other agreements that would give rise to material obligations, nor is Matrikon liable for any material undisclosed or off balance sheet obligations.

Matrikon had cash on hand of \$0.30 million at August 31, 2003 compared to \$0.29 million at August 31, 2002.

Small financing (\$1.9 million) allows a major fund to invest in company

On September 24, 2003, (subsequent to the end of the fourth quarter) Matrikon completed a private placement for 4,545,455 common shares to a group of institutional investors at a price of \$2.20 for net proceeds of approximately \$9.40 million. The net proceeds will be used to fund growth and to enable Matrikon to consider investments or acquisitions that complement our growth strategies. Management believes that the financial resources of the company are sufficient to carry out growth strategies.

(\$ 000s)	31-Aug-03	31-Aug-02	Change	% Change
<b>Cash</b>	295	285	10	4
<b>Accounts Receivable</b>	13,897	11,674	2,223	19
<b>Average Collection Period</b>	97 days	89 days	8 days	
<b>Contracts in Progress</b>	3,457	2,909	548	19
<b>Bank Indebtedness</b>	-	2,273	(2,273)	-
<b>Other Current Liabilities</b>	8,512	6,186	2,326	38

#### Normal Course Issuer Bid – no shares repurchased to date

Matrikon announced a normal course issuer bid on June 6, 2003. Under the bid, the Matrikon may acquire up to 1,211,215 common shares, representing 4% of the then issued and outstanding common shares of the Company. The bid commenced June 9, 2003 and will end June 8, 2004. No shares have been repurchased under the bid to date.

#### Outlook & fiscal year 2004 targets

Matrikon is committed to sustainable long-term growth. Although discretionary IT spending has been weak for some time, Matrikon has been successful at winning projects of increasing size and value and has increased the number of corporate license agreements for its proprietary products. Management believes that the company is positioned to continue to grow. Based on current contracts underway and assuming Matrikon's ability to win new business and enter into corporate license agreements continues at the current pace and other factors remain favorable, we expect to achieve the following:

- revenue growth of 20% to 40%
- earnings growth of 20% to 40%
- 25-30% revenue from software license fees and related support
- 50-55% gross margin

Due to the various risks associated with the numerous factors that may affect actual results, Matrikon discloses a target range and provides refinement to the targets as the year progresses.

We expect to see growth in revenue from the oil and gas, utility and forestry industries and a slight weakness in mining based on various industry events and economic cycles.

#### Accounting policies

Our discussion and analysis of Matrikon's financial condition and the results of operations is based on our consolidated financial statements, which have been prepared in accordance with accounting principles generally accepted in Canada. In preparing the consolidated financial statements, management is required to make estimates and assumptions that may affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities at the date of the financial statements, and the revenues and expenses reported during the reporting period presented. These estimates and judgments are evaluated on an on-going basis and we consider them to be reasonable based on our historical experience and assumptions. Actual results could differ from those estimates made by management.

Matrikon's critical accounting policies are those it believes are the most important in determining our financial position or results or require significant judgment by management. These accounting policies are summarized in the notes to our consolidated financial statements.

#### Revenue Recognition

Matrikon's revenue is earned from four primary sources: Software license fees received for the sale of proprietary software, Consulting fees related to developing solutions for our clients or installation services related to both Matrikon and third-party software, Equipment sales of third party products that are ancillary to consulting engagements, and Extended support contract fees relating to post implementation support services. In addition to complying with the standards set by the Canadian Institute of Chartered Accountants (CICA) for revenue recognition, Matrikon adheres to Statement of Position (SOP) 97-2, *Software Revenue Recognition* as released by the American Institute of Certified Public Accountants (AICPA).

First industry advisory board meeting held with representatives from 9 major clients

In accordance with SOP 97-2, software license revenues are recognized when the following conditions are met:

- 1) persuasive evidence of an agreement exists (such as the customer's execution of a software license agreement and the receipt of a purchase order)
- 2) delivery has occurred (when software is shipped or on receipt of customer acceptance in cases where we have a vendor obligation, such as customization or modification of the software)
- 3) the fee is fixed or determinable (as agreed upon in the software license agreement or purchase order)
- 4) collectability is probable (Matrikon reviews the customer's credit where no historical relationship exists)

Revenue from implementation, support or training activity is recognized as the services are delivered. Consulting services are recognized on the percentage-of-completion basis. Contracts in progress are recorded at the lower of cost and normal profit earned and their estimated realizable value based on the percentage-of-completion method. Losses are provided for in the period when they become apparent. Extended support revenues are deferred and recognized on a straight-line basis over the term of the maintenance period, which is usually one year.

When revenue is derived from several of the sources described above, revenue is recognized based upon the fair value of each element as determined by vendor specific objective evidence (VSOE). VSOE represents the fees charged for each element if sold individually. Where the elements within the arrangement can be separately delivered, revenue is recognized for each element in the same manner as a single element agreement. Where the functionality of the elements are inter-dependant upon each other or the total price of the arrangement is not dependant upon the inclusion or exclusion of an element, the entire arrangement is accounted for using the percentage completion method.

Global project with BOC elevates Matrikon's capability and leverages global offices for implementation

### Research and Development

Matrikon's research and development costs relate principally to enhancing and upgrading our proprietary software products to better serve our end-user's needs. As the research and development costs incurred relate to products that release updates every 12 to 18 months, the benefit of these costs is realized in less than one and a half years. Therefore research and development costs are generally expensed as incurred. However, management does review the criteria for deferring development costs under Canadian generally accepted accounting principles regularly and development costs that meet these criteria are capitalized and amortized over their useful life.

Scientific Research and Experimental Development (SR&ED) tax credits receivable in relation to these costs are recorded using the cost reduction method whereby the tax savings are recorded as a reduction to R&D expenses. Changes to the estimated quantity of tax credits receivable from prior periods are recorded as Other Income or Other Expenses.

### Intangible Assets and Goodwill

Matrikon accounts for intangible assets and goodwill in accordance with CICA Handbook Sections 1581, Business Combinations and 3062, Goodwill and Other Intangible Assets. Intangible assets acquired both individually or with a group of other assets are initially recognized and measured at cost. The cost of a group of intangible assets acquired in a transaction, including those acquired in a business combination that meet the specified criteria for recognition apart from goodwill, is allocated to the individual assets acquired based on their relative fair values. The cost incurred to enhance the service potential of an intangible asset is capitalized as a betterment; costs incurred in the maintenance of the service potential of an intangible asset are expensed as incurred. Intangible assets with finite lives are amortized over their useful lives.

Goodwill is the residual amount that results when the purchase price of an acquired business exceeds the sum of the amounts allocated to the assets acquired, less liabilities assumed, based on their fair values. Goodwill is allocated as of the date of the business combination to the Corporation's reporting units that are expected to benefit from the synergies of the business combination. Subsequent to September 1, 2001, Matrikon no longer amortizes goodwill but now tests the balance for impairment annually, or more frequently if events or changes in circumstances indicate that the asset might be impaired.

### Stock Based Compensation

On September 1, 2002 Matrikon adopted the new Recommendations of the CICA with respect to accounting for stock based compensation and other stock based payments. The new Recommendations were applied prospectively to all stock based payments to non-employees, and to employee awards that are direct awards of stock, call for settlement in cash and other assets, or are stock appreciation rights that call for settlement by the issuance of equity instruments, granted on or after September 1, 2002. Compensation expense for these stock based payments, including Matrikon's Employee Stock Ownership Program, is calculated using the fair value based method. Under the fair value based method, compensation cost attributable to employees that are direct awards of stock, or stock appreciation rights that call for settlement by the issuance of equity instruments, is measured at fair value at the grant date and recognized over the vesting period. For awards that vest at the end of the period, compensation cost is recognized on a straight-line basis. No compensation cost is currently recorded for all other stock based employee compensation awards, which are accounted for using the intrinsic value based method.

Accordingly, when the Corporation awards stock options to employees, no compensation cost is recognized in the consolidated statement of income and retained earnings for common share options granted. Consideration paid by employees on the exercise of stock options is recorded as share capital. The Corporation discloses the pro forma effect of accounting for these awards under the fair value based method in the notes to the consolidated financial statements. In September 2003, the Accounting Standards Board of the CICA amended the requirements for recording stock based compensation, which now require the fair value method to be applied to all stock based compensation. The amendment applies to fiscal years starting after January 1, 2004. As our fiscal year 2004 starts prior to this date, Matrikon will implement the requirement for recording stock based compensation in fiscal year 2005 using retroactive application.

### Risks related to our business

The following internal and external risks may affect Matrikon's operations. Management continually monitors and evaluates these risk factors and takes action to minimize them.

#### Market Demand for Products and Services

There is no guarantee that our products will remain competitive, nor that they will respond to market demands, developments or new industry standards. If we are unable to identify a shift in market demand quickly enough, we may not be able to develop products to meet those new demands, or bring them to market in a timely manner.

*This risk is mitigated through the ongoing commitment to research and development and to constantly improving the products based on industry feedback. Matrikon recently held its inaugural Product Advisory Board meetings where clients from a variety of industries met with the company in a day long planning and strategy session to discuss industry needs in context of Matrikon's existing products and future demand.*

*In addition, Matrikon's service units continually provide insight into the business problems and trends occurring in a variety of industries. To date, Matrikon's products and enhancements have been developed through this insight and a continual feedback loop between industry, our services-based groups and product development teams.*

#### State of the Economy

Operating results may vary significantly based on the impact of changes in global economic conditions on customers.

*Although the current economic environment is uncertain, Matrikon has not observed a change in its sales cycle or ability to win new business in any region. While client needs change based on the economic climate, Matrikon's products and services are currently able to meet those needs. In a growing economy, Matrikon's clients' demand increased throughput and focus on optimization technology. During a recession, the focus shifts to improving efficiencies, reducing costs, and optimizing maintenance and operations. Matrikon's diversification in terms of geography, industrial sectors, and its lack of dependence on any one customer also helps to mitigate this risk.*

#### Exchange Rates

Matrikon operates internationally; accordingly, all contracts outside of Canada are in various local currencies, the largest of which is the United States Dollar.

*Matrikon enters forward contracts to partially hedge exposure to currency fluctuations between the United States (US) and Canadian dollars. Approximately 45% of the company's revenues are received in US dollars while 65% of the expenses are in Canadian dollars.*

*Following the recent, rapid decline of the US dollar relative to the Canadian dollar, Matrikon reviewed its forward contracts policy and adjusted its pricing. Matrikon believes that its practices are sufficient for potential sustained strength in the Canadian dollar, although the company recognizes that this risk cannot be fully mitigated when exchange rates fluctuate very rapidly.*

330 employees

#### **Ability to Retain and Attract Qualified Employees and Contain Payroll Expenses**

Executive management, senior technical personnel and other key personnel are essential to the business. The loss of the services of any of these persons could have a material adverse effect on the business. As a growing company, our ability to develop, market and support our products and deliver services could be harmed if Matrikon is not able to recruit and retain qualified personnel. In addition, due to the service nature of the company, payroll is a significant component of costs.

*To mitigate these risks, Matrikon offers competitive compensation packages, unique and challenging career opportunities and maintains close ties with academic institutions that train specialists in the fields in which it operates. The corporate culture supports diversity, creativity, and equality and values integrity and innovation. In addition to providing a challenging and rewarding work environment, Matrikon's social activities and corporate culture foster creativity and teamwork. Matrikon was named one of the Top 100 Employers in Canada in 2002 and 2003.*

*There has been no turnover at the senior management level since the inception of the company, and very little within the next level of management.*

#### **Availability of Credit Line and Future Financing**

The company may require additional funds through public or private financing, strategic relationships or other arrangements to meet future growth objectives. There can be no assurance that it will be able to obtain additional funding on favorable terms, if at all. If Matrikon cannot raise funds on acceptable terms, if and when needed, we may not be able to develop or enhance products and services, expand the business, acquire complementary businesses or technologies, respond to competitive pressures or unanticipated requirements, or take advantage of future opportunities, which could have a material adverse effect on our business.

*Matrikon recently completed a \$10 million private placement which, coupled with our existing line of credit of \$7 million, we believe is sufficient to meet our growth objectives for the next few years and will enable the company to take advantage of opportunities for strategic acquisitions. The private placement significantly strengthened the company's balance sheet and cash position.*

#### **Research and Development**

If Matrikon does not respond effectively and on a timely basis to rapid technological change, its products and services may become obsolete and customer loss could result.

The markets for Matrikon's products are characterized by:

- rapid and significant technological change;
- frequent new product introductions and enhancements;
- changing customer demands; and
- evolving industry standards.

*To mitigate this risk, Matrikon is committed to research and development to ensure our continued technological leadership position. In addition to internal research and development, Matrikon sponsors the NSERC-Matrikon-ASRA Industrial Research Chair in Computer Process Control at the University of Alberta with a mandate of developing an Industrial Decision Support System.*

*Other strategies for minimizing this risk include Matrikon's Industry and Product Advisory Boards, which serve to alert the company to changes in our clients' technological direction, and membership and active involvement with industry standards organizations, which enables the company to ensure that our products comply with industry standards and helps to identify new trends.*

#### **Lengthy Sales Cycle**

The lengthy sales cycle required to close larger projects makes it difficult to predict quarterly revenue levels and operating results. The sales process for larger projects and solutions can be lengthy and can exceed one year. Moreover, to the extent that Matrikon succeeds in shifting customer purchases toward corporate license agreements and larger solutions, the sales cycle may lengthen, which could increase the likelihood of delays and cause the effect of a delay to become more pronounced. The company has limited experience in forecasting the timing of sales of our integrated software and services solutions. Delays in sales could cause shortfalls in our revenues and operating results for any particular period.

*Matrikon has been focused on building the sales and marketing infrastructure to support the transition to a products company. This includes sales success workshops and hiring senior sales personnel. Biweekly sales meetings also serve as a platform for sharing experiences amongst sales staff and providing an opportunity to learn from each individual's successes and failures.*

### Legal Claims

Intellectual property claims and other claims against the company could be time consuming and costly to defend. If we are unsuccessful, our ability to use intellectual property in the future could be limited or we may have to pay damages.

*Matrikon has established policies that require all staff to comply with intellectual property laws. License agreements are obtained and staff is periodically reminded of their duty to observe these licenses.*

Our license agreements with clients typically contain provisions designed to limit exposure to potential liability claims. In our agreements for the provision of services, we also try to negotiate limitations on liability. Despite this, it is possible that such provisions may not be effective as a result of existing or future laws or unfavorable judicial decisions. We have not received to date any product liability claims nor claims regarding services. A successful liability claim could result in significant monetary liability and could seriously disrupt our business.

*We seek to minimize the risk of liability claims through a thorough quality assurance process, continual development of our products, and staff training. Further, we continually monitor changes to laws and the results of court cases, and strive to keep our agreements up to date to mitigate any claims.*

### Failure to Integrate Operations

If Matrikon fails to integrate the operations of the companies it acquires, it may not realize the anticipated benefits and operating costs could increase. Matrikon continues to pursue strategic acquisitions that will provide complementary products, services and technologies. The identification and pursuit of these acquisition opportunities and the integration of acquired personnel, products, technologies and businesses require a significant amount of management time and skill. There can be no assurance that:

- suitable acquisition candidates can be identified
- any acquisition will be consummated on acceptable terms
- Matrikon will be able to successfully integrate any acquired business into its operations.

Acquisitions also expose Matrikon to potential risks, including diversion of management's attention, failure to retain key acquired personnel, assumption of legal or other liabilities and contingencies, and the amortization of acquired intangible assets. Moreover, customer dissatisfaction with, or problems caused by, the performance of any acquired products or technologies could hurt Matrikon's reputation.

*These risks are mitigated through a thorough due diligence process, which includes measuring a potential acquisition against Matrikon's growth strategy, interviewing key personnel and reviewing the cultural fit, reviewing the financial, legal, and market aspects, talking to a sample of clients from the customer base and, in some cases, conducting character investigations for the company principals.*

### Failure to Address Challenges of International Operations

Business may suffer if there is a failure to address the challenges associated with international operations. Approximately 66% of total revenues were from customers outside of Canada in the past fiscal year. It is expected that revenues from customers outside Canada will continue to account for a significant portion of total revenues for the foreseeable future. Operations outside Canada are subject to additional risks, including:

- unexpected changes in regulatory requirements, exchange rates, tariffs and other barriers
- political and economic instability
- difficulties in staffing and managing foreign subsidiary operation
- difficulties and delays in translating products and product documentation into foreign languages
- difficulties and delays in negotiating software licenses compliant with Canadian accounting revenue recognition requirements
- potentially adverse tax consequences

*To mitigate these risks, Matrikon fully researches the business and economic environment of a country before beginning business in the country. In countries with which Matrikon is unfamiliar, an agent familiar with the region will act on behalf of Matrikon through the tender and negotiation process.*

*In addition, Matrikon's culturally diverse employee base has enabled it to offer product training to clients in numerous languages*

Acquisition of Hunter Control provides Matrikon with significant bench strength in Australia and positions the company for expansion into Asia