



Third Quarter Report

Three and nine months ended June 30, 2007

To Our Shareholders:

Xenos revenues for the third quarter ended June 30, 2007 rose to \$3,803,000 as compared to revenues of \$3,767,000 for the same quarter last year. Revenues for the nine months ended June 30, 2007 were \$11,454,000 as compared to \$10,514,000 for the first nine months of fiscal 2007.

Xenos reported a significantly improved EBITDA of \$385,000 for its third quarter as compared to negative EBITDA of \$786,000 for the third quarter ended June 30, 2006

This improvement, in part reflects the corporate reorganization undertaken in the second quarter that put Xenos on a solid footing for profitable growth. Total expenses were reduced by 30% to \$3,024,000, from \$4,326,000 in the third quarter of fiscal 2006. Year over year sales and marketing expenses were reduced to \$1,512,000 from \$2,716,000.

Xenos third quarter results were significantly impacted by the material decline of the U.S. dollar (7.7%) and UK pound sterling (6.0%) against the Canadian dollar during the quarter.

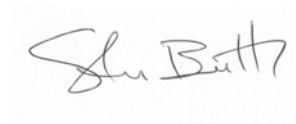
The bulk of Xenos revenues are denominated in these currencies and constitute a significant portion of our balance sheet items. As a result, revenues were lower than they would have been on a constant currency basis and we were forced to take a significant write-down of foreign denominated assets (principally cash and receivables) at the end of the quarter. This write-down represents the bulk of the foreign exchange loss of \$523,220 recorded in the financial statements.

The Company reported a third quarter net loss of \$378,000, or (\$0.04) per share, compared with a net loss of \$1,374,000, or (\$0.14) per share, for the third quarter of fiscal 2006.

As previously announced, an ECM migration project (valued at approximately US\$700,000) signed late in the quarter, did not generate revenue in Q3, but represents an important win that will come into revenue in Q4 and Q1 of 2008.

Stakeholders should not allow the currency issue to mask the very real improvement in operating results and outlook accomplished over the past three quarters.

At June 30, 2007, Xenos reported no significant long-term debt and held cash of \$7,594,000, or \$0.76 per common share, an increase from \$7,308,000, or \$0.74 per common share at September 30, 2006.



Stuart Butts
Chairman of the Board,
Chief Executive Officer
and President

MANAGEMENT'S DISCUSSION AND ANALYSIS

For the three and nine months ended June 30, 2007

This Management's Discussion and Analysis of Financial Condition and Results of Operations of Xenos Group Inc. ("Xenos" or the "Company") has been prepared as of August 3, 2007 and should be read in conjunction with the unaudited Consolidated Financial Statements and Notes included in this Quarterly report for the three and nine months ended June 30, 2007 and should be read in conjunction with the audited Consolidated Financial Statements and Notes, and Management's Discussion and Analysis contained in the Company's Annual Report for the fiscal year ended September 30, 2006.

The financial data contained in this Management's Discussion and Analysis has been prepared in accordance with Canadian generally accepted accounting principles and, unless otherwise indicated, is reported in Canadian dollars.

Corporate History

Xenos was formed under articles of amalgamation dated October 1, 1989. The Company acquired GenText, Inc. ("Gentext"), a private software development company located in Dallas, on January 1, 1998. Gentext had developed printstream transformation software that formed the basis of Xenos' current d2e Platform™ and d2e Vision™ products. On October 1, 1999, Xenos acquired Geneva Digital Limited ("Geneva"), a private value-added software reseller based in London, which sold and maintained third party document solutions in the U.K. Today, Geneva (now Xenos Europe Limited) is the Company's sales office in Europe selling a combination of Xenos products, services and third party based document solutions. Xenos acquired Rush Creek Software Corporation ("Rush Creek"), a private software developer based in Dallas, on May 17, 2002. Rush Creek brought the infoWEB™ report distribution product to Xenos' suite of products in addition to its important customer base. Finally, on November 17, 2003, Xenos acquired the business assets of XML-Global Technologies, Inc. ("XML Global") which included the GoXML™ data integration suite of products, that now form the basis of Xenos' current terminalONE™ product suite, as well as its customer base.

Overview of Business

Xenos high-performance software solutions streamline enterprise information supply chains. We enable our customers to process, transform, repurpose, personalize and deliver their data and documents when they need it, where they need it and how they need it. Xenos extends the value of existing IT investments, enabling organizations to increase efficiency, agility and accountability. By streamlining, standardizing and automating the handling of information on demand, our customers reduce costs while increasing a powerful competitive advantage—adaptability.

Xenos has customers worldwide in financial services, insurance, healthcare, telecommunications, manufacturing, logistics, transportation, retail and government sectors. Xenos sells and supports its solutions directly from offices in Canada, the United States, the United Kingdom and France and through a global partner network.

Xenos focuses on the Enterprise Information Management market as a technology and solutions innovator of high performance data and document solutions specializing in 3 market niches. In the Enterprise Content Management (ECM) space Xenos provides solutions for transactional content repurposing and migration for document archives and for persuasive content integration, personalization, delivery & presentment. In the Structured Data Handling space Xenos provides solutions for structured data handling, repurposing, delivery & presentment.

Xenos is the only vendor with an integrated solution that processes, transforms, repurposes, personalizes and delivers both structured and semi-structured information within Service Oriented Architecture (SOA) environments.

Xenos product technologies include Xenos d2e™, a high-volume document data stream repurposing solution that captures data, transforms, indexes and repurposes document data streams for enterprise content management, enhanced archiving, distribution and printing; Xenos infoWEB™, a secure electronic report distribution and presentment solution; and Xenos terminalONE™, a high volume structured data transformation and intelligent routing solution that expedites business transactions over the Internet.

Xenos partners with industry-leading software companies to provide end-to-end solutions for its customers. Key technology partnerships include Oracle, IBM/FileNet, EMC/Documentum and Navis among others. The Company sells primarily through its direct sales force but also partners with value-added resellers in specific markets such as Latin America, Asia and certain countries of continental Europe. To a much lesser extent, the Company continues to sell through a small number of OEM and Service Bureau partners on an application specific basis.

Xenos Integrated Document Solutions (marketed principally in the U.K.) use in-house expertise, owned and third party software to enable organizations to automate, personalize and manage their business communications through document creation, content automation and content management.

Overall Performance

Xenos reported revenue for the nine months ended June 30, 2007 of \$11.45 million representing an increase of 9% from the nine months ended June 30, 2006. Despite the period over period increase, the decline in the U.S. dollar as compared to the Canadian dollar had a deflating effect, as a majority of the Company's revenue is denominated in U.S. dollars. As a result, revenues were lower than they would have been on a constant currency basis.

In September 2006, Management initiated a right-sizing plan to return the Company to profitability. Beginning in September 2006 the Company reduced its staff levels from a high of 110 employees to a current level of 82, a reduction of 25%. In December 2006 Management announced its commitment to reduce the Company's discretionary marketing expenditures by approximately \$1.7 million for fiscal 2007 as compared to fiscal 2006. As part of the overall right-sizing plan, the Company's offices in Dallas (U.S.A.) and Vancouver (Canada) were closed and all executive management positions were relocated to the Company's North American head quarters in Richmond Hill (Canada). The costs associated with the right-sizing plan were recorded as restructuring charges in the second quarter of fiscal 2007. As a result, third quarter expenses represent the full savings from these right-sizing activities.

While Management is confident that the Company will report a profitable year from operations in fiscal 2007, its overall profitability goal in fiscal 2007 has been negatively impacted by the decline in both the U.S. dollar and the U.K. pound sterling as compared to the Canadian dollar. From March 31, 2007 to June 30, 2007 the U.S. dollar and the U.K. pound sterling have declined 7.7% and 6.0% respectively against the Canadian dollar which has resulted in a material foreign exchange loss in the period.

To continue to meet its profitability goals, the Company must continue to grow new license and professional service revenues by focusing on its core global markets and through the rollout of its ECM migration/consolidation services offering in the rapidly evolving ECM marketplace. Management will continue to align its expenditures with its key strategic objectives.

During the third quarter of fiscal 2007, the Company announced that it had been selected by a major U.S. insurance organization to implement a strategic project for ECM systems document migration from an existing Mobius archive to an enterprise content

management system based on Oracle Content DB. The project is expected to generate in approximately \$700,000 US in revenue for the Company and will be recognized over the fourth quarter of fiscal 2007 and the first quarter of fiscal 2008.

RESULTS OF OPERATIONS

Total sales for the nine months ended June 30, 2007 were \$11.45 million as compared to \$10.51 million for the nine month period ending June 30, 2006 representing an increase of 9%. The increase was largely driven by the increases in both new license revenue and services associated with its infoWEB™ and d2e Vision™ products and its third party related software products offered primarily in Europe.

Geographically, 64% of sales in the first nine months of fiscal 2007 were in North America while 34% were in Europe compared to 68% and 29% respectively in the first nine months of fiscal 2006. New license sales remained consistent at approximately 31% of total sales for the nine months ended June 30, 2007, while professional service revenue increased as a percentage of revenue from 15% for the first three quarters of fiscal 2006 to 17% in fiscal 2007. In addition, the Company's recurring maintenance revenue for the nine months ended June 30, 2007 represented 47% of its overall sales or \$5.4 million for the period as compared to 50% and \$5.3 million for the nine months ended June 30, 2006.

Gross profits for the first nine months of fiscal 2007 were down 2% to 81% of sales as compared to the first nine months of fiscal 2006. The decrease was primarily the result of a higher mix of third party software products sold in Europe.

Sales and marketing expenses consist primarily of salaries and related expenses of the Company's sales and marketing personnel, marketing activities including trade show attendance; outbound telemarketing; print advertising in major publications; white paper placement and other web based initiatives. Sales and marketing expenses were \$4.4 million for the first nine months of the year as compared with \$7.4 million for the same period in the prior year, a decrease of approximately 40%. New investment in marketing is closely aligned with corporate priorities, aligning internal resources to address validated market opportunities qualified in fiscal 2007.

Product research and development expenses consist primarily of costs relating to the development of Xenos' proprietary technology, including salaries and related costs of personnel directly engaged in these activities, and direct materials. Total expenditures on product development, including amounts deferred, for the first nine months of the year were \$2.42 million as compared to \$2.81 million for the same period last year, a decrease of 13.8%. During the first nine months of fiscal 2006, the Company engaged a number of contract workers and in temporary help to assist in product development activities. Historically, financial expenditures in this area have been held relatively steady on a year over year basis notwithstanding our focus and commitment to continued product development.

Administrative and general expenses primarily include: salaries and related expenses (including benefits and payroll taxes) of the Company other than salaries and related expenses paid to personnel engaged in research and development, professional services and sales and marketing activities; facility costs, professional fees, insurance costs and public company costs. In addition, the Company allocates common costs to each department based on relative headcount or other relevant measures. These costs include rent and other facility-related costs, communication and infrastructure expenditures.

The Company incurred administrative and general expenses during the nine months ended June 30, 2007 of \$1.65 million as compared to \$1.69 million in the nine months ended June 30, 2006. The 2% decrease was primarily a result of the restructuring efforts at the end of fiscal 2006.

The Company sells software and services in U.S. dollars, U.K. pound sterling and other currencies while maintaining its primary base of business operations and source of operating expenses in Canada. These factors give rise to the risk that its income, cash flows and the value of assets held in U.S. dollars and U.K. pound sterling may be adversely impacted by fluctuations in foreign exchange rates. The company uses natural hedges to mitigate the effects of such fluctuations and to the extent possible will from time to time, enter into foreign exchange forward contracts to manage foreign exchange risk. Foreign exchange losses were \$550,000 for the first nine months of fiscal 2007 as compared to a gain of \$76,000 in the same period last year.

Interest and other was \$152,000 as compared to \$240,000 in the previous year. The decrease was primarily due to interest paid on lower account balances and a loss incurred on the disposal of furniture and equipment during Q1 of fiscal 2007.

The Company incurred minimal tax charges in the period as compared to a tax expense of \$498,000 for the nine months ended June 30, 2006. The prior year's expense related to lower utilization of tax loss carry-forwards.

Quarterly Results

The following table provides a summary of certain financial information of Xenos for each of the eight most recently completed fiscal quarters:

(\$000's except per share amounts)

	Quarters Ended							
	June 30 2007	Mar 31 2007	Dec 31 2006	Sept 30 2006	June 30 2006	Mar 31 2006	Dec 31 2005	Sept 30 2005
Sales	\$3,803	\$3,720	\$3,931	\$3,327	\$3,767	\$3,128	\$3,619	\$3,231
EBITDA (i)	385	234	226	(622)	(785)	(1,316)	(828)	17
Net (loss) income (ii)	(378)	(340)	16	(7,934)	(1,374)	(1,734)	(927)	(341)
Net (loss) income per share (ii)								
Basic	(\$.04)	(\$.03)	\$0.002	(\$0.79)	(\$0.14)	(\$0.18)	(\$0.09)	(\$0.04)
Diluted	(\$0.04)	(\$0.03)	\$0.002	(\$0.79)	(\$0.14)	(\$0.18)	(\$0.09)	(\$0.04)

(i) – EBITDA - is a non-GAAP measure and is calculated by adding reorganization costs, amortization, and interest and bank charges back to losses before undernoted items on the consolidated statements of operations.

(ii) – Net (loss) income is equivalent to (loss) income from continuing operations for the periods disclosed as there were no discontinued operations or extraordinary items.

Fluctuations in quarterly revenue are primarily a result of timing of larger new enterprise licensing sales and service opportunities. In addition, revenue has been negatively affected by the decline in the U.S. dollar as a majority of the Company's sales are in U.S. denominated currency.

Net losses increased significantly between October 1, 2005 and September 30, 2006 as a result of a significant investment in marketing related expenses including increased personnel and lead focused marketing programs. New investment in marketing was significantly reduced subsequent to September 30, 2006 as were staffing levels resulting in decreases in operating expenditures and decreases in losses.

For the three months ended September 30, 2006, the Company performed an assessment on goodwill associated with the acquisitions of Rush Creek and XML Global for potential impairment and determined that a non-cash write-down of \$6,375,000 for goodwill was necessary. The triggering event that gave rise to the impairment was the continued losses and lack of significant revenue growth over the previous two years.

For the three months ended March 31, 2007, Net (loss) income was impacted by the right-sizing efforts of the company resulting in a restructuring charge of \$206,000.

For the three months ended June 30, 2007, Net (loss) income was significantly impacted by the decline of both the U.S. dollar and the U.K. pound sterling against the Canadian dollar. The company reported a \$523,000 foreign exchange loss in the period.

LIQUIDITY AND CAPITAL RESOURCES

During the first two quarters of fiscal 2007, the Company implemented measures in the form of senior management changes, reduced marketing expenditures and reduced staffing levels in an effort to enhance the operating efficiency of the Company and to reduce or eliminate the drain on its cash resources. As at June 30, 2007, cash and short-term investments stood at \$7.59 million (September 30, 2006 - \$7.31 million) or \$0.76 per common share (i).

The Company currently has an operating line of credit of \$1.0 million of which \$500,000 (September 30, 2006 - \$ 500,000) was unused, bearing interest at bank prime. The Company continues to have no long-term debt other than a small obligation relating to capital leases.

Capital expenditures for the nine months ended June 30, 2007 were \$180,000 versus \$329,000 for the nine months ended June 30, 2006. The expenditure levels in fiscal 2006 were significantly higher as a result of the need to enhance the Company's network infrastructure and to replace computer equipment. It is expected that the level of expenditure for fiscal 2007 will continue to be lower than fiscal 2006 expenditures.

Development costs capitalized for the nine months ended June 30, 2007 were \$161,000 as compared to \$297,000 in the corresponding period last year and represent the internal development costs relating to specific products as required by Canadian GAAP. As the product lines mature there is less opportunity for new development and more time directed toward product enhancements. The result is a decrease in development costs eligible for capitalization.

The Company anticipates that its current cash reserves and available credit facilities will be sufficient to fund its anticipated cash requirements for working capital and capital expenditures for at least the next 12 months. If the Company is required to raise additional funds for rapid expansion of its businesses or technologies, it could potentially issue equity or convertible debt which would cause current shareholders to experience dilution.

Outstanding Share Data

The authorized share capital of the company consists of an unlimited number of Common shares. As at August 3, 2007, there were 9,936,944 shares issued and outstanding. Stock options for a total of 661,250 shares were outstanding at exercise prices ranging from \$1.26 to \$4.36 with various expiry dates, the latest of which is May 2012.

Commitments and Contractual Obligations

As of June 30, 2007, the Company had future commitments and contractual obligations as summarized in the following table.

	Total	Less than 1 year	1-3 Years	4-5 years	After 5 years
Capital Lease Obligations	\$ 177,862	\$ 94,643	\$ 83,219	\$ -	\$ -
Operating Leases	2,493,012	449,312	684,036	636,651	723,013
Purchase Obligations	182,457	152,172	30,285	-	-
Total Contractual Obligations	\$2,853,331	\$ 696,127	\$797,540	\$ 636,651	\$723,013

Payments Due by Period

Critical Accounting Policies and Estimates

The preparation of the Consolidated Financial Statements and the related notes require by necessity, that the Company make estimates and judgments. The Company reviews its estimates, including those related to revenues, bad debts, acquired intangibles, deferred development, income taxes, contingencies and litigation. These estimates are based on historical experience and other assumptions believed to be reasonable under the circumstances. Under different assumptions, the reported results will differ, potentially materially, from those previously estimated. Many of the conditions impacting these assumptions and estimates are outside the Company's control.

The Company believes the following critical accounting policies reflect its more significant judgments and estimates.

Revenue

In accordance with Canadian GAAP, license revenue is recognized when persuasive evidence of an arrangement exists, delivery has occurred, the fee is fixed and determinable, and collectibility is probable. The terms of each contract can vary but the Company endeavors to apply consistent and appropriate treatment to each based on available literature, professional judgment and consultation with its external auditors where deemed necessary.

Allowance for Doubtful Accounts

The Company provides for an allowance for doubtful accounts to reasonably provide for losses resulting from the inability of its customers to make required payments.

Valuation of Intangible Assets

The carrying values of acquired intangibles are compared to their fair value at least annually to determine if a permanent impairment exists, at which time the impairment would be recorded as a charge to earnings. Valuations are inherently subjective and necessarily involve judgments and estimates regarding future cash flows and other operational variables.

Deferred Development

Development costs are deferred only as they relate directly to new products or functionality and where technological feasibility has been established. These deferred amounts are amortized following general release of the products over their estimated useful lives. The assets are also periodically reviewed for impairment by comparison to the expected future undiscounted cash flows that they are expected to generate.

Income, Sales & Other Taxes

Accounting for income taxes, in particular the future benefit of available loss carry forwards is subjective by nature and requires the exercise of judgment. Tax assets are determined using a consistent model which incorporates estimated future earnings, expiry of loss carry forwards and the estimated probability of realization.

Income taxes are framed within a transfer pricing model in which the Canadian parent owns all intellectual property of the software products, the U.S. subsidiary is a service

provider and the U.K. subsidiary is a value-added reseller. The model is supported by contemporaneous documentation and advice from independent transfer pricing consultants.

Sales tax practices vary widely in the various jurisdictions into which we sell our products and services. This area requires the exercise of judgment in respect of applicability and determination of rates. The Company has a review process that is applied to every customer billing and also performs regular analytical reviews to assess its compliance from an overall perspective.

Stock-based Compensation

In accordance with new Canadian GAAP requirements, stock options are required to be expensed and incorporated into the financial statements as per certain transitional timelines (See Notes to Annual Consolidated Financial Statements). The Company uses the Black-Scholes model to establish the fair value of the options granted. The calculation requires the estimation of certain inputs including expected volatility, risk-free interest rates and expected lives of the specific grants.

Litigation

With respect to legal proceedings, the Company assesses the likelihood that a loss will result, as well as the amount of such loss. The financial statements provide for the Company's best estimate of such losses as applicable.

Disclosure Controls and Procedures

As required by Multilateral Instrument 52-109 issued by the Canadian Securities Administrators, the Chief Executive Officer and Chief Financial Officer will be making certifications related to the information in the annual and interim filings. As part of these certifications, the Chief Executive Officer and Chief Financial Officer must certify that they are responsible for establishing and maintaining disclosure controls and procedures and have designed such disclosure controls and procedures to ensure that material information of Xenos is made known to them and that they have evaluated the effectiveness of the disclosure controls and procedures as of the end of the period covered by these annual and interim filings. The Company has documented and implemented such controls and procedures.

Evaluation of Disclosure Controls and Procedures

The Company's Chief Executive Officer and Chief Financial Officer, after evaluating the effectiveness of the disclosure controls and procedures as at June 30, 2007, have concluded that, as at June 30, 2007, the Company's disclosure controls and procedures were effective.

Internal Controls and Procedures

The Company maintains a set of internal controls over financial reporting which have been designed to provide reasonable assurance regarding the reliability of financial reporting and the preparation of financial statements in accordance with Canadian GAAP. The Company evaluated the design of its internal controls and procedures as defined under Multilateral Instrument 52-109 for the nine months ended June 30, 2007. This evaluation was performed by the Chief Executive Officer and the Chief Financial Officer with the assistance of other Company employees to the extent necessary and appropriate.

Evaluation of Internal Controls and Procedures

The Company's Chief Executive Officer and Chief Financial Officer, after evaluating the effectiveness of the internal controls and procedures as at June 30, 2007, have concluded that, as at June 30, 2007, the Company's internal controls and procedures were effective.

There were no changes in the Company's internal control over financial reporting that occurred during the first nine months that have materially affected, or are reasonably likely to materially affect the Company's internal control over financial reporting.

Corporate Governance

The Company's Board of Directors includes a majority of independent Directors and its Committees include Audit, Compensation, Nominating/Corporate Governance and Disclosure.

The members of the Audit Committee are all independent Board members and are financially literate. The Committee meets regularly to approve the release of financial information including the MD&A and also to oversee relations with auditors and stewardship issues including compliance with new regulatory requirements.

Key Performance Drivers

In addition to traditional GAAP financial statements, Management monitors numerous key performance indicators (KPI's) to assist in running the business. Some of these include sales pipeline, lead generation, response from internet based marketing initiatives, maintenance renewal rates, average deal sizes, revenue by channel and component, professional services utilization rates, costs by department and attrition rates. These factors revolve around building an infrastructure that is scalable and which drives profitability at a rate that exceeds top line revenue growth.

Workplace Environment and Compensation Structures

The Company has designed compensation structures aligned to shareholder interests. Bonus allocations are largely driven by company financial performance, depending on job function, and amounts earned under the plan are placed into departmental pools and allocated to individuals based entirely on merit. The workplace culture of the organization is one in which outstanding performance is rewarded and management time is heavily focused on empowering the success of "A" players rather than incrementally improving the performance of "C" players.

Outlook

The Company's strategy for creating value for shareholders is to drive sustainable and significant top line growth for each of its product lines, and increasingly for its overall market offering of "end to end" solutions particularly in its key vertical markets, banking and insurance. Further value will be gained by aligning the structure of the distribution channel accordingly, protecting the recurring revenue base and ultimately driving scalable long-term profitability. The Company will increase its revenue per employee and attain profitability through focused growth oriented activities and cost containment.

Additional information regarding the Company is available on SEDAR at www.sedar.com.

Footnotes:

- (i) Cash per share is a non-GAAP measure and is calculated by dividing the cash and short term investments by the number of common shares outstanding.

Forward Looking Information

Certain information provided by Xenos in this Management's Discussion and Analysis, in the Annual Report and in other documents publicly filed throughout the year that are not recitation of historical facts may constitute forward-looking statements. The words "may", "would", "could", "will", "likely", "estimate", "believe", "expect", "plan", "forecast" and similar expressions are intended to identify forward-looking statements. Readers are cautioned that such statements are only predictions and the actual events or results may differ materially. In evaluating such forward-looking statements, readers should specifically consider the various factors that could cause actual events or results to differ materially from those indicated by such forward-looking statements.

Such forward-looking information may involve important risks and uncertainties that could materially alter results in the future from those expressed or implied in any forward-looking statements made by, or on behalf of, Xenos. Some of the factors and risks and uncertainties that cause results to differ from current expectations discussed in this Management's Discussion and Analysis and elsewhere in the Quarterly Report include, but are not limited to, dependence upon growth in the market for the Company's products, delays in product launches, currency exposure, technology developments by Xenos' competitors and changes in the competitive environment in which Xenos operates.

The foregoing is not an exhaustive list of the factors that may affect Xenos' forward-looking statements. These and other factors should be considered carefully and readers should not place undue reliance on Xenos' forward-looking statements. Xenos assumes no obligation to update the forward-looking statements, or to update the reasons why actual results could differ from those reflected in the forward-looking statements.

NOTICE OF NO AUDITOR REVIEW OF INTERIM FINANCIAL STATEMENTS

Under National Instrument 51-102, part 4, subsection 4.3(3)(a), if an auditor does not perform a review of the interim financial statements, they must be accompanied by a notice indicating that the financial statements have not been reviewed by an auditor.

The accompanying interim consolidated financial statements of the Corporation have been prepared by and are the responsibility of the Corporation's management.

The corporation's independent auditor has not performed a review of these financial statements in accordance with standards established by the Canadian Institute of Chartered Accountants for a review of interim financial statements by an entity's auditor.

Xenos Group Inc.
Consolidated Statements of Operations
(Unaudited)

	Three Months Ended June 30		Nine Months Ended June 30	
	2007	2006	2007	2006
Sales	\$ 3,802,513	\$ 3,767,266	\$ 11,453,762	\$ 10,514,057
Cost of sales	697,680	571,673	2,173,738	1,780,858
Gross profit	3,104,833	3,195,593	9,280,024	8,733,199
Expenses				
Sales and marketing	1,512,019	2,716,212	4,441,831	7,373,399
Research and development	689,854	800,531	2,256,725	2,508,571
Administration and general	496,187	425,313	1,654,965	1,690,344
Reorganization costs	-	-	206,016	-
Amortization	292,070	333,702	872,184	886,976
Stock based compensation	21,536	39,104	81,656	89,792
Interest and bank charges	12,780	11,525	41,370	37,173
	3,024,446	4,326,387	9,554,747	12,586,255
Income (loss) before undernoted items	80,387	(1,130,794)	(274,723)	(3,853,056)
Interest and other	71,668	81,661	151,664	240,088
Foreign exchange (loss) gain	(523,220)	(43,833)	(550,430)	75,560
	(451,552)	37,828	(398,766)	315,648
Loss before income taxes	(371,165)	(1,092,966)	(673,489)	(3,537,408)
Provision for income taxes	6,724	281,012	28,480	497,531
Net loss	\$ (377,889)	\$ (1,373,978)	\$ (701,969)	\$ (4,034,939)
Net loss per common share				
- Basic	\$ (0.04)	\$ (0.14)	\$ (0.07)	\$ (0.41)
- Fully diluted	\$ (0.04)	\$ (0.14)	\$ (0.07)	\$ (0.41)
Weighted average number of shares				
- Basic			9,936,944	9,936,188
- Fully diluted			9,936,944	9,936,188
<hr/>				
Deficit, beginning of year			\$ (36,573,188)	\$ (24,603,941)
Net loss			(701,969)	(4,034,939)
Deficit, end of period			(37,275,157)	(28,638,880)

Xenos Group Inc.
Consolidated Balance Sheets
(Unaudited)

	As at	
	June 30 2007	September 30 2006
ASSETS		
CURRENT		
Cash and short term investments	\$ 7,593,876	\$ 7,308,177
Trade receivables	2,245,243	2,103,212
Other receivables	15,233	3,085
Prepays	536,272	689,491
Income taxes recoverable	11,316	7,204
	<u>10,401,940</u>	<u>10,111,169</u>
LONG TERM		
Future income taxes	1,157,357	1,164,566
Capital assets	1,170,000	1,346,041
Intangibles and other assets	2,046,742	2,470,274
	<u>4,374,099</u>	<u>4,980,881</u>
TOTAL ASSETS	<u>\$ 14,776,039</u>	<u>\$ 15,092,050</u>
LIABILITIES		
CURRENT		
Bank indebtedness	\$ 500,000	\$ 500,000
Payables and accruals	1,834,048	2,307,340
Income taxes payable	11,943	8,095
Deferred revenue	4,039,793	3,261,751
Current portion - capital lease obligations	89,030	64,893
	<u>6,474,814</u>	<u>6,142,079</u>
LONG TERM		
Capital lease obligations	84,371	95,252
Deferred revenue	15,003	13,371
Deferred lease inducements	154,264	173,448
	<u>253,638</u>	<u>282,071</u>
TOTAL LIABILITIES	6,728,452	6,424,150
SHAREHOLDERS' EQUITY		
Capital stock (Note 3)	44,969,035	44,969,035
Contributed surplus (Note 4)	353,709	272,053
Deficit	(37,275,157)	(36,573,188)
TOTAL SHAREHOLDERS' EQUITY	<u>8,047,587</u>	<u>8,667,900</u>
TOTAL LIABILITIES & EQUITY	<u>\$ 14,776,039</u>	<u>\$ 15,092,050</u>

Xenos Group Inc.
Consolidated Statements of Cash Flows
(Unaudited)

	Three Months Ended June 30		Nine Months Ended June 30	
	2007	2006	2007	2006
Operating activities				
Net loss	\$ (377,889)	\$ (1,373,978)	\$ (701,969)	\$ (4,034,939)
Amortization	292,070	333,702	872,184	886,976
Loss on disposal of capital assets	238	3,325	68,075	3,325
Future income taxes	16,036	276,724	7,209	450,469
Stock based compensation	21,536	39,104	81,656	89,792
Change in non-cash working capital	198,408	(710,633)	285,974	189,827
	150,399	(1,431,756)	613,129	(2,414,550)
Financing activities				
Capital lease payments	(21,892)	(9,929)	(62,479)	(29,218)
Proceeds on issue of shares	-	-	-	4,950
	(21,892)	(9,929)	(62,479)	(24,268)
Investing activities				
Additional consideration paid on acquisitions	-	(4,348)	-	(72,036)
Purchase of capital assets	(48,581)	(74,377)	(104,563)	(328,563)
Proceeds on disposal of capital assets	873	-	873	-
Development costs incurred	(20,402)	(73,906)	(161,261)	(297,022)
	(68,110)	(152,631)	(264,951)	(697,621)
Net increase (decrease) in cash and short term investments	60,397	(1,594,316)	285,699	(3,136,439)
Cash and short term investments				
Beginning of period	7,533,479	10,491,618	7,308,177	12,033,741
End of period	\$ 7,593,876	\$ 8,897,302	\$ 7,593,876	\$ 8,897,302

Xenos Group Inc.

Notes to the Condensed Consolidated Financial Statements

June 30, 2007 and 2006

1. Basis of presentation

The unaudited consolidated interim financial statements are prepared in accordance with Canadian generally accepted accounting principles and follow the same accounting policies and methods of their application as at the most recent audited annual financial statements for the year ended September 30, 2006. These financial statements should be read in conjunction with the audited annual financial statements for the year ended September 30, 2006.

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, including the recording of loss carry-forwards. 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.

Revenue recognition

The Company recognizes revenue on the delivery of software licenses when persuasive evidence of an arrangement exists, the fees are fixed and determinable, collection is considered probable, and vendor-specific objective evidence exists to allocate the total fee to the different elements of an arrangement. Customization and implementation revenues are recognized as the services are rendered. Revenue from maintenance services for licenses sold is recognized ratably over the term of the maintenance contract, after ratification thereof.

3. Capital stock

	June 30, 2007		September 30, 2006	
	Number	Amount	Number	Amount
Balance, beginning of year	9,936,944	\$ 44,969,035	9,933,944	\$ 44,964,085
Issued pursuant to exercise of vested stock options	-	-	3,000	4,950
Balance, end of period	9,936,944	\$ 44,969,035	9,936,944	\$ 44,969,035

4. Contributed surplus

	June 30 2007	September 30 2006
Balance, beginning of year	\$ 272,053	\$ 148,638
Stock based compensation	81,656	123,415
Balance, end of period	<u>\$ 353,709</u>	<u>\$ 272,053</u>

5. Supplemental cash flow information

	June 30 2007	June 30 2006
(a) Change in non-cash operating working capital:		
Receivables	\$ (154,179)	\$ (688,155)
Prepays	153,219	132,232
Income taxes recoverable	(4,112)	-
Payables and accruals	(473,292)	291,835
Income taxes payable	3,848	3,588
Deferred lease inducements	(19,184)	16,061
Deferred revenue	779,674	434,266
	<u>\$ 285,974</u>	<u>\$ 189,827</u>
b) Cash and short term investments consist of cash on hand, balances with banks, cash equivalents and short term investments		
(c) Interest paid	\$ 41,371	\$ 37,174
(d) Income taxes paid (net of recoveries)	\$ 15,322	\$ 7,598

6. Commitments

The Company has entered into future commitments and contractual obligations for operating leases, capital leases and certain purchase obligations. Minimum payments in aggregate and for each of the next five years are as follows:

2008	\$ 696,127
2009	437,156
2010	360,384
2011	329,736
2012	306,915
Thereafter	723,013
	<u>\$ 2,853,331</u>

7. Reorganization costs

During the second quarter of fiscal 2007, the Company incurred a reorganization charge of \$206,016, which included a 13% reduction in headcount and the relocation of the remaining US based head office management functions to Toronto. Of this amount, \$45,860 relates to the loss incurred on disposal of excess capital equipment. The total reorganization costs paid during the nine month period ended June 30, 2007 was \$544,352 and includes amounts paid in connection with the reorganization charge incurred during the fourth quarter of fiscal 2006.

8. Stock based compensation plan

The Company has a stock option plan which allows the granting of stock options to employees and service providers up to an aggregate of 1.6 million common shares. Under current company practice the options, which have a five-year term, vest immediately for directors and generally over 3-4 years for all others, commencing on the grant date. The exercise price of each option equals the closing market price of the Company's common shares on the last trading day preceding the date of grant.

A summary of the status of the Company's stock option plan as of June 30, 2007 and September 30, 2006 and any changes during each year-to-date period is presented below:

	Shares		Weighted Average Exercise Price	
	June 30 2007	September 30 2006	June 30 2007	September 30 2006
Outstanding, beginning of year	1,096,138	958,138	\$ 1.87	\$ 2.14
Granted	170,000	544,000	1.78	1.66
Exercised	-	(3,000)	-	1.65
Forfeited	<u>(604,888)</u>	<u>(403,000)</u>	1.88	2.22
Outstanding, end of quarter	<u>661,250</u>	<u>1,096,138</u>	\$ 1.84	\$ 1.87
Options exercisable at quarter end	<u>172,250</u>	<u>364,638</u>		

8. Stock based compensation plan (continued)

The following information applies to options outstanding at June 30, 2007:

Exercise Price	Number outstanding and exercisable	Number outstanding but not exercisable	Weighted average remaining life in months	Weighted average exercise price	Expiry
\$ 1.26	5,000	-	52	\$ 1.26	October, 2011
1.29	-	225,000	51	1.29	September, 2011
1.34	-	25,000	51	1.34	September, 2011
1.35	-	25,000	55	1.35	January, 2012
1.65	62,500	-	6	1.65	December, 2007
1.65	15,000	-	56	1.65	February, 2012
1.85	-	50,000	57	1.85	April, 2012
1.90	12,000	-	43	1.90	January, 2011
1.90	-	50,000	58	1.90	May, 2012
1.99	-	79,000	45	1.99	March, 2011
2.00	-	25,000	58	2.00	May, 2012
2.20	6,000	-	9	2.20	March, 2008
2.35	14,000	-	32	2.35	February, 2010
3.60	7,500	2,500	17	3.60	November, 2008
3.80	41,250	7,500	16	3.80	October, 2008
4.36	9,000	-	21	4.36	March, 2009

9. Segmented information

The Company has determined that it serves one industry segment, information technology.

Geographic information

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

	Sales		Capital Assets	
	Nine Months Ended		As at	
	June 30 2007	June 30 2006	June 2007	September 2006
Canada	\$ 496,545	\$ 698,611	\$ 863,430	\$ 910,547
Europe	1,097,750	1,133,980	7,463	7,026
United Kingdom	2,761,224	1,916,481	257,656	290,668
United States	6,793,442	6,439,758	41,451	137,800
Other	304,801	325,227	-	-
	<u>\$11,453,762</u>	<u>\$ 10,514,057</u>	<u>\$ 1,170,000</u>	<u>\$ 1,346,041</u>

10. Comparative figures

Certain of the comparative figures have been reclassified to conform to the financial statement presentation adopted in the current year.

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This report contains forward-looking statements based on current expectations. These forward-looking statements entail various risks and uncertainties that could cause actual results to differ materially from those reflected in these forward-looking statements. Risks and uncertainties about the Company's business are more fully discussed in the Management Discussion and Analysis published in the Company's annual report.

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Trading

Xenos Group Inc. trades on
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