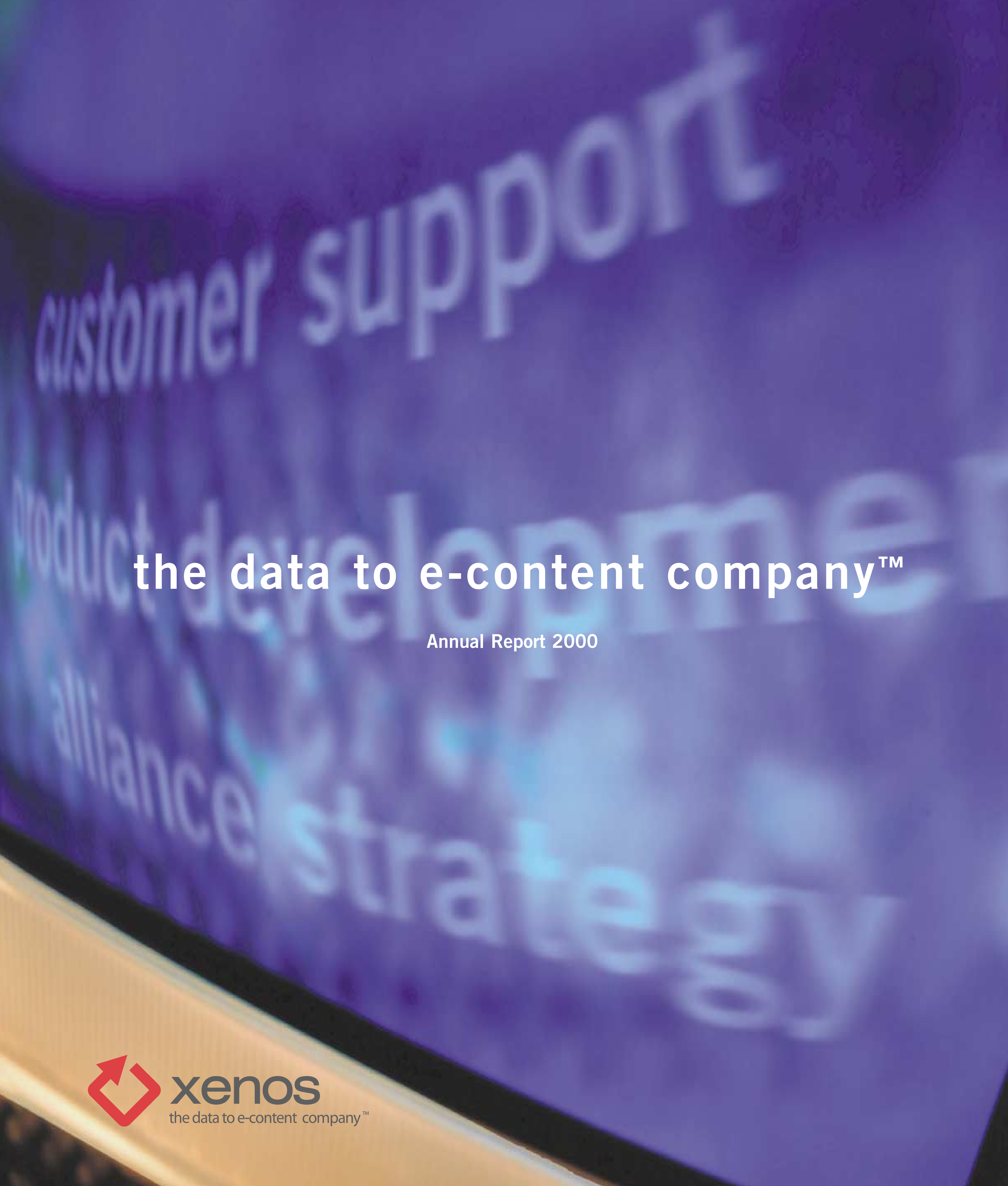

the data to e-content company™

Annual Report 2000

xenos
the data to e-content company™

Xenos

the data to e-content company™

Xenos is a leading provider of software solutions that transform organizations' legacy data and documents into e-content to support their e-business strategies.

The Xenos d2e Platform™ is deployed by some of the world's largest organizations in key industries, including banking, brokerage, insurance, telecommunications and utilities. Our technology enables them to rapidly and cost-effectively re-purpose complex corporate data and documents into e-content to enable critical e-business transactions online, reduce costs and time to market, and gain competitive advantage.

Xenos also provides software to systems integrators, ASPs (application service providers), and industry-leading alliance partners, such as IBM, who incorporate our leading-edge infrastructure software as part of the total e-business solutions they provide to customers.

Headquartered in Toronto, Canada, Xenos has global sales, professional services, product development, customer support and marketing operations. The company is listed on the Toronto Stock Exchange (TSE: XNS).

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data to e-content –
driving e-business >>

Today's large businesses are evolving as e-businesses. To help them make the transition, Xenos provides infrastructure software that transforms business-critical data and documents into e-content, enabling them to implement their e-business strategies – *and do it in Internet time*.

a refocused Xenos >>

>> to our shareholders

A great deal has been accomplished at Xenos in fiscal 2000, particularly during the last quarter, when the company was completely restructured, refocused and rebranded to properly align it with the needs of the market.

When Glen Manchester became President last July, as the architect of the new Xenos he conducted a wide-ranging review of our business, our products, our markets and our strategy. It was important that Xenos was clearly positioned in the marketplace, so in October the Company was rebranded and refocused as '*the data to e-content company*™,' reflecting our emergence as a leader in the data to e-content (d2e) marketplace.

Radical steps were taken to restructure the Company. We reduced our overheads and added new and highly skilled professionals in the key areas of product development, customer support and marketing. The result is a Company that is now appropriately structured to manage the significant growth we are confident we can achieve, with the infrastructure and the talent to service our clients today, and well into the future.

The Company was refocused on its core strengths in data and document transformation to provide a single, integrated infrastructure platform that will enable large organizations, as well as systems integrators, ASPs (application service providers), and solutions providers, to easily purchase and deploy our software to facilitate e-business.

To meet this exciting opportunity, our new development team has enabled us to provide a dynamic, component-based architecture, called the Xenos d2e Platform™. This powerful suite of proven products enables organizations to transform their existing 'legacy' transactional data and documents into Web-ready content. The first phase of this new architecture for document transformation was completed in the last quarter of fiscal 2000 and we plan to launch new configurations for data transformation and for developers in 2001.

This new standards-based platform will significantly expand the breadth of our markets, and also make it possible for Xenos to build long-term alliances with leading industry partners.

In October, key executives were recruited to help drive a new Xenos d2e Alliance Strategy. This will expand our markets by leveraging the extensive sales organizations of our partners, who can now benefit from integrating and reselling our technology.

Our alliance focus is aligning Xenos with a select number of leading e-business solution providers. Accordingly, relationship discussions are underway with such companies.

Subsequent to the year-end, we secured a new alliance agreement with IBM through which both parties are co-funding the marketing of the Xenos d2e Platform™ in conjunction with IBM's Content Manager OnDemand archiving and retrieval software. We have already successfully integrated our solutions at major customer sites, and we are excited about the future potential as we roll out our systems in conjunction with IBM's global sales and marketing support. The partnership with IBM is strong validation that our alliance strategy is effective and on track.

Another exciting development is a new partnership with Net innovators, iPlanet E-Commerce Solutions, a Sun-Netscape-AOL alliance. This partnership will enable large enterprises to transform existing 'legacy' data and present it for Internet Bill Presentment and Payment. Our companies are developing interoperability between the Xenos d2e Platform™ and the iPlanet BillerXpert application.

During the year, we also finalized alliance partnerships with RSD, an information distribution and document classification company, and NET*delivery*, a secure document delivery company. Our new platform and alliance strategy will open up further significant partner opportunities as we go forward. We will be concentrating on building strategic, long-term relationships of high value.

Our direct sales activities are now more focused. We have significant relationships with over 100 blue-chip customers, including such well-known and respected names as Wells Fargo, AXA, Cable & Wireless, Merrill Lynch, Guardian Life, Telenor, Charles Schwab, and NatWest Bank. The key challenge faced by these large, global companies is to release their existing and valuable customer data, currently stored in back office mainframe systems, and transform it into electronic content for the Internet. This is a highly complex process, and Xenos is well positioned to provide the key enabling infrastructure technology to help customers, as well as systems integrators and other partners, meet their e-business goals.

Using Xenos' solutions, companies can save millions of dollars in output, delivery and storage costs by presenting such critical documents as invoices and statements via the Web, while gaining important competitive advantage through improved customer service, unlimited personalization and targeted one-to-one marketing opportunities.

Our sales effort is focused on the key industries of banking, brokerage, insurance, financial services, telecommunications and utilities, where we have proven experience and a successful track record. We are also focusing on the fast-growing ASP (application service provider) marketplace, which analysts predict will grow from $2.7 billion in 1999 to $22.7 billion in 2003.

Underpinning these initiatives, we have put in place a new Global Customer Support infrastructure that will provide global coverage for all our customers and alliance partners.

The market opportunity for Xenos' solutions looks promising. The Electronic Statement Presentation (ESP), Electronic Bill Presentment and Payment (EBPP) and the electronic Customer Relationship Management (eCRM) markets are expanding as businesses around the world seek solutions that reduce costs while positioning them closer to their customers. Industry analysts forecast that within five years, 70% of all invoices and customer statements will be presented over the Internet, generating more than 59 billion electronic documents. Our technology is a key enabler in these markets.

Xenos is now well positioned with refocused product and alliance strategies to capitalize on these major opportunities.

In the second quarter of fiscal 2000, Xenos raised approximately $18 million through the sale of 500,000 common shares. These funds assure our ability to finance our current and future development and growth plans. Our short-term financial goals are to grow revenues by 25% to 30% in fiscal 2001, and to break even on a cash flow basis in the 2002 fiscal year. We are confident that we have the products and the resources to meet these objectives.

Finally, there is no doubt that the new strategy is working. Leading global companies are investing in our technology, the alliance program is established, and we are receiving great validation from industry analysts. The Company is proud of what has been accomplished over the past year and, under the direction of Glen Manchester, we are implementing some exciting initiatives along with the rest of the Xenos team to ensure a bright future for our investors. We are set to become the world leader in the data to e-content marketplace.

Glen Manchester
President and Chief Executive Officer

Stuart Butts
Chairman

evolution of the new Xenos >>

Xenos has refocused and restructured its business in the last year, introducing a new product strategy, a new alliance program, more focused sales activities and new global customer support, professional services and marketing operations.

>> **xenos data to e-content solutions**

As businesses evolve into e-businesses, they rely on multiple channels of communication – 'traditional' channels such as mail, and newer online channels including email, the Internet and wireless applications.

At the heart of this communication evolution is content. For a large organization, competitive advantage lies in re-purposing content, often held in 'legacy' mainframe systems, into electronic content (e-content) to do business on the Web.

Xenos, the data to e-content company™, provides solutions that transform organizations' transactional data and documents into e-content, supporting both offline and online business strategies.

“The Xenos d2e Platform™ provides a compelling solution for helping organizations leverage their investments in existing transactional systems to communicate with customers more effectively over the Web.” – *Doculabs, an independent analyst firm*

>> xenos d2e platform™

The Xenos d2e (data to e-content) Platform™ features a unique integrated architecture that enables companies to tap into existing print stream data (IBM AFP, Xerox Metacode or HP PCL) and turn it into leading e-content formats, such as XML, HTML and PDF. In 2001, this will be complemented by new data transformation and developer configurations, incorporating the same leadership technology. Transformation using the Xenos d2e Platform™ is rapid, highly cost-effective and avoids the requirement to build new and complex applications in order to present data and documents online.

>> integration as part of a total solution

Systems integrators, ASPs (application service providers), and industry-leading alliance partners are incorporating our technology as part of the total e-business solutions they provide to customers. The component-based architecture of the Xenos d2e Platform™ enables our partners to select the appropriate technology to meet the specific needs of customers.

>> a compelling market opportunity for our technology

Leading analysts forecast that within five years, 70% of all statements will be presented electronically. Over 60% of large US-based corporations will purchase content-related solutions in the next 6–12 months. The e-content marketplace will grow from around $6 billion this year to over $26 billion in 2005.

alliance strategy >>

“The combination of IBM Content Manager OnDemand and Xenos d2e Platform™ helps provide companies with a competitive edge. This relationship will help organizations leverage content within their e-business strategies, including electronic statement presentment (ESP), electronic bill presentment and payment (EBPP) and electronic customer relationship management (eCRM).” – *Jim Kelly,* *Vice President, Data Management Marketing, IBM*

>> new alliance with IBM

In December 2000, we secured an agreement with IBM to combine our technologies to assist customers transform legacy data and documents to Web-ready content for e-business. The Xenos d2e Platform™ supports both the data captured and archived into IBM’s Content Manager OnDemand solution, as well as web conversions to the retrieved data. As a result of this agreement we have already successfully integrated our solutions at major global organizations.

>> new agreement with iPlanet

In January 2001, we signed a new alliance agreement with iPlanet E-Commerce Solutions, a Sun-Netscape-AOL partnership, to support their comprehensive Internet bill presentment and payment solution. Through this new alliance we will work together to provide highly scalable, end-to-end Internet billing and presentment solutions to large organizations.

>> forging other new alliances

We have secured alliances with NET*delivery* Corporation, a provider of secure document delivery solutions, and RSD, a supplier of information distribution and document classification solutions. We are in discussions with other leading industry players to further grow our revenues.

>> Xenos' Alliance Strategy expands our market presence by enabling us to forge partnerships with leading industry players to provide complete end-to-end solutions for large companies seeking to transform existing legacy documents and data for presentation over the Internet.

>> To ensure our customers and our alliance partners receive the highest levels of support and service, we initiated a new and comprehensive global customer support infrastructure in fiscal 2000 that includes an advanced call center with Internet and toll free access, as well as real-time access to important customer information.

global customer support >>

"Our new and comprehensive global customer support infrastructure is a key component of the re-positioned and re-focused Xenos. We are now able to provide both our customers and our alliance partners with the highest levels of support and service."

– *Glen Manchester,* *President & CEO, Xenos*

>> **enhanced customer relationship management**

The implementation of a new global customer support infrastructure is just the first step in our commitment to provide our customers and alliance partners with superlative service and support.

>> **advanced call center operations**

Our innovative new call center management system allows us to manage our customer relationships more efficiently by providing instant and real-time access to client information, in addition to detailed reports and other customer data. We are also measuring and monitoring our service levels to ensure complete customer satisfaction. Our new global toll-free telephone number provides customers and business partners with a fast and convenient way to communicate with Xenos.

>> **24x7 coverage and self-service planned**

Future enhancements to our customer support operations include 24x7 coverage and a fully automated, Web-based self-service facility for our customers.

solutions for key industries >>

Xenos is providing data to e-content solutions to some of the world's largest organizations, in key industries including insurance, banking and brokerage, and telecommunications. We enable them to leverage existing 'legacy' transactional data and documents to achieve competitive advantage in their e-business operations.

insurance >>

competitive advantage

Although analysts agree that the insurance industry has been relatively slow in addressing the opportunities of e-business, Xenos has been working closely with innovative companies who are re-inventing critical parts of their businesses to maintain competitive advantage in the new economy. They are using our software to re-purpose their existing data and documents into powerful e-content that can be delivered to customers, brokers and business partners via the Web.

banking and brokerage >>

working with innovators

Xenos' customers include the world's Internet banking innovators. Analysts predict that the major banks will quadruple their investment in the Internet – Xenos' solutions are already proven in this fast growing sector and will enable the banks to move their businesses quickly and easily to the Web.

In retail brokerage, another area of success and excellent opportunity for Xenos, IT spending on Internet-related projects is projected to hit US$2.43 billion. Xenos' expertise in this industry will enable brokerage firms to move to full-service offerings on the Internet.

telecommunications >>

improving customer service

Telecommunications is one of the fastest growing industries in the world. The combined effects of deregulation and globalization of the industry, and the advent of Internet and wireless services, means that telecommunications companies are focusing on the best ways to improve customer service and maintain competitive advantage. Xenos solutions are enabling telecommunications providers to move from printed billing to powerful Internet billing systems, with all the opportunities for customer interaction, cross-selling and up-selling of services that provides.

George Patchen
Senior Software Advisor
The Guardian Life Insurance Company of America

"We chose Xenos' e-commerce software because it is cutting-edge, a necessity in today's digital economy. When you take Xenos' solution, and combine it with the power of IBM's Content Manager OnDemand software, you get a world-class solution that enables Guardian to provide the highest level of customer service."

Juan Paz
Imaging Systems Program Manager, ING ReliaStar

"One of the biggest challenges we faced was to centralize access to diverse information coming from multiple output streams and locations. Using the Xenos d2e Platform… we will save around US$143,000 per year by not printing, scanning, indexing and filing 3 million pages."

Mike Spencer
Vice President of Internet technologies, Bank of New York

"Information is power in the finance business. You need to make decisions quickly and to make decisions quickly you need to have accurate and timely information… Xenos, as a technology, is providing exactly the conduit that we need to channel that information out to our customers."

Al Nixon
Project Manager, KeyBank

"The Xenos Solution allows us to deliver information electronically faster, better and cheaper."

Stefan Albertsson
eCRM Project Manager, eircom

"As part of our CRM (customer relationship management) Program, designed to reinforce our market leadership and exploit growth opportunities, we embarked on a major e-Channel Project. We recognized that Xenos' software would help us replicate existing paper bills online, thereby improving customer service and loyalty, while reducing operating costs and increasing revenues."

Andrea Armani
CEO Delta Progetti 2000, a leading Italian ASP to the telecommunications industry

"Xenos demonstrated how it could take a customer's output of 4.5 million bills per month and transform it quickly and easily for Web presentment. We found Xenos' software to be robust and flexible and very easy to implement, which is a major benefit when selling to large and medium-sized telco companies."


coverage
premium
security


WALL ST

Xenos's financial highlights >>

"Through fiscal 2000 Xenos took a number of decisive steps to re-position and re-focus the Company for future growth and profitability. Our goal is to break even on a cash flow basis in fiscal 2002."

>> **strong revenue growth:**
Sales in fiscal 2000 increased consistently through the year, rising 47% compared to last year as the market for e-business applications grew and demand for Xenos' re-positioned product offering expanded.

>> **solid financial position:**
With working capital of $18.8 million, including cash of $18.5 million or $2.21 per share, and no long-term debt, we are confident that we possess the financial resources to achieve our short-term goals.

>> **an exciting future:**
The initiatives completed in fiscal 2000 position Xenos for continued strong quarterly revenue growth, enhanced margins and improved profitability going forward. Our re-structured operations, with a renewed focus on sales, marketing and customer support, underpin our confidence in a strong 2001. Our target this year is to grow revenues by 25% to 30%.

Management's Discussion and Analysis of Operating Results and Financial Position

Overview

Xenos Group Inc. ("Xenos") develops software solutions that transform existing 'legacy' transactional data and documents into e-content to enable e-business applications. Xenos solutions are deployed by large 'bricks and mortar' organizations in key industry segments, including banking and financial services, insurance, telecommunications and utilities. The Company has corporate headquarters in Toronto, Canada supported by global sales, marketing, product development and customer support. Xenos' leading edge software is used by alliance partners to provide total e-business solutions.

Market penetration of, and demand for, Xenos' products has accelerated as e-business applications have become popular and companies have allocated increased financial resources to solving issues in this industry market space.

During the last half of fiscal 2000, the Company conducted a comprehensive review of its markets, its products and its resources. As a result of this, the Company introduced its new brand as Xenos – the data to e-content company™.

The Company restructured its operations, reducing overheads while adding new and highly skilled professionals in such key areas as product development, customer support, sales and marketing. The Company also re-engineered its product line, creating a component-based architecture to enable customers and alliance partners to purchase the components they need. This re-architected product line was launched in October 2000 as the Xenos d2e Platform™.

In addition, the Company introduced its Alliance strategy in October, 2000 whereby selected industry partnerships were developed allowing the integration of Xenos' products with those of its Alliance partners. Finally, a new and comprehensive customer support infrastructure was put in place to provide global coverage for all Xenos' customers and Alliance partners.

Results of operations for the Year Ended September 30, 2000

For the year ended September 30, 2000, sales rose 47% to $15.4 million from $10.5 million in the previous year. The Company experienced growing demand for its products as compared to the previous year. Sales in the fourth quarter of 2000 were $4.2 million, up from $3.4 million in the third quarter, $3.7 million in the second quarter and $4.1 million in the first quarter. Sales of $4.0 million in the fourth quarter of fiscal 1999 included a one-time extraordinary sale of $2.4 million to Canada Post Corporation/Cebra Inc.

Geographically, 56% of sales in fiscal 2000 were in North America while 40% were in Europe compared to 83% and 5% respectively in fiscal 1999. License sales comprised approximately 50% of total revenues in fiscal 2000 compared to 50% in the prior year.

Gross profits for the year were 77% of sales compared to 90% in the prior year. The drop in gross margins is primarily the result of the Company's increased costs incurred to refocus its product line and enhance its competitive position in the global market for growth.

Overhead expenses including sales, marketing and administration were significantly higher than the prior year, due in part to the acquisition and integration of the European operations on October 1, 1999 and efforts to restructure the Company for future growth. Research and development expenses were 27% of sales (Fiscal 1999 – 13%) for the year and 41% in the fourth quarter. The higher fourth quarter number reflects the accelerated efforts to enhance and reposition the Company's suite of products and build and expand its new platform offering. It also includes a negative adjustment to the Company's Research and Development tax credits receivable of approximately $230,000.

Amortization charges of $4.0 million (Fiscal 1999 – $2.0 million) include $2.7 million relating to goodwill on acquisitions made over the past few years. These are non-cash charges in the income statement and are being amortized over the next four years.

The Company incurred a one-time pre-tax reorganization charge in the fourth quarter of $1.5 million. In addition to significant cost reductions, the Company made staff additions in key areas such as product development, marketing and customer support. These changes were made to ensure that the Company can meet the internal and external demands arising from the significant growth anticipated over the next few years .

Interest expense decreased to $92,811 from $248,660 in the prior year as a result of the repayment of long term debt with the proceeds from the initial public offering in August 1999.

The tax provision of $210,909 (Fiscal 1999 – $370,528) is primarily related to the U.K. and U.S. subsidiaries which are in a taxable position.

Not including the amortization of acquired and tangible assets and the restructuring charge referred to above, the Company incurred an adjusted net loss of $6.9 million or $0.86 per common share compared with an adjusted profit of $1.1 million or $0.20 per share in the prior year. The net loss for the year ended September 30, 2000 was $9.5 million or $1.19 per share compared to net profit of $338,466 or $0.06 per common share in 1999.

Results of Operations for the Year Ended September 30, 1999

Sales for twelve months ended September 30, 1999 increased by 83% to $10.5 million, surpassing 1998's total annual revenue of $5.7 million. During 1999, the Company experienced growing demand for both its software and service offerings, with larger projects for Bell Canada and Canada Post Corporation/Cebra Inc. augmenting increased software license sales volumes. This growth resulted from the internal sales growth generated by the Xenos software sales team, growing demand for project implementation services, and from the successful assimilation of GenText, which was purchased in January 1998.

Software license sales strengthened gross margins to 90%, up from 86% for the prior year despite the occurrence of a cost overrun of approximately $365,000 on a one time professional services project unrelated to the Company's core business.

Overhead expenses including sales, marketing and administration increased to $5.4 million from $3.1 million in the prior year as a result of planned additions to the sales team, an expanded marketing awareness campaign and strengthening of its administrative management team.

The Company expensed $1.4 million in research and development costs compared to $1.0 million in 1998. This effort was primarily focused on product enhancements to the Transform products and the large development project launch of the Documorph™ 2.0 software.

It had been the Company's practice to expense research costs as they were incurred. During the 1999 year, substantial development work related to the Documorph™ 2.0 software totaling $1.65 million was incurred and capitalized in accordance with Canadian generally accepted accounting principles. This is being amortized over three years commencing with $550,098 expensed during 1999.

Total amortization expense increased to more than $2.0 million from 1998's total of approximately $852,000. The goodwill relating to the GenText acquisition is being amortized over a 3 year period. In addition, following the completion of the Initial Public Offering, the Company paid off its long-term debt and as a result of this retirement, the deferred financing costs related to the purchase were written off and an additional $277,420 was expensed.

Interest expense increased to $248,660 compared to $213,602 for the prior year. These costs were substantially incurred prior to the completion of the initial public offering. Prior to the offering, these expenses were a reflection of the increased operational borrowings necessary to support stronger business activities. During this period, the Company also realized a gain of $219,292 on the sale of an investment.

In 1999, a tax provision of $370,528 was established (Fiscal 1998 – $82,604) reflecting the higher taxable income in the year. This arose from non-deductible goodwill amortization and other expenses which directly impacted the tax provision. The use of prior year's tax loss carryforwards also had a greater impact on reducing the 1998 tax provision. In the 1999 year, net earnings were $338,466 (3.2% of sales), a significant improvement over the prior year's loss of $334,539 or 5.8%.

Liquidity and Capital Resources

As at September 30, 2000, cash and short-term investments stood at $18.5 million (September 30, 1999 – $13.5 million) or $2.21 per common share. The Company currently has an operating line of credit of $1.0 million of which $684,615 (September 30, 1999 – $20,200) was unused, bearing interest at prime.

As a result of the increased level of business generated by the Company, working capital requirements have increased. Accounts receivable as at September 30, 2000 grew to $6.2 million from $5.1 million the prior year, and were with primarily large blue chip companies. Compared to the prior year, total working capital rose to $18.8 million from $15 million as at the same time the prior year. As at September 30, 2000 the company had no long-term debt and bank debt of $315,000.

Effective October 1, 1999, the Company acquired all of the issued shares of Xenos Europe Ltd., formerly Geneva Digital Inc., a private software development company located in the United Kingdom, for a total purchase price of $11.6 million (see Note 3 to the financial statements). The variances in Xenos' balance sheet for the year ended September 30, 2000 compared to the prior year are largely reflective of the consolidation of this acquisition.

On February 17, 2000, the Company successfully completed an offering of 500,000 Special Warrants that were converted to common shares on May 25, 2000 and generated net proceeds of approximately $18 million. The proceeds were used to reduce the bank operating lines and to fund the Company's ongoing growth plans.

Capital expenditures for the year ended September 30, 2000 were $2.2 million, significantly higher than the $805,835 in the prior year, and reflect the purchase of Xenos Europe during the year as well as additional expansion in North America.

Shareholders' equity stood at $31.4 million or $3.75 per common share as at September 30, 2000 compared to $18.5 million or $2.52 per common share at the same time the prior year.

Risks and Uncertainties

Xenos is subject to the typical risks of software-based technology companies. These risks and uncertainties include, but are not limited to, the following:

The Company is subject to rapid technological change, particularly the impact of the Internet and its growing adoption as a business tool. The Company's products are focused on helping its customers utilize the Internet, and as such are not as sensitive to these changes as other companies in the software business.

Because most of its sales are to customers in countries outside Canada, the Company is subject to foreign exchange risk. In addition, the Company has assets and liabilities in the United States and United Kingdom that are denominated in foreign currencies. The Company believes that its cash inflows in foreign currencies approximately match its cash outflows in those same currencies, and as such a natural hedge exists for the Company that can protect it from major adverse changes in foreign exchange.

The Company has a number of larger competitors with financial resources that are significantly larger than the Company's. Management believes that its focus on one market, its new Alliance strategy, and its extensive customer base limits its exposure to any one competitor.

The Company can experience fluctuations in operating results caused by changes in demand, sales cycles, delays in new product introductions or unexpected problems related to the implementation of its products.

The Company is dependent on its ability to hire and retain key employees in a market where there is generally a shortage of skilled technical, sales and management personnel. The Company believes its compensation programs, including competitive salaries and bonus plans, are sufficient to attract and retain the resources necessary to carry out its business plans.

Outlook

During and subsequent to the 2000 fiscal year, Xenos completed a number of initiatives to re-focus and re-position the Company for growth. Management believes that these initiatives will result in strong quarterly revenue growth, enhanced gross margins and improved profitability. As stated above, management believes that these factors will lead to Xenos meeting its goals of breaking even on a cash flow basis in the 2002 fiscal year.

Management's Responsibility for Financial Reporting

The accompanying financial statements of Xenos Group Inc. (Xenos) are the responsibility of management and have been approved by the Board of Directors on recommendation by the Audit Committee.

The financial statements have been prepared by management in accordance with generally accepted accounting principles. When alternative accounting methods exist, management has chosen those it deems most appropriate in the circumstances. Financial statements are not precise since they include certain amounts based on estimates and judgements. Management has determined such amounts on a reasonable basis in order to ensure that the financial statements are presented fairly, in all material respects. Management has prepared financial information presented elsewhere in the annual report and has ensured that it is consistent with that in the financial statements.

Xenos maintains systems of internal accounting and administrative controls of high quality, consistent with reasonable cost. Such systems are designed to provide reasonable assurance that the financial information is relevant, reliable and accurate and that the company's assets are appropriately accounted for and safeguarded.

The Board of Directors is responsible for ensuring that management fulfills its responsibilities for financial reporting and is ultimately responsible for reviewing and approving the financial statements. The Board carries out this responsibility through its Audit Committee.

The Audit Committee is appointed by the Board. The Committee meets periodically with management and the external auditors to discuss internal controls over the financial reporting processes, auditing matters and financial reporting issues to satisfy itself that each party is properly discharging its responsibilities, and to review the financial statements and the external auditors' report. The Committee reports its findings to the Board for consideration when approving the financial statements for issuance to the shareholders. The Committee also considers, for review by the Board and approved by the shareholders, the engagement or re-appointment of the external auditors.

Financial statements have been audited by Grant Thornton LLP, the external auditors, in accordance with generally accepted auditing standards on behalf of the shareholders. Grant Thornton LLP has full and free access to the Audit Committee.

Robert J. Kunihiro
Vice President, Finance and Chief Financial Officer
November 17, 2000

Auditors' Report

To the Shareholders of
Xenos Group Inc.

We have audited the consolidated balance sheets of Xenos Group Inc. as at September 30, 2000 and 1999 and the consolidated statements of operations and deficit and cash flows for the years then ended. These financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these financial statements based on our audit.

We conducted our audit in accordance with generally accepted auditing standards. Those standards require that we plan and perform an audit to obtain reasonable assurance whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the consolidated financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation.

In our opinion, these consolidated financial statements present fairly, in all material respects, the financial position of the company as at September 30, 2000 and 1999 and the results of its operations and its cash flows for the years then ended in accordance with generally accepted accounting principles.

Grant Thornton LLP

Chartered Accountants

Markham, Canada
November 17, 2000

Consolidated Statements of Operations and Deficit

Year Ended September 30	2000	1999
Sales	**$ 15,428,328**	$ 10,514,341
Service integration costs	**3,569,585**	1,075,134
Gross profit	**11,858,743**	9,439,207
Expenses		
Sales and marketing	**6,105,910**	2,612,241
Research and development	**4,120,735**	1,406,910
Administration and general	**5,951,398**	2,752,408
Reorganization costs	**1,484,969**	–
Amortization	**4,005,585**	2,009,832
Interest on long term debt	**–**	199,025
Interest and bank charges	**92,811**	49,635
	21,761,408	9,030,051
Earnings (loss) from operations	**(9,902,665)**	409,156
Other income		
Gain on sale of investment *(Note 5)*	**–**	219,292
Dividends, interest and other	**583,345**	80,546
Net earnings (loss) before income taxes	**(9,319,320)**	708,994
Provision for income taxes *(Note 13)*	**210,909**	370,528
Net earnings (loss)	**$ (9,530,229)**	$ 338,466
Net earnings (loss) per common share		
Basic	**$ (1.19)**	$ 0.06
Fully diluted	**$ (1.19)**	$ 0.06
Weighted average number of shares outstanding		
Basic	**7,975,201**	5,631,667
Fully diluted	**9,285,867**	6,368,917
Deficit, beginning of year	**$ (99,376)**	$ (437,842)
Net earnings (loss)	**(9,530,229)**	338,466
Deficit, end of year	**$ (9,629,605)**	$ (99,376)

See accompanying notes to the consolidated financial statements.

Consolidated Balance Sheets

September 30	**2000**	1999
Assets		
Current		
Cash and short term investments *(Note 11)*	**$ 18,470,090**	$ 13,468,550
Trade receivables	**6,172,867**	5,135,695
Other receivables	**409,626**	497,045
Prepaids	**315,228**	231,040
Income taxes recoverable	**202,590**	408,584
Deferred income taxes	**–**	282,000
	25,570,401	20,022,914
Deferred income taxes	**1,925,910**	512,449
Capital assets *(Note 4)*	**2,368,125**	1,012,692
Other assets *(Note 5)*	**831,891**	1,175,413
Goodwill *(Note 6)*	**7,679,324**	986,475
Total assets	**$ 38,375,651**	$ 23,709,943
Liabilities		
Current		
Bank indebtedness *(Note 7)*	**$ 315,385**	$ 1,354,800
Payables and accruals	**3,675,331**	2,377,045
Income taxes payable	**186,395**	–
Deferred revenue	**2,634,886**	1,248,784
	6,811,997	4,980,629
Long term deferred revenue	**183,974**	230,917
	6,995,971	5,211,546
Shareholders' Equity		
Capital stock *(Note 8)*	**41,009,285**	18,597,773
Deficit	**(9,629,605)**	(99,376)
	31,379,680	18,498,397
	$ 38,375,651	$ 23,709,943

Commitments and contingencies (Notes 9 and 10)

See accompanying notes to the consolidated financial statements.

On behalf of the Board

Director

Director

Consolidated Statements of Cash Flows

Year Ended September 30	2000	1999
Cash derived from (applied to)		
Operating activities		
Net earnings (loss)	**$ (9,530,229)**	$ 338,466
Amortization	**4,005,585**	2,009,832
Loss on sale of capital assets	**12,667**	–
Deferred income taxes	**(498,750)**	59,862
Gain on sale of investment *(Note 5)*	**–**	(219,292)
Change in non-cash working capital *(Note 12)*	**1,995,893**	(1,528,240)
	(4,014,834)	660,628
Financing activities		
Bank financing	**(1,039,415)**	1,354,800
Long term debt (net of repayments)	**–**	(2,327,247)
Proceeds on issue of special warrants	**17,941,676**	–
Proceeds on issue of shares	**224,625**	15,549,738
	17,126,886	14,577,291
Investing activities		
Cash paid on acquisition of subsidiary *(Note 3)*	**(5,444,547)**	–
Additional consideration paid on acquisition of subsidiary *(Note 6)*	**(288,248)**	(60,000)
Purchase of capital assets	**(2,152,187)**	(805,835)
Proceeds on sale of investment	**–**	387,681
Development costs incurred	**(263,140)**	(1,650,291)
Notes receivable	**37,610**	–
	(8,110,512)	(2,128,445)
Net increase in cash	**5,001,540**	13,109,474
Cash and short term investments		
Beginning of year	**13,468,550**	359,076
End of year	**$ 18,470,090**	$ 13,468,550

See accompanying notes to the consolidated financial statements.

Notes to the Consolidated Financial Statements

September 30, 2000

1. Nature of operations

Xenos develops software solutions that transform transactional data and documents into e-content to enable e-business applications. Xenos solutions are deployed by large "bricks and mortar" organizations in key industry segments, including banking and financial services, insurance, telecommunications and utilities. The Company has corporate headquarters in Toronto, Canada supported by global sales, marketing, product development and customer support. Xenos' leading-edge software is used by alliance partners to provide total e-business solutions.

2. Summary of significant accounting policies

The consolidated financial statements of the Company were prepared by management in accordance with Canadian generally accepted accounting principles.

Accounting estimates

In preparing the Company's financial statements, management is required to make estimates and assumptions that affect the reported amounts of assets and liabilities, the disclosure of contingent assets and liabilities, and the reported amounts of revenues and expenses. Significant areas requiring the use of management estimates include the useful lives of capital assets, the amount of investment tax credits to be received, the evaluation of impairment for long term assets, the value of assets acquired and liabilities assumed in business combinations, and the provision for income taxes. Actual results could differ from those estimates.

Principles of consolidation

The consolidated financial statements include the accounts of all companies in which the Company has a controlling interest, after the elimination of inter-company transactions and balances.

Investment tax credits

Investment tax credits relating to scientific research and experimental development expenditures are recorded as a reduction of the expenditure whether current or capital in nature in the period in which the investment tax credit was earned.

Amortization

Amortization of capital assets is recorded from the date of acquisition over their estimated service lives, on the following bases:

Computer equipment	– 30% declining balance
Software	– 33% straight-line
Office furniture and equipment	– 20% declining balance
Vehicles	– 25% declining balance
Leasehold improvements	– Straight-line over the term of the lease plus the first option period

Goodwill is amortized on the straight-line basis over its estimated useful life, on the following basis:

Xenos Inc. (formerly GenText, Inc.) – over 3 years

Xenos Europe Limited (formerly Geneva Digital Limited) – over 5 years

Deferred development costs are amortized on the straight-line basis over its estimated useful life, ranging from 1 to 3 years.

Goodwill

Goodwill arises on acquisitions and comprises the excess of amounts paid over the fair value of the net assets acquired.

Contingent payments made to the former owners of Xenos Inc. (Note 6) will be capitalized and amortized over three years beginning in the period the payment is made.

An evaluation to determine the amount of goodwill impairment, if any, is measured on the basis of estimated future undiscounted cash flows associated with the asset. The estimated future undiscounted cash flows is compared to the asset's carrying value to determine whether a write-down is required.

Revenue recognition
The Company recognizes revenue on software licenses upon satisfactory delivery to the customer. Customization and implementation revenues are recognized as the services are performed on a percentage of completion basis. Revenue from annual maintenance and support is recognized on a monthly basis over the term of the contract after ratification thereof.

Research and development
Research costs are expensed as incurred. Development costs are expensed as incurred unless a project meets the criteria under generally accepted accounting principals for deferral and amortization. The Company has deferred development costs in the current year.

Earnings per share
Basic earnings per share have been calculated using the weighted average number of common shares outstanding for the period.

Fully diluted earnings per share have been calculated under the assumption that all dilutive instruments were exercised at the beginning of the year, or at the date of issue, if later.

Translation of foreign currencies
Canadian legal entities and integrated foreign subsidiaries translate monetary assets and liabilities at the year end rate of exchange. Revenue and expenses are translated at average rates of exchange, except for depreciation, which is translated at the rates prevailing when the related assets were acquired. Translation gains and losses are included in earnings, except for unrealized gains and losses arising from translation of long-term monetary assets and liabilities, which are deferred and amortized over the remaining lives of the related items.

3. Acquisition

Effective October 1, 1999 the Company acquired all of the issued shares of Xenos Europe Limited, a private software development company located in the United Kingdom, for a total purchase price of $11,578,846.

The net assets acquired are as follows:

Total identifiable assets	$ 4,500,334
Total liabilities	1,978,533
Net assets	$ 2,521,801
Acquisition price	$ 11,578,846
Allocation:	
Net assets	$ 2,521,801
Goodwill	9,057,045
	$ 11,578,846
Consideration:	
Cash paid	$ 7,966,346
Shares issued	3,612,500
	$ 11,578,846
Net cash paid:	
Cash, per above	$ 7,966,346
Less: cash acquired	2,521,799
	$ 5,444,547

This acquisition has been accounted for by the purchase method and the results of operations from the acquired assets are included in the accounts of the Company from the effective date of acquisition.

4. Capital assets

	2000	1999
Cost		
Computer equipment	**$ 1,860,231**	$ 1,297,698
Software	**399,031**	–
Leasehold improvements	**665,745**	141,456
Vehicles	**218,882**	–
Office furniture and equipment	**636,667**	260,508
	3,780,555	1,699,662
Accumulated amortization		
Computer equipment	**820,265**	525,776
Software	**167,494**	–
Leasehold improvements	**149,350**	27,358
Vehicles	**54,721**	–
Office furniture and equipment	**220,601**	133,836
	1,412,430	686,970
Net book value		
Computer equipment	**1,039,966**	771,922
Software	**231,537**	–
Leasehold improvements	**516,395**	114,098
Vehicles	**164,161**	–
Office furniture and equipment	**416,066**	126,672
	$ 2,368,125	$ 1,012,692

5. Other assets

	2000	1999
Cost		
Financing fee	**$ 587,500**	$ 587,500
Deferred development costs	**1,913,431**	1,650,291
	2,500,931	2,237,791
Accumulated amortization		
Financing fee	**587,500**	587,500
Deferred development costs	**1,119,150**	550,098
	1,706,650	1,137,598
Net book value		
Financing fee	**–**	–
Deferred development costs	**794,281**	1,100,193
	794,281	1,100,193
Note receivable	**37,610**	75,220
	$ 831,891	$ 1,175,413

During the year ended September 30, 1999, the Company sold its investment for $500,511 for cash and a note receivable resulting in a gain of $219,292. The note receivable bears interest at 8% and is repayable bi-annually over a three year period. The current portion of this note is included in receivables.

6. Goodwill

	2000	1999
Cost	**$ 11,676,837**	$ 2,331,542
Accumulated amortization	**3,997,513**	1,345,067
Net book value	**$ 7,679,324**	$ 986,475

As part of the purchase price, the Company has agreed to pay the former principals of Xenos Inc. additional consideration. The consideration will be equal to the lesser of (i) US $2,500,000 and (ii) 8% of the amount by which the total net selling price of all Xenos Inc. products which use the Gentrans architecture sold by Xenos Inc. from the date of sale to December 31, 2003 exceeds US $1,750,000.

Subsequent to September 30, 2000, the Company made a prepayment of the additional consideration in the amount of US $500,000 to the former owners of Xenos Inc.

7. Bank indebtedness

The Company has a revolving operating line of credit available for $1,000,000 (1999 – $1,375,000), of which $684,615 was unused at September 30, 2000 (1999 – $20,200). This demand loan bears interest at prime which was 7.5% at September 30, 2000.

Security provided by the Company for the line of credit includes a general security agreement covering all the assets of the Company and cash collateral of $1,000,000 which is invested at the same institution.

8. Capital stock

Authorized:

An unlimited number of common shares.

		2000		1999
	Number	**Amount**	Number	Amount
Issued and outstanding:				
Balance, beginning of year	**7,347,500**	**$ 18,597,773**	5,185,000	$ 2,193,724
Issued for cash under private agreements	–	–	162,500	464,374
Issued pursuant to exercise of vested stock options	**89,500**	**224,625**	–	–
Issued in initial public offering	–	–	2,000,000	17,000,000
Issued in secondary offering	**500,000**	**19,500,000**	–	–
Share issuance costs	–	**(1,558,324)**	–	(1,914,636)
Deferred tax benefit of share issuance costs	–	**632,711**	–	854,311
Issued pursuant to acquisition of subsidiary	**425,000**	**3,612,500**	–	–
	8,362,000	**$ 41,009,285**	7,347,500	$ 18,597,773

The Company's stock option plan has authorized the issuance of 1,645,000 stock options. As at September 30, 2000, 1,212,375 common shares of the Company were reserved for stock options to employees and other service providers. These options may be exercised only while services continue to be provided. Options may be exercised as follows:

Option Price	Number	Expiry	Option Price	Number	Expiry
$ 0.44	45,000	July, 2003	$ 6.00	215,000	July, 2005
1.15	9,500	November, 2000	7.50	3,750	November, 2000
1.15	25,000	August, 2001	7.50	31,000	October, 2004
1.15	45,000	September, 2001	8.50	42,000	August, 2004
1.15	250,500	July, 2003	10.70	500	December, 2000
3.00	25,000	August, 2001	10.70	10,875	September, 2001
3.00	25,000	September, 2001	10.70	157,000	October, 2004
3.00	25,000	October, 2004	13.25	40,500	June, 2005
5.00	3,750	November, 2000	13.50	5,000	July, 2005
5.00	37,500	August, 2001	40.00	16,000	February, 2005
5.00	12,500	September, 2001	40.00	5,000	March, 2005
5.00	80,000	September, 2005	40.50	10,000	February, 2005
5.00	67,000	October, 2005	42.00	25,000	January, 2005

9. Commitments

The Company has entered into agreements to lease its premises and office equipment for various periods. The annual rent of premises consists of a minimum rent plus realty taxes, maintenance, heat and certain other expenses. Minimum rent payable for premises and equipment in aggregate and for each of the next five years is as follows:

2001	$ 704,075
2002	550,442
2003	332,894
2004	299,431
2005	204,980
Thereafter	1,279,913
	$ 3,371,735

10. Contingencies

The Company is a party to a legal proceeding brought by a former employee alleging entitlement to stock options for 50,000 common shares of the Company exercisable at a price of $3.00 per share plus damages which cannot be estimated at this time, if any.

The Company is a party to a legal proceeding brought by a shareholder of a predecessor company alleging entitlement to 135,900 Class A shares of the predecessor company. An estimate of the potential loss cannot be determined.

The Company denies entitlement and intends to vigorously defend both of these actions.

11. Financial instruments

Current financial assets and liabilities

Due to the short period to maturity of the instruments, the carrying values as presented in the consolidated balance sheets are reasonable estimates of fair value.

Short term investments

The fair value of the Company's short term investments approximates their carrying amounts. As at September 30, 2000 cash and short term investments include $15,237,481 of interest bearing notes (1999 – $13,028,276), all maturing by December 1, 2000.

Foreign currency risk

The following factors create significant exposure with regard to fluctuations in exchange rates:

- the majority of the Company's sales are denominated in U.S. dollars and British pounds
- Xenos Inc., a subsidiary of the Company, operates in the United States
- Xenos Europe Limited, a subsidiary of the Company, operates in the United Kingdom

The Company attempts, as much as possible, to match cash outlays with cash inflows in the same currency.

The Company's revenues denominated in U.S. dollars generate sufficient U.S. dollars to cover its annual U.S. dollar expenses and act as a hedge against exchange rate fluctuations. U.S. cash deposits are first reserved for anticipated payables in U.S. dollars, and any excess is converted into Canadian dollars.

The Company's revenues denominated in British pounds generate sufficient British pounds to cover its annual British pound expenses and act as a hedge against exchange rate fluctuations.

Other

Credit risk related to the Company's trade receivables is minimized due to its customer base of large and financially sound companies.

12. Supplemental cash flow information

	2000	1999
(a) Change in non-cash working capital:		
Receivables	**$ (949,753)**	$ (3,838,171)
Prepaids	**(84,188)**	(201,614)
Income taxes recoverable	**205,994**	94,627
Payables and accruals	**1,298,286**	1,627,685
Income taxes payable	**186,395**	–
Deferred revenue	**1,339,159**	789,233
	$ 1,995,893	$ (1,528,240)
(b) Cash and cash equivalents consists of cash on hand, balances with banks, and short term investments.		
(c) Interest paid	**$ 92,811**	$ 248,660
(d) Income taxes paid	**$ 604,111**	$ –
(e) Non-cash investing and financing activities:		

On October 1, 1999, the Company issued 425,000 common shares valued at $3,612,500 as part of the acquisition of Xenos Europe Limited.

13. Income taxes

The reconciliation of the statutory federal and provincial rates to the Company's effective income tax rate is as follows:

	2000	1999
Combined basic income tax	**$ (4,119,139)**	$ 316,353
Effect of differing tax rates of foreign jurisdictions	**(51,719)**	(19,186)
Benefit of previously unrealized tax loss carryforward	**–**	(185,252)
Non-deductible expense	**1,218,268**	346,605
Other	**44,479**	(87,992)
Increase in valuation allowance	**3,119,020**	–
	$ 210,909	$ 370,528

Future income taxes represent the future benefits of temporary differences between the tax and accounting bases of assets and liabilities consisting of:

	2000	1999
Future tax assets		
Net operating loss carryforwards	**$ 3,579,752**	$ –
Share issue costs	**959,937**	683,449
Investment tax credits	**598,970**	111,000
Foreign Tax credits	**18,589**	–
Valuation allowance	**(3,231,338)**	–
	$ 1,925,910	$ 794,449

The loss carryforward amounts for income tax purposes expire as follows:

	Non-capital losses		Investment tax credits	
	Federal	Provincial/ State	Federal	Provincial/ State
2005	$ –	$ 612,857	$ –	$ –
2006	–	–	–	–
2007	7,536,492	7,735,688	–	–
2009–2019	731,245	–	386,135	–
	$ 8,267,737	$ 8,348,545	$ 386,135	$ –

14. Segmented information

Management has determined that the Company operates primarily within one dominant business segment, being electronic commerce.

Geographic information

The following table provides information about geographic sales, capital assets and goodwill.

	Sales		Capital Assets and Goodwill	
	2000	1999	**2000**	1999
Canada	**$ 856,986**	$ 3,099,400	**$ 998,337**	$ 656,283
United Kingdom	**5,500,829**	141,300	**7,892,948**	–
United States	**7,710,414**	5,600,600	**1,156,164**	1,342,884
Other	**1,360,099**	1,673,041	**–**	–
	$ 15,428,328	$ 10,514,341	**$ 10,047,449**	$ 1,999,167

15. Related party transactions

The Company had the following transactions with companies owned by significant shareholders:

	2000	1999
Interest expense	**$ –**	$ 174,277

16. Change of name

During fiscal 1999, the Company changed its name from The Xenos Group Inc. to Xenos Group Inc.

Directors and Officers

Stuart Butts [1,2,3]
Director and Chairman of the Board

George Fowlie [1,3]
Director
Partner, NB Capital Partners

James Farmer
Senior Vice-President of Sales

Calvin Galatiuk
Director and Development Manager

Robert Hines [1,2]
Director
Partner, Heidrick & Struggles

Robert Kunihiro
Vice-President, Finance and Chief Financial Officer

Chungsen Leung
Director
President, UTC Universal Trading Corporation, a technology trading company

Marian Lewandowski
Vice-President

Glen Manchester
Director and President & Chief Executive Officer

Edmund Merringer [3]
Director and Secretary
Partner, Borden Ladner Gervais LLP

Barry Monk
Vice-President, Marketing

Kent Petzold [2]
Director, Chairman and Chief Executive Officer
Cyclone Commerce, Inc.

Notes:
1 Member of the Audit Committee
2 Member of the Compensation Committee
3 Member of the Corporate Governance Committee

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Trading
Xenos Group Inc. trades on The Toronto Stock Exchange and is listed under the symbol XNS.

Investor Relations
Robert Kunihiro
Vice-President Finance and Chief Financial Officer
e-mail: rkunihiro@xenos.com

Report Availability
This annual report can be downloaded from the Xenos Group web site at www.xenos.com

Annual General Meeting
Xenos will hold its 2000 Annual General Meeting at 10:00 am on Tuesday, March 27, 2001 in the Auditorium of The Toronto Stock Exchange, The Exchange Tower, 2 First Canadian Place, Toronto, Ontario

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