



Interim Financial Report  
**2007 Third Fiscal Quarter**  
ended August 31, 2007

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# MANAGEMENT'S DISCUSSION AND ANALYSIS

for the three and nine months ended August 31, 2007

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## **OSI Geospatial Inc.**

Management's Discussion and Analysis  
For the three and nine months ended August 31, 2007  
(expressed in U.S. dollars)

### **MANAGEMENT'S DISCUSSION AND ANALYSIS** of Financial Condition and Results of Operations

The following discussion and analysis provides a review of activities, results of operations, and financial condition of OSI Geospatial Inc. for the three and nine months ended August 31, 2007 in comparison with those for the nine months ended August 31, 2006. The following discussion should be read in conjunction with our unaudited interim consolidated financial statements prepared in accordance with generally accepted accounting principles in Canada ("Canadian GAAP"), including the notes thereto, for the three and nine months ended August 31, 2007, and the audited annual consolidated financial statements for the year ended November 30, 2006 prepared in accordance United States generally accepted accounting principles ("U.S. GAAP"). These previously released financial statements include a reconciliation to Canadian GAAP in Note 21. The following discussion should also be read in conjunction with Management's Discussion and Analysis prepared for the year ended November 30, 2006.

Effective March 1, 2006, we adopted the U.S. dollar as our reporting currency. All references in this report to financial information concerning OSI Geospatial Inc. are in accordance with Canadian GAAP and all dollar amounts are in U.S. dollars unless otherwise indicated.

Beginning in the first quarter of fiscal 2006, we have changed our financial reporting segments in order to reflect changes in management's analysis of our business. Our consolidated revenue categories have changed to marine systems, land and air systems, and mapping and our reportable segments are now U.S. Systems Operations, International Systems Operations, Mapping Operations, and Corporate and Public Company costs. On April 12, 2006 at the Company's annual general meeting, its shareholders voted in favor of changing the Company's name from Offshore Systems International Ltd. to OSI Geospatial Inc. The name change was effective June 5, 2006. For the purposes of this report, the Company is referred to by its new legal identity.

This report contains forward-looking statements within the meaning of securities laws including Section 27a of the Securities Act of 1933, as amended, and Section 21e of the Securities Exchange Act of 1934, as amended, including statements regarding the future achievement of corporate objectives, advancement of additional project interests, analysis and development of acquisition opportunities, various project interests and other matters. These statements are neither promises nor guarantees, but involve known and unknown risks and uncertainties that may cause our actual results, levels of activity, performance or achievements to be materially different from any future results, levels of activity, performance or achievements expressed in or implied by these forward-looking statements. These risks include risks related to the effects of general economic conditions, changing foreign exchange rates, actions by government authorities, uncertainties associated with contract negotiations, and industry supply, as well as other factors discussed below and those risks which are discussed under the heading "Risks and Uncertainties". Readers should not place undue reliance on any such forward-looking statements, which speak only as of the date they were made. We disclaim any obligation to publicly update or revise any such statements to reflect any change in our expectations or in events, conditions or circumstances on which any such statements may be based, or that may affect the likelihood that actual results will differ from those set forth in the forward-looking statements, except as required by law.

ECPINS and COP-IDS are registered trademarks of Offshore Systems Ltd., an OSI Geospatial company. Other company brand, product and service names are for identification purposes only and may be either trademarks, service marks or registered trademarks of their respective owners. Data is subject to change without notice.

Additional information relating to OSI Geospatial, including our Annual Information Form and our Form 20-F report is filed on SEDAR at [www.sedar.com](http://www.sedar.com), on EDGAR at [www.sec.gov](http://www.sec.gov), and is also available on the company's investor web site at [www.osigeospatial.com](http://www.osigeospatial.com).

This management's discussion and analysis is dated October 10, 2007.

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### **Overview**

Founded in 1977 and headquartered in Ottawa, Ontario, Canada, the Company designs, develops and markets the proprietary ECPINS® line of electronic chart navigation systems for commercial and military customers. ECPINS® helps to reduce the risk of navigation-related incidents by giving bridge crews a precise, real-time display of their position, course and speed, against a background of fixed obstacles and other navigational hazards. The Company has developed a strong market position in military navigation, and has ECPINS® systems deployed with the Canadian and United States Coast Guards, the Canadian Navy, the Royal New Zealand Navy, the Royal Danish Navy, the Royal Australian Navy, the Royal Navy of the United Kingdom and the United States Navy.

The Company's growth strategy is built on four fronts – diversifying its technology, partnering with the best, building on its customer relationships and completing acquisitions complimentary to its existing lines of business.

In diversifying its technology, the Company will lever its market and technology position as a leader in the naval surface and subsurface navigation market to access adjacent markets. Building on its ECPINS® line of electronic chart navigation systems for commercial and military customers, the Company has expanded into the Command & Control (C2) and homeland security markets through the development of applications like the Common Operational Picture product line (COP-PL), Warship Automatic Identification System (W-AIS) and the C2 product line C3CORE. Also, the Company has expanded its product offerings in the commercial market with the introduction of its simplified voyage data recorder (S-VDR) product, the integrated ECPINS®/S-VDR 5000 system.

The Company continues to partner with the best using its technology dominance in the military navigation market to gain entry into major defence programs. We currently have partnering agreements with Terma A/S in Denmark, Lockheed Martin in the U.S. and the U.K. and, Raytheon, L3 Communications, General Dynamics and Northrop Grumman in the U.S.

The Company continues to build on its current customer base by leveraging the strong customer relationships it has developed through the successful execution of major projects. We have existing customers in the military agencies of Canada, U.S., European NATO and other allies of Canada, and national and international commercial marine transportation companies.

The Company has completed acquisitions complimentary to its existing businesses to gain access to key markets, build critical mass and expand its products and markets. In April 2005, the Company completed the acquisition of all the outstanding shares of Mapcon Mapping Consultants Inc. (Mapcon) of Salt Lake City, Utah for \$1.1 million. Mapcon is a land mapping company in the U.S. geomatics (digital map and electronic chart data production) market. In December 2005, the Company completed the acquisition of CHI Systems Inc., a United States defence contracting company for \$9 million. CHI has three offices in the United States, is a supplier of technology and services to the U.S. Department of Defence and key defence prime contractors. CHI has developed C2, training simulation and cognitive agent applications to support its customers in multiple U.S. military agencies. In April 2007, the Company through its subsidiary CHI Systems Inc., acquired the assets of Liddy International Inc. ("Liddy"), a United States defense contracting company and established Layered Security Solutions ("LSS"). LSS provides business continuity solutions against all hazards and is qualified to develop deterrence, response and recovery strategies designed to deal with global threats to business and government.

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### SELECTED DATA

The following tables contain financial information that is derived from the unaudited interim consolidated financial statements for the nine months ended August 31, 2007.

<b>Operations:</b>	<b>For the nine months ended August 31</b>	
	<b>2007</b>	<b>2006</b>
In thousands of U.S. dollars except share related data		
	<b>\$</b>	<b>\$</b>
Revenue	17,050	14,119
Gross profit	6,172	5,192
Gross profit percentage	36%	37%
Net loss	(2,076)	(1,853)
Net loss attributable to common shareholders	(2,628)	(2,642)
Loss per share – basic and diluted	(0.07)	(0.08)
Weighted average common shares outstanding – basic and diluted	39,635,112	32,160,508

Our quarterly and year-to-date results are primarily influenced by the level, timing, and duration of customer orders, and customer product delivery requirements. We depend heavily on government contracts and derive a significant amount of revenue from a few customers, which may result in varying revenue, gross profit, and earnings. Some of our government customers have cyclical purchasing patterns which can also impact our quarterly and year-to date results.

The slightly lower gross profit percentage for the nine months ended August 31, 2007 as compared to the nine months ended August 31, 2006 is largely due to the mix of revenue. There was less software revenue and more systems and services revenue in the nine months ended August 31, 2007 than in the nine months ended August 31, 2006.

Fluctuations in gross profit are influenced by the proportion of engineering labor, third-party systems or third-party labor or portions of all three required for a project, and a high proportion of these factors can result in increased cost of sales and therefore lower gross profit. Certain contracts awarded may require the inclusion of engineering labor, third-party systems or third-party labor. In order to maintain competitiveness on these contracts, we may elect to reduce our usual margins on the third-party components. In addition, the product mix of services revenue, software, mapping, and systems and systems components in any given period may impact the gross profit for the period.

<b>Financial Position:</b>	<b>At August 31, 2007</b>	<b>At November 30, 2006</b>
In thousands of U.S. dollars		
	<b>\$</b>	<b>\$</b>
Working capital <sup>(1)</sup>	8,205	7,789
Current assets	12,775	14,333
Total assets	23,542	24,345
Current liabilities	4,570	6,544
Long term liabilities	425	20
Total liabilities	4,995	6,564
Shareholders' equity	18,547	17,781

(1) Working capital is defined as current assets less current liabilities. Working capital does not have a standardized meaning or comparable measure under generally accepted accounting principles and may not be comparable to similar measures presented by other companies.

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Dividends declared per share In U.S. dollars	In nine months ended August 31,	
	2007	2006
	\$	\$
Common shares	-	-
Class A preference shares	-	-
Class B preference shares – series 1	-	-
Class B preference shares – series 2	1.64	1.59

**RESULTS OF OPERATIONS – Three and nine months ended August 31, 2007 as compared to three and nine months ended August 31, 2006**

**Overall Performance**

Three months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Net earnings (loss) before income taxes	\$ 332	\$ (913)	\$ 1,245
Net earnings (loss)	\$ 279	\$ (709)	\$ 988
Net earnings (loss) attributable to common shareholders	\$ 109	\$ (972)	\$ 1,081
Earnings (loss) per share – basic and diluted	0.00	(0.03)	0.03
Nine months ended August 31			
In thousands of U.S. dollars			
Net loss before income taxes	\$ (2,032)	\$ (2,058)	\$ 26
Net loss	\$ (2,076)	\$ (1,853)	\$ (223)
Net loss attributable to common shareholders	\$ (2,628)	\$ (2,642)	\$ 14
Loss per share – basic and diluted	(0.07)	(0.08)	0.00

The net loss reported in the nine months ended August 31, 2007 was largely driven by lower revenues and the mix of contracts executed in the period and higher operating expenses due to the addition of costs from our acquired operations, product launch activities, and an increase in staff to support our growth plans.

**Backlog**

Total backlog is the sum of the firm and option backlogs. As at August 31, 2007 total backlog was \$70.2 million compared to \$35.2 million at August 31, 2006.

Firm backlog consists of firm, fixed, or signed orders issued and executable subsequent to the balance sheet date. Firm backlog as at August 31, 2007 was at \$45.9 million compared to \$14.9 million at August 31, 2006. Of the \$45.9 million firm backlog, \$30.1 million is expected to be executed in fiscal 2009 and beyond.

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Option backlog consists of unexercised contract options at the balance sheet date and indefinite-quantity contracts executable subsequent to the balance sheet date. Option backlog as at August 31, 2007 was at \$24.3 million compared to \$20.3 million at August 31, 2006.

There is no guarantee or certainty that our customers will elect to exercise their contract option backlog. Should our customers elect to exercise contract options or place orders against indefinite-quantity contracts, the option backlog converts to firm backlog, which then may convert to revenue as contract execution occurs. Backlog metrics are non-GAAP measures. These measures do not have a standardized meaning or comparable GAAP measure and are likely not comparable to similar measures presented by other companies.

The timing of major contracts awarded can significantly impact our total backlog position and revenue. Historically, major contracts awarded have taken up to three years to finalize. The contracting process involves lengthy discussions and negotiations with several groups of people within the prospective customer's organization. We have continually pursued, and will continue to pursue, major contracts with lengthy sales cycles, and as a result, there could be large variations in our total backlog and revenue from quarter to quarter.

Multi-year contracts with government agencies have a termination-for-convenience clause because governments approve budget expenditures on an annual basis. This allows contracts to be terminated by the contracting government agency should future budget funding not be approved. Historically, the termination-for-convenience clause has not been exercised by any of our customers. We have included the full value of these government contracts in total backlog.

### Revenue

Three months ended August 31	2007	% of total revenue	2006	% of total revenue	2007 to 2006
In thousands of U.S. dollars					
Marine systems	\$ 3,124	42%	\$ 1,240	29%	\$ 1,884
Land and air systems	2,627	36%	2,022	47%	605
Mapping	1,591	22%	1,054	24%	537
	<u>\$ 7,342</u>	100%	<u>\$ 4,316</u>	100%	<u>\$ 3,026</u>

  

Nine months ended August 31	2007	% of total revenue	2006	% of total revenue	2007 to 2006
In thousands of U.S. dollars					
Marine systems	\$ 6,267	37%	\$ 4,958	35%	\$ 1,309
Land and air systems	7,294	43%	6,244	44%	1,050
Mapping	3,489	20%	2,917	21%	572
	<u>\$ 17,050</u>	100%	<u>\$ 14,119</u>	100%	<u>\$ 2,931</u>

Our core revenue stream is derived from three sources: marine systems, land and air systems, and mapping. Our land and air systems through our U.S. Systems operations delivered 43% of our revenue for the nine months ended August 31, 2007. Our principal developed and manufactured product, ECPINS®, delivers the majority of the marine systems revenue. We also derive revenue from the delivery of the ECPINS® software component of our system product. Combined, ECPINS® systems and software delivered 24% of revenue in the nine months ended August 31, 2007.

Our results are primarily affected by the level, timing, and duration of customer orders and customer product delivery requirements. The main customers for our products and services in the nine months

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ended August 31, 2007 were the U.S. Army, the Royal Navy of the U.K., the Defense Threat Reduction Agency, the Defense Advanced Research Projects Agency, the Royal Australian Navy and the U.S. Navy. Revenue from these customers accounted for 58% of the consolidated revenue.

The main customers for our products and services for the nine months ended August 31, 2006 were the U.S. Navy's Naval Aviation, U.S. Army, the Canadian Navy, and the Royal Australian Navy through Nautronix Ltd. Revenue from these customers accounted for 70% of the consolidated revenue.

### Revenue by Segment

Three months ended August 31	2007	% of total revenue	2006	% of total revenue	2007 to 2006
In thousands of U.S. dollars					
International Systems operations	\$ 2,390	32%	\$ 1,240	29%	\$ 1,150
U.S. Systems operations	3,361	46%	2,022	47%	1,339
Mapping operations	1,591	22%	1,054	24%	537
	<u>\$ 7,342</u>	<u>100%</u>	<u>\$ 4,316</u>	<u>100%</u>	<u>\$ 3,026</u>

  

Nine months ended August 31	2007	% of total revenue	2006	% of total revenue	2007 to 2006
In thousands of U.S. dollars					
International Systems operations	\$ 5,533	33%	4,958	35%	575
U.S. Systems operations	8,028	47%	6,244	44%	1,784
Mapping operations	3,489	20%	2,917	21%	572
	<u>\$ 17,050</u>	<u>100%</u>	<u>14,119</u>	<u>100%</u>	<u>2,931</u>

Revenue from the International Systems operations for the three months ended August 31, 2007 increased 93% and for the nine months ended August 31, 2007 increased 12% due to the growth in the business, timing of new contracts awarded, the delivery schedules of existing contracts and the mix of products and services delivered.

Revenue from the U.S. Systems operations for the three months ended August 31, 2007 increased by 66% and for the nine months ended August 31, 2007 increased 29% over the same period from the prior year. The increase is due to the acquisition of the Layered Security Solutions business unit as well as general growth in the segment. For the three months ended August 31, 2006, delays in the approval of the U.S. federal budget negatively impacted revenue.

Revenue from our Mapping operations for the three and nine months ended August 31, 2007 as compared to the nine months ended August 31, 2006 increased 51% and 20% respectively. This is consistent with the increased business volume and the nature and timing of mapping contracts.

We continue to invest significant corporate, sales, and marketing resources in identifying and pursuing new opportunities and contracts, both in our existing customer base and with new prospective customers.

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**Gross Profit**

Three months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Gross profit	\$ 3,048	\$ 1,403	\$ 1,645
Gross profit percentage	42%	33%	9%
Nine months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Gross profit	\$ 6,172	\$ 5,192	\$ 980
Gross profit percentage	36%	37%	(1%)

Gross profit increased by 117% in the three months ended August 31, 2007 compared to the three months ended August 31, 2006 and the gross profit percentage was 9 percentage points higher period-over-period. This was due to higher margin systems and software sales. Gross profit decreased 1% in the nine months ended August 31, 2007. The reduced gross profit percentage compared to the prior fiscal year is due to the mix of contracts in the period.

**Gross Profit by Segment**

Three months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
<b>Gross profit:</b>			
International Systems operations	\$ 1,331	\$ 719	\$ 612
U.S. Systems operations	1,127	472	655
Mapping operations	590	212	378
Consolidated operations	\$ 3,048	\$ 1,403	\$ 1,645
<b>Gross profit percentage:</b>			
International Systems operations	56%	57%	(1)%
U.S. Systems operations	34%	23%	11%
Mapping operations	37%	20%	17%
Consolidated operations	42%	33%	9%
Nine months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
<b>Gross profit:</b>			
International Systems operations	\$ 2,915	\$ 3,012	\$ (97)
U.S. Systems operations	2,092	1,439	653
Mapping operations	1,165	741	424
Consolidated operations	\$ 6,172	\$ 5,192	\$ 980
<b>Gross profit percentage:</b>			
International Systems operations	53%	61%	(8)%
U.S. Systems operations	26%	23%	3%
Mapping operations	33%	25%	8%
Consolidated operations	36%	37%	(1)%

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Gross profit from the International Systems operations increased \$612,000 and gross profit percentage was 1% higher for the three months ended August 31, 2007 when compared to the three months ended August 31, 2006. Gross profit decreased \$97,000 and gross profit percentage decreased 8% for the nine months ended August 31, 2007. The changes are the result of higher revenues in the International Systems operations and slightly lower margins on projects that generated revenue during the three months ended August 31, 2007 when compared to the three months ended August 31, 2006.

Gross profit from the U.S. Systems operations increased \$655,000 and gross profit percentage was 11% higher for the three months ended August 31, 2007 when compared to the three months ended August 31, 2006. Gross profit increased \$653,000 and gross profit percentage increased 3% for the nine months ended August 31, 2007. This increase in the three and nine months ended August 31, 2007 compared to the three and nine months ended August 31, 2006 is the result of over \$700,000 in higher margin marine navigation revenue to U.S. customers during for the period.

Gross profit from the Mapping operations for the three months ended August 31, 2007 increased \$378,000 compared to the same in the prior year. Gross profit percentage increased 17% period over period, consistent with the mix and timing of contracts in the business unit, and in particular, due to lower subcontractor work utilized in the period. Gross profit from the Mapping operations for the nine months ended August 31, 2007 increased \$424,000 compared to the same period in the prior year. Gross profit percentage increased 8%. Again, this is consistent with the mix of contracts for the period.

### Operating Expenses

Three months ended August 31	2007	% of total revenue	2006	% of total revenue	2007 to 2006
In thousands of U.S. dollars					
General and administrative	\$ 1,451	20%	\$ 1,460	34%	\$ (9)
Engineering	231	3%	389	9%	(158)
Sales and marketing	755	10%	510	12%	245
Nine months ended August 31	2007	% of total revenue	2006	% of total revenue	2007 to 2006
In thousands of U.S. dollars					
General and administrative	\$ 4,249	25%	\$ 4,320	31%	\$ (71)
Engineering	1,101	6%	1,382	10%	(281)
Sales and marketing	2,252	13%	1,668	12%	584

**General and administrative** ("G&A") expenses consist mainly of salaries and benefits of management and administrative personnel, professional fees, public company expenses, related facility costs, and other general administrative expenses.

G&A decreased slightly for three months ended August 31, 2007 and also for the nine months ended August 31, 2007, compared to the same periods in the prior year. There was little change in G&A staffing levels and costs between the two periods.

**Engineering** expenses consist mainly of salaries and benefits of software and hardware engineering personnel, sub-contractor costs, facilities expenses, and related expenses. The company expenses research and development-related costs in the period incurred unless, in the opinion of management, certain develop costs meet the deferral criteria under Canadian GAAP, in which case development

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expenditures are capitalized and amortized over the estimated lives of the related projects. To date, the Company has not capitalized any development costs.

Engineering costs decreased by 6% for the three months ended August 31, 2007, compared to the three months ended August 31, 2006, and by 4% for the nine months ended August 31, 2007, compared to the nine months ended August 31, 2006. The decreases are related to engineering staff and related costs charged to cost of sales to support specific customer orders during the periods. We believe that in order to maintain our technological leadership, we must continue to develop existing products and introduce innovative new products that challenge and redefine the industry standards.

**Sales and marketing** ("S&M") expenses consist primarily of compensation of sales and marketing personnel, as well as expenses associated with advertising, trade shows, facilities, and other expenses related to the sales and marketing of our products and services.

S&M expenses increased by 48% and 35% for the three and nine months ended August 31, 2007 compared to the three and nine months ended August 31, 2006. The increases in S&M expenses are primarily due to additional sales and marketing emphasis. We believe our current level of S&M staff continues to allow us to pursue business development activities relating to our expansion efforts targeting new and existing customers in the military agencies of Canada, the U.S., European NATO, and other allies of Canada, and national and international commercial marine transportation companies. To increase our profile and our products, and to broaden our customer base in international markets, we have established marketing agreements with companies local to the targeted regions. Some of these activities will not result in closing orders during the current year but may yield orders in subsequent fiscal years.

### Depreciation and Amortization

Three months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Depreciation and amortization	\$ 129	\$ 191	\$ (62)
Nine months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Depreciation and amortization	\$ 377	\$ 580	\$ (203)

Total depreciation and amortization decreased by 32% and 35% on the three and nine months ended August 31, 2007 as compared to the three and nine months ended August 31, 2006. For the three months ended August 31, 2007 and 2006, a portion of the depreciation, \$54,000 and \$49,000 respectively, was included in cost of sales for equipment used in revenue-generating activities.

### Interest expense

Three months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Interest expense	\$ 22	\$ 3	\$ 19
Nine months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Interest expense	\$ 48	\$ 15	\$ 33

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Interest expense increased \$19,000 in the three months ended August 31, 2007 as compared to the three months ended August 31, 2006. Interest expense increased \$33,000 in the nine months ended August 31, 2007 as compared to the nine months ended August 31, 2006. The Company increased its utilization of its credit facility during the three and nine months ended August 31, 2007. Additionally, there was also an increase in the interest rates in the period.

### Interest income

Three months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Interest income	\$ -	\$ -	\$ -
Nine months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Interest income	\$ 7	\$ 20	\$ (13)

Interest income was nil in the three months ended August 31, 2007 and 2006. Interest income decreased \$13,000 in the nine months ended August 31, 2007 as compared to the nine months ended August 31, 2006 as the Company did not have surplus funds to invest.

### Foreign Exchange

Three months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Foreign exchange loss (gain)	\$ 43	\$ (18)	\$ (61)
Nine months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Foreign exchange loss (gain)	\$ 65	\$ (18)	\$ (83)

Foreign exchange gain and loss is largely the result of exchange rate movements of the Australian dollar and the UK pound which were not in the Company's favour during the nine months ended August 31, 2007 as compared to August 31, 2006.

### Technology Partnerships Canada

Three months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Royalty	\$ 139	\$ 55	\$ 84
Contribution	-	(227)	(227)
Nine months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Royalty	\$ 276	\$ 220	\$ 56
Contribution	-	(731)	(731)

As part of the agreement entered into on November 15, 1999 with TPC, we are required to pay a royalty of 3% on annual gross revenue in our subsidiary Offshore Systems Ltd. for the period December 1, 1999 to November 30, 2008. In addition, as part of the agreement entered into on April 26, 2004, we are required to pay a royalty of 1.4% on annual gross revenue in our subsidiary Offshore Systems for the

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period January 1, 2006 to December 31, 2008 and a royalty of 2.5% on annual gross revenue for the period January 1, 2009 to December 31, 2013.

The company entered into two agreements with Technology Partnerships Canada ("TPC") whereby TPC granted financial assistance for the purpose of funding research and development activities which were completed on March 31, 2007. The contributions we received were based on the eligible expenditures we made during each period. As at August 31, 2006 the Company has received the entire \$2.9 million of the eligible TPC contributions.

### Income Taxes

Three months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Future income tax expense (recovery)	\$ (10)	\$ (117)	\$ 107
Current income tax expense (recovery)	63	(87)	150
	<u>53</u>	<u>(204)</u>	<u>257</u>
Nine months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Future income tax expense (recovery)	\$ (59)	\$ (140)	\$ 81
Current income tax expense (recovery)	103	(65)	168
	<u>44</u>	<u>(205)</u>	<u>249</u>

Based on the information available at the time of the issue of the interim financial statements for the three and nine months ended August 31, 2007, we estimated that we would not have sufficient taxable earnings in Canada in future periods to utilize a portion of our \$2.1 million Canadian non-capital losses carried forward, \$8.6 million scientific research and experimental development costs and other Canadian tax balances.

We have recognized a future income tax recovery in the three months ended August 31, 2007 related to temporary timing differences between accounting income and income for tax purposes in our U.S. subsidiaries as we believe that it is more likely than not that these differences will be realized in future fiscal years. In accordance with Canadian GAAP, we provided a valuation allowance against deferred tax assets where realization did not meet the requirements of "more likely than not" under the liability method of tax allocation. We continue to evaluate our taxable position quarterly and consider factors such as estimated taxable income, the history of losses for tax purposes, and the growth of the Company, among others.

### LIQUIDITY AND CAPITAL RESOURCES - August 31, 2007 compared to November 30, 2006

In thousands of U.S. dollars	August 31, 2007	November 30, 2006	2007 to 2006
Cash	\$ 202	\$ -	\$ 202
Current assets	12,685	14,333	(1,791)
Current liabilities	4,553	6,544	(2,210)
Working capital <sup>(1)</sup>	8,132	7,789	419

<sup>(1)</sup> Working capital is defined as current assets less current liabilities. Working capital does not have a standardized meaning or comparable measure under generally accepted accounting principles and may not be comparable to similar measures presented by other companies.

## OSI Geospatial Inc.

Management's Discussion and Analysis

For the three and nine months ended August 31, 2007

(expressed in U.S. dollars)

We strive to maintain cash-contributing profitable operations that provide an adequate liquidity and capital resource base for growth. We believe that cash flow from operating activities, together with lines of credit borrowings of Canadian \$2.0 million and US \$600,000 available under our revolving credit facilities, will be sufficient to fund operations and to provide for needed capital spending for the next 12 months. We expect cash flow from operations will continue to improve during the year as scheduled contract milestone payments will be made on several contracts.

At August 31, 2007 our current assets decreased primarily due to a reduction in accounts receivable. Our working capital has increased due to the proceeds received from the share issue, some of which were used to repay our line of credit and other current liabilities.

We have credit facilities consisting of an operating line and forward exchange contract facilities. The credit facilities permit us to borrow funds directly for general corporate purposes, including acquisitions, at floating rates. At August 31, 2007, we had no borrowings against our operating line. During the three months ended August 31, 2007, we utilized the facility which increased interest expense for the period.

### Cash Flows

Three months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Cash flows provided by (used in):			
Operating activities	\$ (1,383)	\$ (525)	\$ (858)
Investing activities	(651)	-	(651)
Financing activities	2,214	53	2,161
Impact of foreign exchange on cash balances	22	(34)	56
Nine months ended August 31	2007	2006	2007 to 2006
In thousands of U.S. dollars			
Cash flows provided by (used in):			
Operating activities	\$ (837)	\$ 1,405	\$ (2,242)
Investing activities	(821)	(8,333)	7,512
Financing activities	1,858	(468)	2,326
Impact of foreign exchange on cash balances	2	87	(85)

Cash flows used in operating activities for the three months ended August 31, 2007 were the result of an increase in accounts receivables offset by the net earnings for the period.

Cash flows used in investing activities for the three months ended August 31, 2007 were primarily reflective of additions to plant and equipment, intangibles and other assets.

Cash flows from financing activities for the three months ended August 31, 2007 were the result of the net proceeds of common share financing offset by a decrease in the operating line of credit.

Cash flows used in operating activities for the nine months ended August 31, 2007 were largely the result of the net loss for the period.

Cash flows used in investing activities for the nine months ended August 31, 2007 were primarily reflective of additions to plant and equipment, intangibles and other assets.

## OSI Geospatial Inc.

Management's Discussion and Analysis  
For the three and nine months ended August 31, 2007  
(expressed in U.S. dollars)

Cash flows from financing activities for the nine months ended August 31, 2007 were the result of the net proceeds of the common share financing offset by a decrease in the operating line of credit and the semi-annual dividends on our Class B preference shares.

As a result of the above mentioned changes, the line of credit utilization decreased by \$548,000 for the three months ended August 31, 2007, and decreased by \$904,000 for the nine months ended August 31, 2007.

In order to reduce the impact of exchange rate fluctuations, we use the forward exchange contract facility to mitigate any foreign exchange gain or loss that might occur. We use the forward exchange contract facility only for known or reasonably certain future foreign currency transactions. At August 31, 2007 we had not entered into any forward exchange contracts.

There can be no assurance that we will have adequate financial resources, financing, or cash flows to support the Company into the future.

## CONTRACTUAL OBLIGATIONS

Payments due by period	Total	Less than 1 year	1 to 3 years	4 to 5 years	After 5 years
In thousands of U.S. dollars					
Facility leases	\$ 3,761	\$ 643	\$ 1,194	\$ 869	\$ 1,055
Equipment leases	79	32	38	9	-
Total contractual obligations	<u>\$ 3,840</u>	<u>\$ 675</u>	<u>\$ 1,232</u>	<u>\$ 878</u>	<u>\$ 1,055</u>

## OFF BALANCE SHEET ARRANGEMENTS

### Guarantees

The Company has entered into a one year guarantee for one of the Company's subsidiaries, CHI Systems Inc. The Company has guaranteed CHI's bank line of credit that was put in place by the previous owners prior to OSI Geospatial's acquisition of CHI. The maximum potential amount of future payments the Company could be required to make under this guarantee is \$600,000. At August 31, 2007, the carrying amount of the liability was nil.

We warrant that our software and hardware products will operate substantially in conformity with product documentation and that the physical media will be free from defect. The specific terms and conditions of the warranties are generally one year but may vary depending on the country in which the products are sold. We accrue for known warranty issues if a loss is probable and can be reasonably estimated, and accrue for estimated incurred but unidentified warranty issues based on historical activity. To date, we have had no material warranty claims.

## TRANSACTIONS WITH RELATED PARTIES

In the periods being reported, the Company had no related party transactions.

## OSI Geospatial Inc.

Management's Discussion and Analysis  
For the three and nine months ended August 31, 2007  
(expressed in U.S. dollars)

### PROPOSED TRANSACTIONS

We are not currently engaged in any proposed transactions.

### SELECTED QUARTERLY DATA

In thousands of U.S. dollars

For the three months ended	August 31 2007	May 31 2007	February 28 2007	November 30 2006
Revenue	\$ 7,342	\$ 6,138	\$ 3,571	\$ 10,018
Gross profit	3,048	2,455	669	5,783
Gross profit percentage	42%	40%	19%	58%
Net earnings (loss)	279	(366)	(1,989)	2,780
Net earnings (loss) attributable to common shareholders	109	(748)	(1,989)	2,293
Loss per share – basic	0.00	(0.02)	(0.06)	(0.07)
Loss per share – diluted	0.00	(0.02)	(0.06)	(0.05)

  

	August 31 2006	May 31 2006	February 28 2006	November 30 2005
Revenue	\$ 4,316	\$ 6,140	\$ 3,662	\$ 5,137
Gross profit	1,403	2,595	1,193	2,636
Gross profit percentage	32%	42%	33%	51%
Net earnings (loss)	(709)	87	(1,229)	(783)
Net earnings (loss) attributable to common shareholders	(972)	(439)	(1,229)	(1,320)
Loss per share – basic	(0.03)	(0.01)	(0.04)	(0.05)
Loss per share – diluted	(0.03)	(0.01)	(0.04)	(0.05)

### CRITICAL ACCOUNTING POLICIES

These items are substantially unchanged as discussed in the Company's MD&A for the year ended November 30, 2006 as contained in our 2006 Annual Report filed on SEDAR at [www.sedar.com](http://www.sedar.com) or our annual Form 20-F report filed on EDGAR at [www.sec.gov](http://www.sec.gov).

### CHANGE IN ACCOUNTING POLICIES

In line with the conversion to Canadian GAAP, the Company has adopted the provisions of CICA Handbook Section 3855 *Financial Instruments – Recognition and Measurement*, CICA Handbook Section 3861 *Financial Instruments – Presentation and Disclosure*, CICA Handbook Section 3865 *Hedges* and CICA Handbook Section 1530 *Comprehensive Income*. These provisions became effective for the fiscal year beginning December 1, 2006.

#### (i) Financial Instruments – Recognition and Measurement

This standard prescribes the recognition and measurement of financial instruments. Section 3855 requires that all financial assets and liabilities (including derivatives) be measured at fair value on initial recognition except for certain related party transactions. Measurement in subsequent periods depends on the classification of the instruments. All financial instruments must be classified as one of the following

## **OSI Geospatial Inc.**

Management's Discussion and Analysis

For the three and nine months ended August 31, 2007

(expressed in U.S. dollars)

categories: held for trading, held to maturity, loans and receivables, available for sale assets and other financial liabilities.

The financial assets categorized as held for trading are measured at fair value with unrealized gains and losses recognized in net income. Section 3855 permits an entity to designate any financial instruments as held for trading on initial recognition or adoption of this standard, even if that instrument would not otherwise meet the definition of held for trading as specified in Section 3855. The Company's financial instruments classified as held for trading have included forward contracts and marketable securities, when used. The Company has historically measured these instruments at fair value and any unrealized gains and losses have been included in income. The Company's accounting treatment of these instruments remains unchanged as a result of adoption of the new accounting standards.

Available for sale financial assets are measured at fair value with unrealized gains and losses recognized in other comprehensive income. The Company currently has no assets classified as available for sale.

The financial assets classified as loans and receivables and held to maturity are measured at amortized cost. There is no change in accounting treatment for these financial instruments as a result of adoption of Section 3855.

### **(ii) Financial Instruments – Presentation and Disclosure**

CICA Handbook Section 3861 establishes standards for presentation of financial instruments and non-financial derivatives, and identifies the information that should be disclosed about them. Effective December 1, 2007, the Company will be required to adopt two new CICA standards: Section 3862 Financial Instruments – Disclosures; and Section 3863 Financial Instruments – Presentation, which will replace Section 3861 Financial Instruments – Disclosure and Presentation. The new disclosure standard increases the emphasis on the risks associated with both recognized and unrecognized financial instruments and how those risks are managed. The new presentation standard carries forward the former presentation requirements. The new financial instruments presentation and disclosure requirements were issued in December 2006 and the Company is assessing the impact on its consolidated financial statements.

### **(iii) Hedges**

This standard sets out the criteria of when hedge accounting is applied and how it is applied. It provides the option of designating qualifying transactions as hedges for accounting purposes. The qualifying hedging relationships include fair value hedges, cash flow hedges, and hedges of foreign currency exposures of net investments in self-sustaining foreign operations. The changes in the fair value of the hedging derivatives will be recognized in net earnings or other comprehensive income depending on the nature of the hedging relationships. Any gains and losses resulting from any ineffectiveness in hedging relationships are recognized in net income immediately. The Company does not currently have any hedges and as a result there is no change on adoption of Section 3865.

### **(iv) Comprehensive Income**

This section establishes standards for the reporting and disclosure of other comprehensive income ["OCI"] in a new category, Accumulated Comprehensive Income, which will be added to shareholders' equity on the consolidated balance sheet. Comprehensive income includes all changes in equity of the Company during a period except those resulting from investments by shareholders and distributions to shareholders. The major components included in Accumulated Comprehensive Income are unrealized gains and losses on financial assets classified as available for sale, and unrealized foreign exchange gains and losses arising on translation of the financial statements of self-sustaining foreign operations.

As a result of previously preparing the Company's financial statements in accordance with U.S. GAAP,

## **OSI Geospatial Inc.**

Management's Discussion and Analysis  
For the three and nine months ended August 31, 2007  
(expressed in U.S. dollars)

the adoption of Section 1530 alongside the conversion to Canadian GAAP has not resulted in any change in disclosure on the Company's balance sheet.

### **FINANCIAL INSTRUMENTS AND OTHER INSTRUMENTS**

#### **Foreign Exchange Forward Contracts**

The Company's Canadian subsidiaries use foreign exchange forward contracts to reduce their exposure on transactions denominated in U.S. dollars, Australian dollars, British pounds and euros. The purpose of these contracts is to reduce the level of exposure to exchange rate movements.

Derivative financial instruments are utilized by the Company to reduce our exposure to fluctuations in foreign exchange on certain committed and anticipated transactions. Derivatives are recorded as assets or liabilities, measured at fair value. Derivatives instruments are adjusted to fair value through income or loss.

At August 31, 2007, we had not entered into any foreign exchange forward or other derivative contracts.

### **DISCLOSURE OF OUTSTANDING SHARE DATA**

As at September 30, 2007, we had 42,242,326 issued and outstanding common shares and 3,141,166 outstanding stock options. As at September 30, 2007, we also had 30,262 issued and outstanding class A preference shares and 190,670 issued and outstanding class B preference shares series 2 convertible into common shares at conversion ratios of 1:1 and 1:58.82353 respectively which represents 11,215,588 common shares. Also at September 30, 2007, we had 16,568,368 outstanding common share purchase warrants convertible to common shares at a conversion ratio of 1:1, representing 16,568,368 common shares.

### **DISCLOSURE CONTROLS AND PROCEDURES**

The Company maintained a set of disclosure controls and procedures during the three and nine months ended August 31, 2007 designed to ensure that information required to be disclosed is recorded, processed, summarized and reported within the time periods specified in provincial securities legislation as defined under Multilateral Instrument 52-109. The Chief Executive Officer and the Vice President Finance have determined that there were no changes to the company's disclosure controls and procedures during the three and nine month period ended August 31, 2007 that have materially affected, or are likely to materially affect the design and operation of these disclosure controls and procedures.

### **INTERNAL CONTROLS OVER FINANCIAL REPORTING**

The Company maintains internal controls over financial reporting which have been designed to provide reasonable assurance of the reliability of external financial reporting as required by Multilateral Instrument 52-109. The Chief Executive Officer and the Vice President Finance, along with other employees to the extent considered necessary and appropriate, have designed internal controls over financial reporting that are effective as at August 31, 2007.

Nonetheless, the Chief Executive Officer and the Vice President Finance have identified areas where the Company can enhance process controls and they intend to incorporate such enhancements into the internal controls over financial reporting during the current fiscal year. The Company employs entity level controls to compensate for any deficiencies that may exist. Under 52-109, the Chief Executive Officer and the Vice President Finance are not required to, and have not yet tested the actual effectiveness of the Company's internal controls over financial reporting.

**OSI Geospatial Inc.**

Management's Discussion and Analysis

For the three and nine months ended August 31, 2007

(expressed in U.S. dollars)

There were no changes in the Company's internal controls over financial reporting that occurred since the beginning of the Company's current fiscal year to the date of this document that have materially affected, or are likely to materially affect the Company's internal controls over financial reporting.

**RISKS AND UNCERTAINTIES**

The primary risks and uncertainties that affect and may affect the Company and its business, financial condition and results of operations are substantially unchanged as discussed in the company's MD&A for the year ended November 30, 2006 as contained in our 2006 Annual Report filed on SEDAR at [www.sedar.com](http://www.sedar.com) or our annual Form 20-F which will be reported on EDGAR at [www.sec.gov](http://www.sec.gov).

# **OSI Geospatial Inc.**

**Interim Consolidated Financial Statements (Unaudited)  
Three and Nine Months ended August 31, 2007 and 2006  
(expressed in U.S. dollars)**

(Prepared in accordance with Canadian Generally Accepted Accounting Principles)

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# OSI Geospatial Inc.

(Incorporated under the laws of the Province of British Columbia, Canada)  
Consolidated Balance Sheets (unaudited)

In thousands of U.S. dollars

August 31, 2007 November 30, 2006

## Assets

### **Current assets**

Cash	\$ 202	\$ -
Accounts receivable (note 5)	10,425	12,707
Income taxes recoverable	173	28
Inventory (note 6)	1,336	1,063
Prepaid expenses and deposits	549	535
Current portion of future income tax asset	90	-
	<hr/>	<hr/>
	12,775	14,333

### **Future income tax asset**

49 -

### **Equipment and furnishings**

1,690 1,089

### **Intangible and other assets**

698 794

### **Goodwill**

8,330 8,129

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**\$ 23,542 \$ 24,345**

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## Liabilities

### **Current liabilities**

Bank indebtedness	\$ -	\$ 904
Accounts payable and accrued liabilities	4,011	4,887
Income taxes payable	54	86
Unearned revenue	452	667
Current portion of deferred rent	36	-
Current portion of future income tax liability	17	-
	<hr/>	<hr/>
	4,570	6,544

### **Deferred rent**

342 -

### **Future income tax liability**

83 20

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**4,995 6,564**

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### **Commitments and contingency** (note 8)

## Shareholders' Equity

### Issued and outstanding

30,262 Class A Series A preference shares (November 30, 2006 – 30,262) (note 7a)	19	19
190,670 Class B, Series 2 preference shares (November 30, 2006 – 279,840) (note 7b)	4,850	7,115
46,242,326 common shares (November 30, 2006 – 35,137,046) (note 7b)	21,058	15,887
	<hr/>	<hr/>
	25,927	23,021

### **Warrants**

4,618 4,286

### **Contributed surplus**

1,562 1,343

### **Accumulated deficit**

(15,806) (13,296)

### **Accumulated other comprehensive income**

2,246 2,427

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18,547 17,781

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**\$ 23,542 \$ 24,345**

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The accompanying notes are an integral part of the consolidated financial statements.

# OSI Geospatial Inc.

## Consolidated Statements of Operations (unaudited)

In thousands of U.S. dollars, except share related data	Three months ended August 31,		Nine months ended August 31,	
	2007	2006	2007	2006
<b>Revenue</b>				
Marine systems	\$ 3,124	\$ 1,240	\$ 6,267	\$ 4,958
Land and air systems	2,627	2,022	7,294	6,244
Mapping	1,591	1,054	3,489	2,917
	<u>7,342</u>	<u>4,316</u>	<u>17,050</u>	<u>14,119</u>
<b>Cost of sales</b>	<u>4,294</u>	<u>2,913</u>	<u>10,878</u>	<u>8,927</u>
<b>Gross profit</b>	<u>3,048</u>	<u>1,403</u>	<u>6,172</u>	<u>5,192</u>
<b>Expenses</b>				
General and administrative	1,451	1,460	4,249	4,320
Engineering	231	389	1,101	1,382
Sales and marketing	755	510	2,252	1,668
Depreciation and amortization	75	142	220	412
Interest expense	22	3	48	15
Interest income	-	-	(7)	(20)
Foreign exchange loss (gain)	43	(18)	65	(18)
Loss on sale of fixed assets	-	2	-	2
Technology Partnerships Canada royalty	139	55	276	220
Technology Partnerships Canada contribution	-	(227)	-	(731)
	<u>2,716</u>	<u>2,316</u>	<u>8,204</u>	<u>7,250</u>
<b>Net earnings (loss) before income taxes</b>	<u>332</u>	<u>(913)</u>	<u>(2,032)</u>	<u>(2,058)</u>
Future income tax recovery	(10)	(117)	(59)	(140)
Current income tax expense (recovery)	63	(87)	103	(65)
<b>Income tax expense (note 9)</b>	<u>53</u>	<u>(204)</u>	<u>44</u>	<u>(205)</u>
<b>Net earnings (loss)</b>	<u>\$ 279</u>	<u>\$ (709)</u>	<u>\$ (2,076)</u>	<u>\$ (1,853)</u>
<b>Net earnings (loss) available to common shareholders (note 7d)</b>	<u>\$ 109</u>	<u>\$ (972)</u>	<u>\$ (2,628)</u>	<u>\$ (2,642)</u>
<b>Earnings (loss) per share (note 7d) - basic and diluted</b>	\$ 0.00	\$ (0.03)	\$ (0.07)	\$ (0.08)
<b>Weighted average number of common shares outstanding (note 7d) – basic and diluted</b>	42,377,958	32,891,635	39,635,112	32,160,508
<b>Dividends declared per share</b>				
Class B preference shares – Series 2	\$ -	\$ -	\$ 1.64	\$ 1.59

The accompanying notes are an integral part of the consolidated financial statements.

# OSI Geospatial Inc.

## Consolidated Statements of Shareholders' Equity and Accumulated Deficit (unaudited) For the nine months ended August 31, 2007

In thousands of U.S. dollars except share numbers

	Units		
<b>Class A preference shares</b>			
Balance at November 30, 2006	30,262	\$	19
Balance at August 31, 2007	30,262	\$	19
<b>Class B preference shares</b>			
Balance at November 30, 2006	279,840	\$	7,115
Class B preference shares converted to common shares	(89,170)		(2,265)
Balance at August 31, 2007	190,670	\$	4,850
<b>Common shares</b>			
Balance at November 30, 2006	35,137,046	\$	15,887
Class B preference shares converted to common shares	5,245,280		2,265
Shares issued	5,860,000		3,219
Share issue costs, net of tax benefit			(313)
Balance at August 31, 2007	46,242,326	\$	21,058
<b>Warrants</b>			
Balance at November 30, 2006	13,788,368	\$	4,286
Warrants issued	2,780,000		332
Balance at August 31, 2007	16,568,368	\$	4,618
<b>Contributed surplus</b>			
Balance at November 30, 2006		\$	1,343
Share based broker compensation			74
Stock-based compensation			145
Balance at August 31, 2007		\$	1,562
<b>Accumulated deficit</b>			
Balance at November 30, 2006		\$	(13,296)
Dividends on Class B preference shares			(382)
Tax expense on dividends			(52)
Net loss for the period			(2,076)
Balance at August 31, 2007		\$	(15,806)
<b>Accumulated other comprehensive income</b>			
Foreign currency translation adjustment			
Balance at November 30, 2006		\$	2,427
Adjustment for the period			(181)
Balance at August 31, 2007		\$	2,246
<b>Total shareholders' equity</b>		<b>\$</b>	<b>18,547</b>

The accompanying notes are an integral part of the consolidated financial statements.

# OSI Geospatial Inc.

## Consolidated Statements of Cash Flows (unaudited)

Three and Nine Months Ended August 31, 2007 and 2006

In thousands of U.S. dollars	Three Months ended August 31,		Nine months ended August 31,	
	2007	2006	2007	2006
<b>Cash flows from (used in) operating activities</b>				
Net earnings (loss) for the period	\$ 279	\$ (709)	\$ (2,076)	\$ (1,853)
Items not affecting cash				
Depreciation and amortization	129	191	377	580
Stock-based compensation	5	-	145	104
Future income taxes	(83)	(116)	(177)	(73)
	330	(634)	(1,731)	(1,309)
Changes in non-cash working capital items				
Accounts receivable	(2,644)	690	2,504	4,326
Inventory	96	(190)	(155)	(300)
Prepaid expenses and deposits	75	(151)	36	(59)
Accounts payable and accrued liabilities	367	(167)	(1,381)	(1,387)
Income taxes payable	87	(85)	(143)	(256)
Unearned revenue	(57)	12	(330)	390
Deferred rent	363	-	363	-
	(1,713)	109	894	2,714
	(1,383)	(525)	(837)	1,405
<b>Cash flows from (used in) investing activities</b>				
Purchase of CHI Systems Inc., net of cash acquired (note 4b)	-	(4)	-	(8,127)
Purchase of Liddy International Inc. (note 4a)	-	-	(25)	-
Decrease (increase) in marketable securities	-	16	-	(143)
Decrease in restricted cash	-	-	-	129
Additions to equipment and furnishings	(111)	-	(225)	(83)
Additions to leasehold improvements	(540)	-	(540)	-
Additions to intangibles and other assets	-	(12)	(31)	(109)
	(651)	-	(821)	(8,333)
<b>Cash flows from (used in) financing activities</b>				
Payments to operating line of credit	(548)	-	(904)	-
Issue of common shares	2,812	53	2,812	59
Issue of warrants	332	-	332	-
Class B preference share dividends	(382)	-	(382)	(527)
	2,214	53	1,858	(468)
<b>Effect of foreign exchange on cash</b>	22	(34)	2	87
<b>Increase (decrease) in cash</b>	202	(506)	202	(7,309)
<b>Cash – beginning of period</b>	-	1,419	-	8,222
<b>Cash – end of period</b>	\$ 202	\$ 913	\$ 202	\$ 913

The accompanying notes are an integral part of the consolidated financial statements.

# OSI Geospatial Inc.

## Notes to the Consolidated Financial Statements (unaudited) Three and Nine Months Ended August 31, 2007 and 2006

### 1 Basis of presentation

These unaudited interim consolidated financial statements have been prepared by management and include the accounts of OSI Geospatial Inc. and its subsidiaries, collectively referred to as OSI Geospatial or the Company. These unaudited interim consolidated financial statements have been prepared in accordance with generally accepted accounting principles in Canada ("Canadian GAAP") and all amounts have been expressed in thousands of U.S. dollars unless otherwise noted.

The annual and interim consolidated financial statements issued to date in 2007, 2006 and 2005 were prepared in accordance with generally accepted accounting principles in the United States ("U.S. GAAP"). These previously released financial statements included a reconciliation to Canadian GAAP. The Company has restated all comparative amounts presented in the financial statements in accordance with Canadian GAAP and will re-issue the unaudited interim consolidated financial statements for the quarters ended February 28, 2007 and May 31, 2007, including full comparative information presented in accordance with Canadian GAAP.

These unaudited interim consolidated financial statements do not include all the information and footnote disclosures required by Canadian GAAP for annual financial statements. These unaudited interim consolidated financial statements should be read in conjunction with the Company's audited consolidated financial statements and notes thereto.

On April 12, 2006 at the Company's annual general meeting its shareholders voted in favor of changing the Company's name from Offshore Systems International Ltd. to OSI Geospatial Inc. The name change was effective June 5, 2006. For the purposes of this report, the Company is referred to by its new legal identity.

The preparation of these unaudited interim consolidated financial statements and requires management to make estimates and assumptions that affect the amounts reported. Actual results could vary from these estimates and the operating results for the interim period presented are not necessarily indicative of the results expected for the full year.

### 2 Nature of operations

OSI Geospatial Inc. designs, develops, and markets software and systems for enhancing situational awareness in command, control, and intelligence applications. OSI Geospatial's principal product is the proprietary ECPINS® line of electronic chart navigation systems for commercial and military customers. OSI Geospatial conducts its operations through three business units – International Systems Operations, U.S. Systems Operations and Mapping Operations. The Company's International and U.S. Systems business units develop and produce geographic information display systems and software for the marine navigation, and command and control markets, and situational awareness products for land-based and aeronautical command and control markets. The Company's Mapping business unit provides digital land map and electronic nautical chart production services, and produces and distributes electronic nautical chart data.

### 3 Accounting changes

#### a) Changes in accounting policies

In line with the conversion to Canadian GAAP referred to in Note 1 above, the Company has adopted the provisions of CICA Handbook Section 3855 *Financial Instruments – Recognition and Measurement*, CICA Handbook Section 3861 *Financial Instruments – Presentation and Disclosure*, CICA Handbook Section 3865 *Hedges* and CICA Handbook Section 1530 *Comprehensive Income*. These provisions became effective for the fiscal year beginning December 1, 2006.

#### (i) Financial Instruments – Recognition and Measurement

# OSI Geospatial Inc.

## Notes to the Consolidated Financial Statements (unaudited)

### Three and Nine Months Ended August 31, 2007 and 2006

This standard prescribes the recognition and measurement of financial instruments. Section 3855 requires that all financial assets and liabilities (including derivatives) be measured at fair value on initial recognition except for certain related party transactions. Measurement in subsequent periods depends on the classification of the instruments. All financial instruments must be classified as one of the following categories: held for trading, held to maturity, loans and receivables, available for sale assets and other financial liabilities.

The financial assets categorized as held for trading are measured at fair value with unrealized gains and losses recognized in net income. Section 3855 permits an entity to designate any financial instruments as held for trading on initial recognition or adoption of this standard, even if that instrument would not otherwise meet the definition of held for trading as specified in Section 3855. The Company's financial instruments classified as held for trading have included forward contracts and marketable securities, when used. The Company has historically measured these instruments at fair value and any unrealized gains and losses have been included in income.

Available for sale financial assets are measured at fair value with unrealized gains and losses recognized in other comprehensive income. The Company currently has no assets classified as available for sale.

The financial assets classified as loans and receivables and held to maturity are measured at amortized cost. There is no change in accounting treatment for these financial instruments as a result of adoption of Section 3855.

#### **(ii) Financial Instruments – Presentation and Disclosure**

CICA Handbook Section 3861 establishes standards for presentation of financial instruments and non-financial derivatives, and identifies the information that should be disclosed about them. Effective December 1, 2007, the Company will be required to adopt two new CICA standards: Section 3862 Financial Instruments – Disclosures; and Section 3863 Financial Instruments – Presentation, which will replace Section 3861 Financial Instruments – Disclosure and Presentation. The new disclosure standard increases the emphasis on the risks associated with both recognized and unrecognized financial instruments and how those risks are managed. The new presentation standard carries forward the former presentation requirements. The new financial instruments presentation and disclosure requirements were issued in December 2006 and the Company is assessing the impact on its consolidated financial statements.

#### **(iii) Hedges**

This standard sets out the criteria of when hedge accounting is applied and how it is applied. It provides the option of designating qualifying transactions as hedges for accounting purposes. The qualifying hedging relationships include fair value hedges, cash flow hedges, and hedges of foreign currency exposures of net investments in self-sustaining foreign operations. The changes in the fair value of the hedging derivatives will be recognized in net earnings or other comprehensive income depending on the nature of the hedging relationships. Any gains and losses resulting from any ineffectiveness in hedging relationships are recognized in net income immediately. The Company does not currently have any hedges and as a result there is no change on adoption of Section 3865.

#### **(iv) Comprehensive Income**

This section establishes standards for the reporting and disclosure of other comprehensive income ["OCI"] in a new category, Accumulated Comprehensive Income, which will be added to shareholders' equity on the consolidated balance sheet. Comprehensive income includes all changes in equity of the Company during a period except those resulting from investments by shareholders and distributions to shareholders. The major components included in Accumulated Comprehensive Income are unrealized gains and losses on financial assets classified as available for sale, and unrealized foreign exchange gains and losses arising on translation of the financial statements of self-sustaining foreign operations.

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### Three and Nine Months Ended August 31, 2007 and 2006

As a result of previously preparing the Company's financial statements in accordance with U.S. GAAP, the adoption of Section 1530 alongside the conversion to Canadian GAAP has not resulted in any change in disclosure on the Company's balance sheet.

#### b) Change in reporting currency

Effective March 1, 2006, the Company adopted the U.S. dollar as its reporting currency. In general this change results from an increase in the overall proportion of business activities conducted in U.S. dollars. The change was effected by translating assets and liabilities at the existing U.S./Canadian dollar foreign exchange spot rate on the last day of the month, while earnings were translated at the average rate for each month. Equity transactions have been translated at historical rates; with opening equity restated at the rate of exchange on December 1, 2001. The resulting net translation adjustment has been credited to the foreign currency translation adjustment.

Prior to March 1, 2006, the reporting currency of the Company was Canadian dollars.

## 4 Acquisitions

### a) Liddy International Inc.

On April 23, 2007, the Company through its subsidiary CHI Systems Inc., acquired the assets of Liddy International Inc. ("Liddy"), a United States defense contracting company and established Layered Security Solutions ("LSS"). LSS provides business continuity solutions against hazards and has the capability to develop deterrence, response and recovery strategies designed to deal with global threats to business and government. Under the terms of the agreement, the Company paid approximately \$184,000 for assets and goodwill of Liddy, of which \$25,000 was paid in cash with the balance paid by the issuance of 300,000 common shares of the Company of which 200,000 common shares are held in escrow subject to the satisfaction of certain contractual provisions.

The following table summarizes the fair value of the assets acquired by the Company at April 23, 2007, the date of acquisition. The acquisition was accounted for using the purchase method whereby assets acquired were recorded at their fair values at April 23, 2007. The excess of the purchase price over the fair market value was recorded as goodwill. The allocation of the purchase price is preliminary and the final allocation may be subject to refinement in the next three months subject to the final review by an independent business valuator.

In thousands of U.S. dollars

<b>Assets</b>	
Furniture and Fixtures	\$ 8
Computer Equipment	17
Goodwill	200
<b>Total assets acquired</b>	<u>225</u>
Net assets acquired (cash and common share consideration)	184
Direct acquisition costs incurred by the Company	<u>41</u>
<b>Total acquisition costs</b>	\$ 225
Less fair value of net identifiable assets acquired	<u>25</u>
<b>Goodwill</b>	<u>200</u>

The assets acquired are fully deductible for US tax purposes.

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Three and Nine Months Ended August 31, 2007 and 2006

## b) CHI Systems Inc.

On December 14, 2005, the Company acquired CHI Systems Inc. ("CHI Systems"), a United States defense contracting company. CHI Systems has multiple offices in the United States and is a supplier of technology and services to the U.S. Department of Defense and key defense prime contractors. Under the terms of the agreement, the Company paid approximately \$9.0 million for 100% of the outstanding shares of CHI Systems, of which \$8.1 million was paid in cash with the balance paid by the issuance of 1,067,975 common shares of the Company. Information regarding this acquisition can be found in the company's audited consolidated financial statements for the year ended November 30, 2006 as reported in our 2006 Annual Report filed on SEDAR at [www.sedar.com](http://www.sedar.com) or our annual Form 20-F reported on EDGAR at [www.sec.gov](http://www.sec.gov). The results of CHI Systems' operations have been included in the consolidated financial statements commencing December 14, 2005.

## 5 Accounts receivable

In thousands of U.S. dollars

	August 31, 2007	November 30, 2006
Trade	\$ 5,232	\$ 5,143
Unbilled revenue	4,961	7,257
Technology Partnerships Canada contribution	32	269
Other	254	97
Allowance for doubtful accounts	(54)	(59)
	<u>\$ 10,425</u>	<u>\$ 12,707</u>

## 6 Inventory

In thousands of U.S. dollars

	August 31, 2007	November 30, 2006
Materials and components	\$ 1,107	\$ 958
Finished goods	229	105
	<u>\$ 1,336</u>	<u>\$ 1,063</u>

## 7 Capital Stock

### a) Class A preference shares

The Company has 30,262 (November 30, 2006 – 30,262) Class A preference shares outstanding that have a value of \$19,000 (November 30, 2006 - \$19,000) for financial statement purposes. These Class A preference shares are being held in escrow but are no longer subject to any escrow restrictions and may be converted at any time into common shares of the Company, by notice in writing from the holders.

### b) Issued and outstanding common shares

- (i) During the nine months ended August 31, 2007, 89,170 Class B preference shares were converted into 5,245,280 common shares. The Class B preference shares were reduced, and the common shares were increased, by \$2.3 million, the carrying value of the shares converted. An additional 300,000 common shares were issued as part of the Liddy acquisition (note 4a).
- (ii) On July 31, 2007, the Company closed a private placement offering resulting in the placement of 5,560,000 units (the "Units") of the Company at a price of \$0.61 per Unit (CDN \$0.65), for gross

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### Three and Nine Months Ended August 31, 2007 and 2006

proceeds of \$3.4 million. Each Unit consists of one common share and one-half of one common share purchase warrant. Each warrant entitles the holder to purchase one common share of the Company at a price of \$0.75 per common share (CDN \$0.80) for a period of 24 months expiring July 31, 2009.

The gross proceeds from the private placement were allocated as follows: \$3.1 million was allocated to the 5,560,000 common shares issued and \$332,000 was allocated to the 2,780,000 warrants issued. Share issue costs associated with the private placement amounted to \$322,000 and included a \$74,000 broker compensation warrant entitling the broker to purchase up to 333,600 Units of the Company at a price of \$0.61 per Unit (CDN \$0.65) for a period of 24 months from the closing of the offering.

#### c) Stock option plans

A summary of the status of the Company's stock option plans at August 31, 2007 is as follows:

In U.S. dollars

	Number of shares	Weighted average exercise price
Outstanding – November 30, 2006	3,417,584	\$ 0.89
Granted	625,000	0.60
Cancelled	(203,000)	0.87
Expired	(698,418)	1.03
Outstanding – August 31, 2007	3,141,166	0.81
Exercisable – August 31, 2007	3,057,207	0.82

#### Stock-based compensation

For the three and nine months ended August 31, 2007 the Company incurred non-cash stock-based compensation expense of \$5,000 and \$145,000, related to 625,000 stock options granted (three and nine months ended August 31, 2006 - \$nil and \$104,000). Of the options granted in the nine month period ended August 31, 2007, 521,000 options vested immediately, 52,000 will vest over one year and 52,000 will vest over two years from the grant date. The expense was included in general and administrative costs and was recorded in contributed surplus.

The fair value of stock options was estimated using the Black-Scholes option pricing model using the following weighted average assumptions by grant year:

	2007	2006
Risk-free interest rate	4.09%	2.98%
Volatility	49%	54%
Estimated average option lives	5 years	5 years
Dividend yield	0.0%	0.0%

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Three and Nine Months Ended August 31, 2007 and 2006

## d) Earnings (loss) per share

In thousands of U.S. dollars except share related data	<b>For the three months ended August 31,</b>	
<b>Earnings (loss) per share – basic and diluted</b>	<b>2007</b>	<b>2006</b>
Net earnings (loss) for the period	\$ 279	\$ (709)
Less:		
Class B preference share dividends	(170)	(263)
Net earnings (loss) available to common shareholders	\$ 109	\$ (972)
Weighted average number of common shares outstanding – basic and diluted	42,377,958	32,891,635
Earnings (loss) per share – basic and diluted	\$ 0.00	\$ (0.03)

In thousands of U.S. dollars except share related data	<b>For the nine months ended August 31,</b>	
<b>Loss per share – basic and diluted</b>	<b>2007</b>	<b>2006</b>
Net loss for the period	\$ (2,076)	\$ (1,853)
Less:		
Class B preference share dividends	(552)	(789)
Net loss available to common shareholders	\$ (2,628)	\$ (2,642)
Weighted average number of common shares outstanding – basic and diluted	39,635,112	32,160,508
Loss per share – basic and diluted	\$ (0.07)	\$ (0.08)

The preference shares, the outstanding warrants and stock options were anti-dilutive for the purposes of calculating diluted earnings (loss) per share for the three and nine months ended August 31, 2007 and 2006.

If all preferred shares were converted, and all warrants and options were exercised, there would be a total of 77,198,001 common shares outstanding at August 31, 2007 (November 30, 2006 – 68,834,425). As a result of the exercise of all warrants and options, the Company would receive cash of \$16.2 million (November 30, 2006 - \$13.4 million).

## 8 Commitments and Contingency

The Company has entered into a one year guarantee for one of the Company's subsidiaries, CHI Systems Inc. The Company has guaranteed CHI's bank line of credit that was put in place by the previous owners prior to OSI Geospatial's acquisition of CHI. The maximum potential amount of future payments the Company could be required to make under this guarantee is \$600,000. At August 31, 2007, the carrying amount of the liability was nil.

# OSI Geospatial Inc.

## Notes to the Consolidated Financial Statements (unaudited)

### Three and Nine Months Ended August 31, 2007 and 2006

In July 2002, two of the Company's subsidiaries, Offshore Systems Ltd. and OSI Geomatics Ltd. (now Mapcon Mapping Ltd.), and four employees became subject to a lawsuit for an undisclosed amount by Triathlon Ltd., a subsidiary of MacDonald, Dettwiler and Associates Ltd., related to use of confidential information and breach of fiduciary duty. No amount has been accrued at August 31, 2007 in respect of these claims because the potential liability for the claims and the amount of damages, if any, cannot be reasonably estimated.

In January 2007, the Company signed a 10 year lease for new office facilities in Burnaby, British Columbia. It relocated its North Vancouver, British Columbia operations to Burnaby, British Columbia on August 1, 2007.

In April 2007, the Company signed a three year lease for new office facilities in Kanata, Ontario. It opened a corporate head office in Kanata on June 1, 2007.

The company has entered into operating leases for its office premises in Canada, United States and for certain equipment. Minimum lease payments required under the remaining terms of the leases are as follows:

Payments due by period	Total	Less than 1 year	1 to 3 years	4 to 5 years	After 5 years
In thousands of U.S. dollars					
Facility leases	\$ 3,761	\$ 643	\$ 1,194	\$ 869	\$ 1,055
Equipment leases	79	32	38	9	-
Total contractual obligations	<u>\$ 3,840</u>	<u>\$ 675</u>	<u>\$ 1,232</u>	<u>\$ 878</u>	<u>\$ 1,055</u>

## 9 Income taxes

The Company is subject to income taxes in Canada and the United States and the use of estimates is required in determining the Company's provision for income taxes. Although the Company believes its tax estimates are reasonable, the ultimate tax determination involves significant judgement that could become subject to audit by tax authorities in the ordinary course of business. The effective rate used to record income tax expense for the three and nine months ended August 31, 2007 differed from the Canadian federal and provincial combined statutory tax rate primarily due to the change in valuation allowance to reflect those future tax benefits that were more likely than not to be realized, and items not deductible for income tax purposes. The change in effective tax rate from 2007 to 2006 was due primarily to the effect of the change in valuation allowance.

At August 31, 2007, the Company adjusted its valuation allowance against future tax assets to reflect the amount of the future tax benefit that was more likely than not to be realized. A valuation allowance continues to be provided against those future tax assets for which there is significant uncertainty of future realization.

In thousands of U.S. dollars	Three months ended August 31,		Nine months ended August 31,	
	2007	2006	2007	2006
Future income tax recovery	\$ (10)	\$ (117)	\$ (59)	\$ (140)
Current income tax expense (recovery)	63	(87)	103	(65)
Income tax expense	<u>\$ 53</u>	<u>\$ (204)</u>	<u>\$ 44</u>	<u>\$ (205)</u>
Effective tax rate	16%	22%	(2%)	10%

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Notes to the Consolidated Financial Statements (unaudited)

Three and Nine Months Ended August 31, 2007 and 2006

## Segmented information

The Company's reportable segments are as outlined below. The Company defines reportable segments as components of the Company about which separate financial information is available and which is evaluated regularly by the chief operating decision maker in deciding how to allocate resources and in assessing performance.

In thousands of U.S. dollars

Three Months Ended August 31, 2007

	International Systems Operations	U.S. Systems Operations	Mapping Operations	Corporate and Public Company Costs	Total
Revenue	\$ 2,390	\$ 3,361	\$ 1,591	\$ -	\$ 7,342
Gross profit	1,331	1,127	590	-	3,048
Technology Partnerships Canada	139	-	-	-	139
Interest expense	-	7	-	15	22
Income tax expense (recovery)	-	(5)	36	23	54
Net earnings (loss)	287	578	194	(781)	279
Equipment and furnishings expenditures	441	15	170	25	651
Intangible expenditures	5	(12)	6	1	-
Depreciation and amortization	\$ 56	\$ 43	\$ 28	\$ 2	\$ 129

In thousands of U.S. dollars

Nine Months Ended August 31, 2007

	International Systems Operations	U.S. Systems Operations	Mapping Operations	Corporate and Public Company Costs	Total
Revenue	\$ 5,533	\$ 8,028	\$ 3,489	\$ -	\$ 17,050
Gross profit	2,915	2,092	1,165	-	6,172
Technology Partnerships Canada	276	-	-	-	276
Interest expense	-	8	-	40	48
Income tax expense	-	(17)	(25)	86	44
Net earnings (loss)	(656)	859	117	(2,396)	(2,076)
Equipment and furnishings expenditures	489	58	183	35	765
Intangible expenditures	15	(3)	18	1	31
Depreciation and amortization	\$ 159	\$ 113	\$ 101	\$ 4	\$ 377

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Notes to the Consolidated Financial Statements (unaudited)

Three and Nine Months Ended August 31, 2007 and 2006

In thousands of U.S. dollars

Three Months Ended August 31, 2006

	International Systems Operations	U.S. Systems Operations	Mapping Operations	Corporate and Public Company Costs	Total
Revenue	\$ 1,240	\$ 2,022	\$ 1,054	\$ -	\$ 4,316
Gross profit	719	472	212	-	1,403
Technology Partnerships Canada - net	(172)	-	-	-	(172)
Interest expense	-	-	-	3	3
Income tax expense (recovery)	-	6	(210)	-	(204)
Net earnings (loss)	(91)	25	85	(728)	(709)
Equipment and furnishings expenditures	(4)	4	2	(2)	-
Intangible expenditures	1	10	1	-	12
Depreciation and amortization	\$ 48	\$ 77	\$ 65	\$ 1	\$ 191

In thousands of U.S. dollars

Nine Months Ended August 31, 2006

	International Systems Operations	U.S. Systems Operations	Mapping Operations	Corporate and Public Company Costs	Total
Revenue	\$ 4,958	\$ 6,244	\$ 2,917	\$ -	\$ 14,119
Gross profit	3,012	1,439	741	-	5,192
Technology Partnerships Canada - net	(511)	-	-	-	(511)
Interest expense	-	-	-	15	15
Income tax expense (recovery)	11	12	(218)	(10)	(205)
Net earnings (loss)	169	75	(35)	(2,062)	(1,853)
Equipment and furnishings expenditures	42	19	24	(2)	83
Intangible expenditures	53	23	33	-	109
Depreciation and amortization	\$ 145	\$ 230	\$ 201	\$ 4	\$ 580

In thousands of U.S. dollars

Total assets employed

	International Systems Operations	U.S. Systems Operations	Mapping Operations	Corporate and Public Company Costs	Total
As at August 31, 2007	\$ 8,995	\$ 10,578	\$ 3,692	\$ 277	\$ 23,542
As at November 30, 2006	\$ 10,483	\$ 10,599	\$ 3,283	\$ (20)	\$ 24,345

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Three and Nine Months Ended August 31, 2007 and 2006

Geographically, revenues reported are based on the location of the Company's customers as follows:

In thousands of U.S. dollars	Three months ended August 31,		Nine months ended August 31,	
	2007	2006	2007	2006
Europe	\$ 1,166	\$ 651	\$ 3,297	\$ 1,084
Australia/New Zealand	1,121	149	1,556	933
United States	4,235	3,304	9,773	10,006
Canada	820	212	2,424	2,096
<b>Total</b>	<b>\$ 7,342</b>	<b>\$ 4,316</b>	<b>\$ 17,050</b>	<b>\$ 14,119</b>

Geographically, equipment and furnishings, and intangible and other assets are reported based on location. At August 31, 2007 and November 30, 2006, all of the Company's equipment and furnishings, and intangible and other assets were located in Canada and the U.S. as follows:

In thousands of U.S. dollars	August 31, 2007		
	Canada	U.S.	Total
Equipment and furnishings	\$ 1,406	\$ 284	\$ 1,690
Intangible and other assets	463	235	698
Goodwill		8,330	8,330
<b>Total</b>	<b>\$ 1,869</b>	<b>\$ 8,849</b>	<b>\$ 10,718</b>

In thousands of U.S. dollars	November 30, 2006		
	Canada	U.S.	Total
Equipment and furnishings	\$ 859	\$ 230	\$ 1,089
Intangible and other assets	322	472	794
Goodwill	-	8,129	8,129
<b>Total</b>	<b>\$ 1,181</b>	<b>\$ 8,831</b>	<b>\$ 10,012</b>