

**INTERNATIONAL BARRIER TECHNOLOGY INC.**  
**YEAR END REPORT**  
for the year ended June 30, 2008

**Management Discussion & Analysis**

**Date of Report – October 14, 2008**

**Description of Business**

International Barrier Technology Inc. (Barrier) manufactures and sells fire-rated building materials primarily in the United States. Barrier has a patented fire protective material (Pyrotite™) that is applied to building materials to greatly improve their respective fire resistant properties. Coated wood panel products are sold to builders through building product distribution companies all over the United States. Many of the top multifamily homebuilders in the United States utilize Barrier's fire-rated structural panel Blazeguard® in areas where the building code requires the use of a fire-rated building panel.

**Discussion of Operations**

Barrier's financial statements are filed with both the SEC (USA) and SEDAR (Canada) and are disclosed in US dollars utilizing US generally accepted accounting principles. Barrier's filings with the SEC consist of quarterly reviewed financial statements on Form 10-Q and annual audited financial statements on Form 10-K. Barrier continues to file the above financial statements with SEDAR in Canada.

**Sales** revenue reported for the fiscal year ending June 30, 2008 was \$4,877,605. Total sales volume, as measured by surface volume of product shipped, was 7,222,500 sq.ft. During the same period in the previous year, Barrier shipped 8,908,100 sq.ft. with sales revenue of \$6,130,226.

The loss of sales volume, year to year, is attributed to the substantial decline in US residential housing starts. Barrier sold 1,517,300 sq. ft. to residential markets in FY2008, only 44 percent of what was shipped in the previous year; representing a decline in sales volume to this market of 1,950,600 sq.ft. All other markets experienced increases in sales volume.

Sales into the Commercial Modular Sector grew by four percent to 5,637,000 sq.ft., up from last year's total of 5,421,500 sq.ft. The remainder of the current fiscal sales volume, 68,200 sq.ft. was shipped into the SIPs (structural insulated panel) market. This was an increase of 49,400 sq.ft. over the 18,700 sq.ft. shipped into this market in 2007.

Barrier continues to expand the geographic base for Blazeguard sales in the US. Barrier and is actively marketing Blazeguard to the multi-family residential roof deck market in Southern California and in Texas. Barrier's wholesale building products distributor in California has invested in Blazeguard inventory and expects to see increased sales to builders and lumber dealers in the coming months.

In August 2008, Blazeguard® was added to the short list of the California State Fire Marshall's Office (CSFM) approved products for high risk wildfire zones. Blazeguard® is listed as an approved exterior sheathing for roof and wall applications; a "limited ignition" material; and, for use in soffit areas under eaves. Barrier is currently marketing this fact to local architects, building code officials, and builders in the area. The initial response has encouraged Barrier to believe that as the housing economy improves in California, Blazeguard® sales there to residential markets could exceed any other area previously targeted.

Barrier believes that recent success in introducing Blazeguard into other market applications (such as commercial modular), and other emerging geographical locations for multi-family residential, have served to lower risk by spreading sales over a broader market playing field and making the business less vulnerable to cyclicity in any one region or product application. The broadening of the geographic markets served will help Barrier withstand periodic cyclicity in one market by focusing efforts and providing sales opportunities to others.

As the US building industry continues its recovery throughout Calendar 2008, and as housing starts continue their climb back to levels reflecting the underlying need for new homes, Barrier anticipates a significant recovery in the growth rate of Blazeguard residential sales volume. Barrier continues its press to add builders, one by one. During "slow times", Barrier, and the existing Blazeguard distribution network, have found builders eager to learn about how Blazeguard can improve the value of their homes. Barrier's aggressive positioning during this time period has created future opportunity and set the stage for strong growth as the housing market improves.

**Gross profit** for the Fiscal 2008 was \$339,086 down from \$829,020 in the previous year. There was a classification change during the current and prior year to include amortization and R&D in cost of sales. Therefore, the reclassified gross margin, as a percentage of sales revenue was 7% year-to-date in comparison to 13.5% in the prior year.

For historical comparison purposes, and as previously reported, the gross margin less the non-cash items of amortization and R&D was 17.8%, down from the 23.2% reported in 2007. Lower volumes of production contributed to the lower gross margins as fixed costs are spread over a smaller volume of product.

The "new" production line became "fully" operational in October 2007, nearly mid-way through the fiscal year. While the "old" line continues to produce odd size orders and plywood (warped boards), all other Blazeguard® production is run on the new line. The new line is proving out that expected gains in efficiency and quality are possible at speeds over twice as fast as the old line. As sales volumes increase to levels where the new line is allowed to produce over full weeks, efficiency gains will be noticeable on the bottom line as profits improve substantially.

**Cost of sales** decreased to \$4,538,519 from \$5,301,206 in Fiscal 2007. Reduced production volumes have impacted the cost of sales directly. As mentioned previously, the cost of sales was reclassified to include amortization and R&D expenses in this reporting period. After reclassification, the average cost per sq.ft. of production year to date was \$0.63 in comparison to \$0.60 in the year prior. For historical comparison purposes and as previously reported, in 2007 net of amortization and R&D the average cost of production was \$0.53 (\$0.56 in 2008).

R&D expenses which were incurred as new market applications continue to be explored and developed were \$144,181 vs. \$219,319 in Fiscal 2007. Barrier continues to invest in R&D to potentially develop other markets for Pyrotite™ and Blazeguard® products for future diversification, while keeping the expenses as low as possible. Directly applying Pyrotite™ to foam insulation is quickly proving to be a viable opportunity for Fiscal 2009 and a significant amount of R&D expenses incurred in 2008 was in support of that endeavor.

Included in cost of sales was amortization on plant and equipment. Amortization increased slightly from \$246,847 in 2007 to \$260,335 in 2008. The expense reflects scheduled depreciation of the new manufacturing line equipment and building expansion. The amortization of the worldwide Pyrotite technology (including patents, technical know-how, and trademarks) began when Barrier purchased it in 2004 and will continue at existing rates until it is fully depreciated (eight years). Neither of these items have an impact on the cash position of the Company.

**Administrative expenses** for Fiscal 2008 decreased from \$1,378,896 to \$1,199,715. The administrative costs per sq. ft. increased slightly for the reporting period, from \$0.16 to \$0.17. As volumes continue to increase, a reduction in the average cost of administrative expense per sq.ft. produced is expected. Barrier expects the reduction in the average cost of administration to have a significant impact on bottom line performance in future reporting periods.

Barrier is required to report a line item entitled “stock-based compensation”. This figure is an estimate of the value of stock options awarded to management and key personnel as a portion of their total compensation package (see section: Critical Accounting Estimates below). The Company uses the Black-Scholes formula to calculate the fair value of the stock options. While this reporting is a requirement, and a true reflection of value the company is granting to key personnel, it is a “non-cash” item that does not affect current operating cash flows. Stock-based compensation for Fiscal 2008 was \$47,329, in contrast to \$113,681 during the previous year.

**Accounting and Audit Fees** are substantially lower year to date (\$45,331 in 2008 vs. \$91,582 in 2007). This is attributed to moving several tasks “in-house” and the completion of a tax-filing project that occurred in 2007 to capture loss/carry forward amounts for future filings.

**Consulting Fees** increased to \$19,934 this year in comparison to \$3,428 in 2007. In June 2008, Barrier enlisted the services of the George May International Consulting Group to evaluate management practices and existing accountability requirements within the operating facility in Watkins. As a result, the organizational structure has been modified, and an entire layer of management removed. Barrier anticipates that the improved communications and accountability requirements also implemented will allow this change to occur without negatively impacting management effectiveness.

Fiscal 2008 **insurance costs** have decreased to \$125,974 in comparison to \$130,873 last year. The difference is due to slightly lower premiums due to lower volume of sales.

**Interest on Long Term Obligations** has increased from \$52,870 to \$82,109 for the reporting period. This increase is a result of utilizing an operating line of credit that has enabled Barrier to grow inventory levels to anticipate customer needs and to provide interim funding for short term capital requirements.

In July 2008, the line of credit was modified to include \$500,000 of capital debt which is being amortized at the bank over a 10-year period. This debt for capital is being secured by the building, property, and equipment in the building. An additional \$500,000 of credit was provided by the bank as an “operating” line of credit, secured by inventory, receivables, and cash. The current amount of debt on the operating line is \$250,000.

**Legal fees** declined significantly to \$64,024 for Fiscal 2008. For Fiscal 2007, legal fees were \$109,359. Legal fees were expended on activities in support of Blazeguard and Pyrotite patent and trademark registration activities for New Zealand and Australia. Legal fees were also incurred for Barriers registration of the trade name MycoGuard™ and Firepatch™ Kit. Barrier believes protecting its technology and trademarks is an important step in positioning itself to develop strategic partners and potential technology licensees.

**Sales, marketing, and investor relations** expenses are considerably lower at \$68,909 vs. \$171,753, in comparison to the prior year. Sales expenses are expected to grow during Fiscal 2009 with the development of Texas, Kansas City, and the southern California territories. Barrier will also continue to expand upon its shareholder and customer communication programs to ensure the public is informed about business development and emerging opportunities as they arise.

**Other income** includes income not directly related to business operations. Other items reported herein include \$21,152 in interest income vs. \$33,968 in prior year and a gain of \$31,127 in foreign exchange vs. \$24,885 in prior year.

**Net income (loss)**

A net loss of (\$808,350) is being reported for Fiscal 2008, whereas in fiscal 2007, a net loss of (\$491,023) was reported. Barrier will continue its efforts to cut costs wherever it can to help offset the decline in sales volume during this steep retraction in residential construction. Keeping a vigilant handle on costs will help keep operational losses as low as possible and enable recovery to occur sooner and at lower volumes than previously possible.

It is important to note that even with these significant reported losses, the company experienced a negative cash flow for the year ended June 30, 2008 of only (\$79,654). It is difficult for any small-cap company to withstand long periods of financial losses; sooner or later, the money required to operate may simply run out. However, the Company has continued to sustain operations through some very difficult economic times without having to experience any significant curtailment in capacity or loss of market share. There is urgency in addressing the negative financial statement opportunity at Barrier and Barrier’s management team and Board of Directors are actively addressing these issues. Barrier is confident that the company will remain solvent and move into profitable territory very soon.

**Summary of Quarterly Results.** The following is a summary of the Company's financial results for the eight most recently completed quarters:

	June 30 2008	March 31 2008	Dec 31 2007	Sept 30 2007	June 30 2007	March 31 2007	Dec 31 2006	Sept 30 2006
Volume shipped (MSF)	1891	1,893	1,555	1,883	2,273	1,643	2,252	2,692
Total Revenues (000)	\$1,349	\$1,214	\$1,065	\$1,249	\$1,434	\$1,068	\$1,643	\$1,985
Operating Income (000)	(\$143)	(\$208)	(\$271)	(\$239)	(\$44)	(\$204)	(\$181)	(\$127)
Net income (loss) (000)	(\$134)	(\$224)	(\$258)	(\$193)	\$12	(\$191)	(\$205)	(\$107)
EPS (Loss) Per Share	(\$0.01)	(\$0.01)	(\$0.01)	(\$0.00)	\$0.00	(\$0.01)	(\$0.01)	(\$0.00)

### **Selected Annual Information**

The following financial data is for the three most recent years ended June 30:

	<u>2008</u>	<u>2007</u>	<u>2006</u>
Total Revenue	\$4,878.0	\$6,130.0	\$6,604.4
Net income (loss)	(808.0)	(491.0)	(211.7)
Per share	(0.03)	(0.02)	(0.01)
Per share, fully diluted	(0.03)	(0.02)	(0.01)
Total assets	5,738.0	5,887.9	6,172.2
Total long-term financial liabilities	1,212.3	819.4	630.0
Cash dividends declared per share	Nil	Nil	Nil

### **New product and market development**

Barrier continues to invest time and financial resources in an effort to accelerate long and near term growth. While these expenditures take away from near term profits, research and development of new products and applications as well as market development for existing products and applications are crucial to the attainment of strategic objectives and business alliances. Barrier intends to grow the business to levels far beyond those currently attained and new initiatives in products and markets are necessary if these long term goals are to be achieved. Ongoing initiatives continue to provide opportunities for sales expansion and growth.

Barrier, in collaboration with MuleHide Products, continues to experience success in supply both Class A and C rated roof assemblies in commercial modular roof decks for buildings destined for military use on domestic military bases. A "new" Underwriters Laboratories (UL) listing allows a FR C board to be utilized under an alternate single-ply membrane (FPEM) while achieving a Class A system rating. This system significantly reduces the cost of the structure and Barrier and MuleHide believe this system has a great future in commercial modular sales.

In support of the strength requirements for fire and strength rated walls, Barrier completed an extensive testing protocol performed by Progressive engineering, Inc. (PEI), an ICS certified independent testing, certification, and listing laboratory. The results demonstrate Blazeguard's ability to improve lateral load capability (shear strength for earthquake zones) and include new span and load ratings for both roof and wall applications (allowable vertical load for snow and wind load requirements).

Blazeguard treatment has always been known to increase the strength of the substrate panel, now these strength improvements are certified in a way that will improve an architect's ability to reach required designed loads in a variety of applications without having to use thicker panels to improve strength.

Barrier has been working with a major insulative foam producer in an attempt to develop a fire rated foam product that can be used both in the finishing of basement walls as well as in "built-up" commercial roof decks. While it is still early in the R&D phase, Barrier and the foam producer has developed samples and have scheduled to fire test them in October 2008.

Barrier improved certain elements of the old production line in the current quarter in an effort to produce structural insulated panels (SIPs) with a more consistent surface appearance. SIPs were a significant business for Blazeguard from 1996–1999. Variability in the surface appearance of the coating, however, created repeatable issues and complaints when the panels were used as an exposed interior wall surface, especially in residential applications. The improvements completed will help to improve the consistency of Blazeguard panels used in SIPs and make them more appealing and marketable to SIPs customers.

#### **Global licensing opportunities**

Barrier continues to solicit opportunities for licensing arrangements wherever in the world that opportunity exists. When interested parties inquire regarding licensing, Barrier responds with an information packet and begins an assessment of appropriateness of fit with our technology. Barrier believes that expansion of production capacity to meet the increased demand for Blazeguard in particular geographies or in particular market applications may be best served by cooperating with a partner company in the targeted industry when a new production facility is built. Barrier is exploring both joint venture and licensing scenarios as plans for future growth are discussed.

Any licensing agreements will be designed to protect the technology, prohibit competition, and provide for royalties to be paid to Barrier on an ongoing basis.

Product and technology licensing scenarios are being developed within Barrier and management is confident that licensing relationships or relationships leading to licensing contracts will be in existence in the near future.

#### **Financial position & financings**

Barrier ended the period with a working capital surplus of \$432,882.

The Company generated negative operating cash flow for the fiscal year ended June 30, 2008 of (\$79,654) from \$76,746 for the fiscal year ended June 30, 2007. The net cash outflow from operating activities for the current fiscal year ended was primarily a result of a net loss of \$(808,350), an increase in accounts receivable of \$109,486 and reduction of finished goods in inventory and an increase in accounts payable of \$217,885. The Company expects to fund short-term cash needs out of current operations and supplement other short-term needs with the operating line of credit that is secured by current working capital.

Investing activities resulted in a net cash outflow of \$434,095 in this year compared to a net cash outflow of \$463,853 in prior year. The Company incurred a significant amount of \$420,145 in manufacturing equipment. The Company does not expect any additional long-term capital needs in the near future as they recently expanded the operations with a more efficient automated process that is projected to fulfill future growth needs. The new automation was funded largely by a private placement coupled with operating cash flows.

Financing activities resulted in a net cash inflow of \$392,859 in the current year compared to a net cash inflow of \$200,804 for the same period last year. The increase in cash inflow in financing activities was primarily from obtaining more debt financing and no repayment of debt.

There is no assurance that we will operate profitably or will generate positive cash flow in the future. In addition, our operating results in the future may be subject to significant fluctuations due to many factors not within our control, such as the unpredictability of when customers will order products, the size of customers' orders, the demand for our products, the level of competition or general economic conditions.

Although management believes that revenues will increase, management also expects an increase in operating costs. Consequently, the Company expects to incur operating losses and negative cash flow until our products gain market acceptance sufficient to generate a commercially viable and sustainable level of sales, and/or additional products are developed and commercially released and sales of such products made so that we are operating in a profitable manner.

The Auditors' Report on the June 30, 2008 consolidated financial statements includes an additional comment that states that there exists substantial doubt about the Company's ability to continue as a going concern. The financial statements do not include any adjustments as a result of this uncertainty.

#### **Related Party Transactions**

During the twelve months ended June 30, 2008 the Company incurred wages and management fees of \$180,504 with directors of the Company and companies with common directors. The Company paid \$177,419 wages and management fees for the same prior year ended.

#### **Capitalization**

Authorized: 100,000,000 common shares without par value.

Issued as of June 30, 2008: 29,414,925 common shares at \$15,079,071

Issued as of October 14, 2008: 29,414,925 common shares at \$15,079,071

Options outstanding:

On January 10, 2008, the Company granted 740,000 share purchase options entitling the holders thereof the right to purchase one common share for each option held at \$0.45 per share up to January 10, 2010. Included in this stock purchase option grant are 522,500 options which vested immediately and the remaining 217,500 options which vest equally on July 10, 2008, January 10, 2009 and July 10, 2009.

At June 30, 2008, the Company has granted directors, officers and consultants the option to purchase 2,107,550 common shares of the Company.

The following summarizes information about the stock options outstanding at June 30, 2008 reflected in US dollar currency:

<u>Number</u>	<u>Exercise Price</u>	<u>Expiry Date</u>
40,000	\$0.38	March 6, 2009
1,077,550	\$0.65	August 24, 2009
740,000	\$0.45	January 10, 2010
<u>250,000</u>	<u>\$0.55</u>	<u>August 9, 2010</u>
<u>2,107,550</u>		

### **Critical Accounting Estimates**

#### **Stock-based Compensation Charge and Expense**

As described in Note 2 to the audited annual financial statements dated June 30, 2008, the Company accounts for all stock-based payments and awards under the fair value based method. This fair value of the stock options is estimated at the date the stock options are granted using the Black-Scholes option-pricing model. Stock-based payments to non-employees is periodically re-measured until counter-party performance is complete and any change is recognized over the life of the award. The Company accounts for share purchase options to employees by recording the fair value of the awards on the grant date and the related stock-based compensation expense is recognized over the period in which the options vest. In addition, this is a non-cash compensation charge and the cash flow effects are realized only at the time of exercise.

#### **Internal Control and Financial Reporting Procedures**

The board of directors evaluates and maintains internal control procedures and financial reporting procedures to ensure the safeguarding of Barrier's assets as well as to ensure full, true, accurate and timely disclosure of Barrier's financial position for the fiscal period ended June 30, 2008, which would materially affect the accuracy of this financial report.

There has been no change in internal control procedures in the twelve month period ending June 30, 2008.

### Other Matters

As at June 30, 2008 and 2007, the Company did not have any off-balance sheet arrangements to report.

International Barrier Technology Inc. (the Company) has received a preliminary liability and damage report from a New Jersey townhouse association in connection with a lawsuit the association has filed against its contractor, engineering consultant, property manager and the Company (the “Defendants”). The lawsuit involves alleged water damage in a 1997/1998 roof replacement project that was allegedly caused by claimed Company product failure along with other alleged deficiencies. The Company first reported on the prospect of this litigation in December 2005. The townhouse association claims that as a result of defective product supplied, and negligent work performed by other named Defendants, the association has suffered damages of US\$5,506,409.46. Repairs, to date, have been limited to certain townhouse units where water stains have appeared in ceiling areas. The damages claimed include the costs of repairs made subsequent to the initial installation work, attorney and consultant fees, and the estimated anticipated future costs for roof repairs on all units including those that have not previously required roof repairs nor have shown any sign of damage.

The Defendants, through their insurers, have engaged qualified experts to consider the report and to prepare a response to refute it. The townhouse association’s request for mediation resulted in the scheduling of a “non-binding” mediation hearing held on May 15, 2007. Counsel for Barrier and the plaintiffs failed to negotiate a resolution during this mediation hearing. The parties continue to negotiate settlement terms but if the parties cannot agree to a settlement, the suit may go to court. The Company carries \$1 million of product liability insurance, including the cost of attorney’s fees, to protect itself against such claims and has documented that any damage occurring to date was the result of insufficient ventilation and incorrect installation. The Company anticipates that the claim will have no material financial impact on the Company.

The lawsuit by the townhouse association is the first involving the Company in 17 years of product distribution in the United States. Over that time, millions of square feet of the Company’s products have been successfully installed for roofing and other applications.

The Company will report further on this matter as developments occur.