



Quarterly Report

FOR OUR SHAREHOLDERS



> QUARTER ENDING SEPTEMBER 30, 2003



CEO'S MESSAGE

Nstein's objective is to strive for profitability in the near term. In order to attain this objective, the Company remains fully committed to the e-publishing market, where Nstein concluded a total of seven new agreements in the third quarter of 2003 – most of which were not publicly announced at the request of our customers. At the same time, Nstein continues to aggressively maintain an effective expenditure management strategy and has reduced the overall loss for the first nine months of the present fiscal year to \$1.9 million versus \$4.2 million in 2002.

Nstein's increase in deal volume this quarter is directly attributed to its customer acquisition strategy. The majority of its sales this quarter were accomplished by selling pilot projects that are expected to lead to full-scale implementations. This strategy will enable our customers to quantify their return on investment, justifying the expense of the full-scale implementation – a valuable approach considering Nstein's track record of success in transforming pilots into full-scale implementations.

Despite the Company's commitment to streamlining costs, Nstein has continued to develop products required by our e-publishing customer base. For example, Nstein launched the Knowledge Base Manager that has resulted in two immediate sales of this product.

Along with the e-publishing market, the Company continues to develop solutions that solve mission-critical business issues in the law enforcement, legal, pharmaceutical, government and health markets. In order to address a number of these verticals, the Company has employed a channel strategy including the creation of long-term partnerships with integrators and vertical leaders that, once fully implemented, will accelerate the market penetration of Nstein solutions. These agreements – signed, planned and/or in the process of negotiation – greatly improve our positioning for sales in the next quarters. Two recent examples of such partnerships include Context Media as well as Interdoc Corporation. These partnerships have already yielded results, as witnessed by a sale to CMP Media Ltd via our partnership with Context Media.

Finally, Nstein continues to have a very strong backing from its investors as evidenced by the recent commitment of an additional \$2 million investment by the Solidarity Fund QFL and a loan of \$2.25 million authorized by the Bank of Montreal and Investissement Québec. These funds come at a very opportune time for Nstein, assuring the sustainability of the Company's current momentum and enabling Nstein to fulfill its corporate objectives.



MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL SITUATION AND OPERATING RESULTS

The following discussion and analysis should be read in conjunction with the non-audited consolidated financial statements for the three month period ending September 30, 2003, as well as the Management's Discussion and Analysis in the 2002 Annual Report, including the section Risks and Uncertainties.

Operating Results

During the third quarter of 2003, Nstein recorded a loss of \$445,350 or \$0.004 per share, as compared with a loss of \$1,353,497 or \$0.013 per share for the same quarter last year, representing an amelioration of 67%. During the nine-month period ending September 30, 2003, the loss totalled \$1,896,010 compared to \$4,242,263 for the same period in 2002, representing an amelioration of 55%.

The Company earned revenues of \$307,155 during the three-month period ending September 30, 2003, compared to \$263,768 for the same period last year, representing a 16% increase. Income recorded in the third quarter of 2003 is attributable to maintenance services provided to current customers and to the delivery of the new Knowledge Base Manager module to some of those clients. Nstein also generated income within the framework of pilot projects aiming at demonstrating the efficiency of its tools with important customers.

Operating, selling and administrative expenses amounted to \$583,172 during the third quarter of 2003, a 47% amelioration from the third quarter of 2002, when they stood at \$1,102,150. Meanwhile, research and development expenses totalled \$425,121 for the three-month period ended September 30, 2003, a reduction from last year when they totalled \$646,749. These cost reductions result from a program initiated during the fourth quarter of 2002. During the third quarter, the Company received \$221,125 related to research and development tax credits for the year 2002. Since these tax credits had not been accounted for in 2002 due to the uncertainty surrounding their realization, the amount of \$221,125 was included in the results of the third quarter of 2003.

Financial Situation and Cash flow

As at September 30, 2003, current assets were \$2.1 million compared to \$4.6 million as at December 31, 2002. Current liabilities reached \$1.1 million compared with \$1.8 million as at December 31, 2002.

Also at the end of the quarter, cash and cash equivalents stood at \$1.1 million compared to \$3.3 million as at December 31, 2002. Nstein's long-term debt was \$91,858 compared to \$129,963 as at December 31, 2002.

During the third quarter of 2003, cash flow assigned to operations reached \$460,586 compared to \$1,332,422 for the same quarter in 2002. This improvement can be explained with the decrease of this year's loss.

Cash flow allocated to debt repayment during the period ending September 30, 2003 totalled \$178,846 compared to \$342,600 for

Mario Girard
Chairman and Chief Executive Officer



MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL SITUATION AND OPERATING RESULTS

the same period last year. During this period, Nstein obtained a bank loan of \$172,011 for the financing of its research and development tax credits of the current year. Term deposits, which had been given in guarantee of the long-term debt, were released during the quarter, explaining the positive cash flows in investing activities in the amount of \$202,285.

Subsequent events

In the month of November 2003, the Solidarity Fund QFL made an additional investment in Nstein's capital through a private placement of 28.6 million common shares issued at \$0.07 each, for a \$2 million gross proceed. A term loan of \$2.25 million of the Bank of Montreal was also authorized, guaranteed in 80% by La Financière du Québec. An amount of \$1 million was disbursed upon the closing of the transaction. The balance of the loan will be gradually paid out according to the commercialization expenses committed by the end of financial year 2004 and conditionally to the achievement of certain levels of sale and operating results. As part of the transaction, equity warrants were also issued to the Solidarity Fund as well as to La Financière du Québec. The proceeds of the financing will allow the Company to pursue actively the commercialization of its products.

Bruno Martel
Finance Director

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This quarterly report includes forward-looking statements that are based on certain assumptions and reflect Nstein's current expectations. These forward-looking statements are subject to a number of risks and uncertainties that could cause actual results or events to differ materially from current expectations. Additional factors are discussed in Nstein's materials filed with the securities regulatory authorities in Canada from time to time. Nstein disclaims any intention or obligation to update or revise any forward-looking statements.

> QUARTER ENDING SEPTEMBER 30, 2003



CONSOLIDATED FINANCIAL STATEMENTS

NSTEIN TECHNOLOGIES INC. Consolidated Balance Sheets[†]

	As at Sept. 30 2003 \$ (unaudited)	As at Dec. 31 2002 \$
Assets		
Current assets		
Cash and cash equivalents	1,079,376	3,341,078
Term deposits	170,315	372,600
Accounts receivable		
Trade	537,697	405,387
Commodity taxes recoverable and others	61,060	75,779
Tax credits recoverable	252,500	352,500
Prepaid expenses	26,451	38,021
	<u>2,127,399</u>	<u>4,585,365</u>
Property, plant and equipment	<u>523,167</u>	<u>692,157</u>
	<u>2,650,566</u>	<u>5,277,522</u>
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities	685,356	677,018
Deferred revenues	184,245	250,056
Bank loan	172,011	-
Current portion of long-term debt	86,221	893,600
	<u>1,127,833</u>	<u>1,820,674</u>
Long-term debt	<u>91,858</u>	<u>129,963</u>
	<u>1,219,691</u>	<u>1,950,637</u>
Shareholders' Equity		
Share capital	18,445,136	18,445,136
Deficit	(17,014,261)	(15,118,251)
	<u>1,430,875</u>	<u>3,326,885</u>
	<u>2,650,566</u>	<u>5,277,522</u>

[†] The accompanying notes are an integral part of these consolidated financial statements.

Approved by the Board of Directors,

Mario Girard
Director

Marc Dutil
Director



CONSOLIDATED FINANCIAL STATEMENTS



CONSOLIDATED FINANCIAL STATEMENTS

NSTEIN TECHNOLOGIES INC. Consolidated Statements of Earnings†

	Three Months Ended Sept. 30		Nine Months Ended Sept. 30	
	2003	2002	2003	2002
	\$	\$	\$	\$
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
Revenues	307,155	263,768	1,021,526	915,072
Expenses				
Operating, selling and administrative	583,172	1,102,150	2,018,369	3,443,448
Research and development	425,121	646,749	1,271,365	1,843,328
Research and development tax credits	(304,625)	(230,241)	(522,714)	(420,241)
Depreciation of property, plant and equipment	39,170	56,986	132,545	148,858
Net financial expenses	9,667	41,621	17,971	141,942
	752,505	1,617,265	2,917,536	5,157,335
Loss for the period	445,350	1,353,497	1,896,010	4,242,263
Basic and diluted loss per share	0.004	0.013	0.018	0.043
Basic and diluted weighted average number of shares outstanding	104,267,165	104,267,165	104,267,165	99,651,780

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

NSTEIN TECHNOLOGIES INC. Consolidated Statements of Deficit†

	Nine Months Ended Sept. 30	
	2003	2002
	\$	\$
	(unaudited)	(unaudited)
Balance – Beginning of period	(15,118,251)	(10,440,115)
Loss for period	(1,896,010)	(4,242,263)
Balance – End of period	(17,014,261)	(14,682,378)

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



CONSOLIDATED FINANCIAL STATEMENTS



CONSOLIDATED FINANCIAL STATEMENTS

NSTEIN TECHNOLOGIES INC.

Consolidated Statements of Cash Flows[†]

	Three Months Ended Sept. 30		Nine Months Ended Sept. 30	
	2003	2002	2003	2002
	\$	\$	\$	\$
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
Cash flows from operating activities				
Loss for the period	(445,350)	(1,353,497)	(1,896,010)	(4,242,263)
Depreciation of property, plant and equipment not affecting cash and cash equivalents	39,170	56,986	132,545	148,858
	(406,180)	(1,296,511)	(1,763,465)	(4,093,405)
Change in non-cash operating working capital items				
Accounts receivable				
Trade	26,019	(49,477)	(132,310)	28,510
Commodity taxes recoverable and other	(6,045)	131,268	14,719	46,416
Tax credits recoverable	(82,500)	174,001	100,000	(15,999)
Prepaid expenses	(3,358)	(26,779)	11,570	11,286
Accounts payable and accrued liabilities	(8,330)	(52,538)	8,338	(145,777)
Deferred revenues	19,808	(212,386)	(65,811)	(33,479)
	(54,406)	(35,911)	(63,494)	(109,043)
	(460,586)	(1,332,422)	(1,826,959)	(4,202,448)
Cash flows from financing activities				
Bank loan	172,011	-	172,011	-
Payments on long-term debt	(178,846)	(342,600)	(845,484)	(1,089,780)
Variation in share capital, net of share issue expenses	-	(146,954)	-	5,628,067
	(6,835)	(489,554)	(673,473)	4,538,287
Cash flows from investing activities				
Variation in term deposits	202,285	19,734	202,285	176,377
Additions to property, plant and equipment	-	(10,420)	(2,294)	(517,312)
Tax credits related to property, plant and equipment	-	-	38,739	-
	202,285	9,314	238,730	(340,935)
Net change in cash and cash equivalents	(265,136)	(1,812,662)	(2,261,702)	(5,096)
Cash and cash equivalents - Beginning of period	1,344,512	5,367,413	3,341,078	3,559,847
Cash and cash equivalents - End of period	1,079,376	3,554,751	1,079,376	3,554,751
Additional information				
Interest paid	8,409	41,943	47,069	110,917
Interest cashed	(10,012)	(39,763)	(40,149)	(66,315)

[†] The accompanying notes are an integral part of these consolidated financial statements.



NOTES TO FINANCIAL STATEMENTS

1. Summary of significant accounting policies

The financial information as at September 30, 2003 and for the periods ended September 30, 2002 and 2003 is unaudited; however, in the opinion of management, all adjustments necessary to present fairly the results of these periods have been included. The adjustments made were of a normal recurring nature. Interim results may not necessarily be indicative of results anticipated for the year.

These interim financial statements have been prepared in accordance with Canadian generally accepted accounting principles and use the same accounting policies and methods used in the preparation of the Company's most recent annual financial statements. However, all disclosures required for annual financial statements have not been included in these financial statements. These interim financial statements should be read in conjunction with the Company's most recent annual financial statements.

2. Segment information

The Company is organized under a single operating segment, that being the sale of software and related post-contract customer support. Substantially all of the Company's property, plant and equipment are located in Canada. The accounting policies used for these reportable segments are consistent with those described in the summary of significant accounting policies.

Revenues by geographic region are detailed as follows:

	Three Months Ended Sept. 30	
	2003	2002
	\$	\$
	(unaudited)	(unaudited)
United States	270,155	254,018
Canada	37,000	9,750
	<u>307,155</u>	<u>263,768</u>
	Nine Months Ended Sept. 30	
	2003	2002
	\$	\$
	(unaudited)	(unaudited)
United States	880,893	850,572
Canada	140,633	64,500
	<u>1,021,526</u>	<u>915,072</u>

Revenues have been allocated to geographic regions based on the country of residence of the related customers.



NOTES TO FINANCIAL STATEMENTS

3. Accounting for stock-based compensation

The Company has elected not to use the fair value-based method to measure the compensation cost related to grants of stock options. In this instance, however, under section 3870, Stock-Based Compensation and Other Stock-Based Payments, the Company is required to make pro-forma disclosures of loss and basic and diluted loss per share as if the fair value based method of accounting had been applied.

The fair value of options granted was estimated using the Black-Scholes options pricing model with the following weighted average assumptions:

Period ending September 30, 2003

Risk-free interest rate	3.9%
Expected volatility	75%
Dividend yield	nil
Weighted average expected life	60 months

The Black-Scholes options valuation model was developed for use in estimating the fair value of traded options which have no vesting restrictions, and are fully transferable. In addition, option valuation models require the input of highly subjective assumptions including the expected stock price volatility. Because the Company's employee stock options have characteristics significantly different from those of traded options, and because changes in the subjective input assumptions can materially affect the fair value estimate, in management's opinion, the existing models do not necessarily provide a reliable single measure of the fair value of its employee stock options.

If the fair value based method had been used to account for stock-based compensation costs related to stock options issued to employees, directors and executive officers, the loss and related loss per share would be as follows:

	Three Months Ended Sept. 30	
	2003	2002
	\$	\$
	(unaudited)	(unaudited)
Pro-forma loss for the period	469,925	1,386,711
Pro-forma basic and diluted loss per share	0.005	0.013
	Nine Months Ended Sept. 30	
	2003	2002
	\$	\$
	(unaudited)	(unaudited)
Pro-forma loss for the period	1,958,045	4,334,575
Pro-forma basic and diluted loss per share	0.019	0.044



NOTES TO FINANCIAL STATEMENTS

4. Subsequent events

In the month of November 2003, the Company issued 28,571,429 common shares at a price of \$0.07 each to the Solidarity Fund QFL (the "Fund") for a gross amount of \$ 2,000,000. As part of this private placement, Nstein also granted the Fund equity warrants allowing the Fund to acquire 2 million of treasury shares to be issued at \$0.10 per share. These equity warrants are exercisable for a period of five years. In connection with the transaction, 6.7 million equity warrants previously issued to the Fund have been cancelled. The Company also obtained a \$2.25 million term loan from the Bank of Montreal, which is guaranteed at 80% by La Financière du Québec. In consideration for the loan guarantee, Nstein granted La Financière du Québec 2,649,429 equity warrants, each warrant entitling La Financière du Québec to acquire one common share to be issued at a price of \$0.13 each. These equity warrants are exercisable for a period of five years. An amount of \$1 million was disbursed upon the closing of the transaction. The balance of the loan will be used to finance commercialization expenses committed until the end of 2004. The subsequent disbursements are to be made subject to certain conditions in favor of the lender and guarantor, including achievement by Nstein of certain financial milestones relating to its income and profits for the fiscal year ending December 31, 2004 and for each of the three month periods ending March 31, 2004 and June 30, 2004. The term loan will be reimbursed over a 48 months period, starting in May 2004 and bears interests at the prevailing prime lending rate plus 2.95%. A second moveable hypothec of \$2,700,000 on Nstein's intellectual property and patent and the universality of the Company's present and future properties has been given as securities for this loan.

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