Management's Discussion & Analysis

For the fiscal year ended May 31, 2021

BIOQUAL, INC.

Prepared by:

David Newcomer
Chief Financial Officer

MANAGEMENT'S DISCUSSION AND ANALYSIS

Items of Note

In fiscal year 2021, which ended on May 31, 2021, the Company realized net income of $6,326,825 compared to net income of $4,230,938 for fiscal year 2020, for reasons discussed in the results of operations section below.

During the first quarter of fiscal year 2021, the National Institute of Allergies and Infectious Diseases (NIAID) provided $238,225 of additional funding for the existing task order "Refinement of a Pig-Tail Macaque Model of Gonococcal Infection" under Part B of the Pre-Clinical Models of Infectious Diseases (PCMID) Master Contract. The additional funds increase the total amount of the task order from $2,461,275 to $2,699,500. The contract period of performance end date was September 30, 2020. There are, however, no assurances that the Company will be awarded any other task orders under the PCMID Master Contract.

During the second quarter of fiscal year 2021, the NIAID provided $8,125,898 of incremental funding for the first option year of the contract entitled "Animal Care and Laboratory Support Services to the Vaccine Research Center." Additionally, subsequent to the end of the fiscal year, the NIAID provided $681,000 of funding to purchase a needed PET/CT machine for use on the contract. The seven-year contract has a maximum potential funding amount of $69,174,672 including all options. The cumulative funding of the contract increased from $7,883,552 to $16,690,450. The incremental funding covers costs incurred from September 28, 2020, through September 27, 2021. There are, however, no assurances that any other options will be exercised under this contract.

On October 21, 2020, the Company held its Annual Meeting of Shareholders (the "Annual Meeting"). Set forth below are the proposals voted upon at the Annual Meeting and the final voting results.

As of the close of business on September 1, 2020, the record date for the Annual Meeting, 894,416 shares of the Company's common stock, par value $0.01 per share (the "Common Stock"), were outstanding and entitled to vote. 859,997 shares of Common Stock were voted in person or by proxy at the Annual Meeting, representing 96.2% percent of the shares entitled to be voted.

Proposal 1 – Election of Directors. The Company's shareholders elected each of the directors listed below to serve on the Board until the Company's next Annual Meeting of shareholders or until their successors have been duly elected or appointed, as set forth below.

Director	For	Withheld	Non Votes
Mark G. Lewis, Ph.D.	799,431	5,716	54,850
Charles C. Francisco	799,481	5,666	54,850
Charles F. Gauvin	799,481	5,666	54,850
Michael P. O'Flaherty	799,431	5,716	54,850
David B. Landon, Ph.D.	804,431	716	54,850
Vivek R. Shinde Patil, Ph.D.	804,381	766	54,850

Proposal 2 – To Approve a Proposal for the Establishment of a Stock Incentive Plan. The Company's shareholders approved the establishment of the 2020 Stock Incentive Plan.

For	Against	Abstain	Non Votes
783,325	20,512	1,310	54,850

Proposal 3 – Ratification of Independent Auditors. The Company's shareholders ratified the Company's selection of Aronson LLC to serve as the Company independent auditors for the fiscal year ending May 31, 2021.

For	Against	Abstain
844,112	7,004	8,881

Based on fiscal year 2020 earnings, the Board of Directors declared a cash dividend of $1.10 per share for shareholders of record on September 28, 2020. The dividend was paid on October 21, 2020. This amount is $.40 per share greater than the $.70 per share cash dividend paid on October 16, 2019.

On November 25, 2020, the Board determined that it would be in the best interest of the Company's shareholders and therefore resolved to amend the Stock Incentive Plan by reducing the number of shares that may be issued pursuant to the Plan from 500,000 to 180,000 shares of the Company's common stock and to increase the percentage of shares that may be issued as Incentive Stock Options from 5 percent of the then issued and outstanding common stock of the Company to 20 percent of such common stock. The amendments described above are subject to the approval by a majority of the Company's shareholders within 12 months of the resolution.

During the fourth quarter of fiscal year 2021, the NIAID provided $595,216 of incremental funding for the first option year of two task orders awarded under the contract entitled "Simian Vaccine Evaluation Units (SVEUs)." The seven-year contract has a maximum potential funding amount of $6,682,071 including all options. The cumulative funding of the contract increased from $579,882 to $1,175,098. The incremental funding covers costs incurred from April 1, 2021, through March 31, 2022. Subsequent to the end of the fiscal year, the NIAID awarded BIOQUAL with a third task order under this contract totaling $1,413,583 including all options. The current funding is $530,959 which covers costs from September 8, 2021, until March 8, 2024. There are, however, no assurances that any other options will be exercised or task orders awarded under this contract.

COVID-19

During fiscal year 2021, in collaboration with other organizations, BIOQUAL staff have been listed as co-authors of several peer reviewed articles in scientific journals. Certain data included in the articles were obtained during studies performed in our laboratories. Several of the articles are available for review on the Company's website (www.bioqual.com).

Over the past two fiscal years, the Company temporarily shifted its focus away from supporting AIDS, influenza and other infectious disease research to apply the majority of its resources to supporting the global need for vaccines and therapeutics to combat COVID-19. The Company continued to perform then on-going non-COVID-19 contracts; however, no new non-COVID 19 contacts were started during this time. Although the Company had a few non-COVID-19 contracts cancelled, the lost revenue was replaced by contracts related to potential COVID-19 vaccines and therapeutics. During the second quarter of fiscal year 2021, the Company began to re-initiate work with clients involved with in-vivo testing programs related to research efforts to develop vaccines and therapies against emerging diseases including AIDS, Zika, Chikungunya and others as well as influenza. The Company believes it has the capacity and resources to support all of these efforts simultaneously. Approximately 40% of the revenues generated this fiscal year were in support of COVID-19 related research.

Results of Operations

Results of Operations 2021 versus 2020

The $11,323,301 increase in revenues to $57,683,502, for fiscal year 2021, compared to $46,360,201 for fiscal year 2020, is primarily the result of increased activity in commercial contracts of approximately $14,609,000. Additionally, the revenue related to federal grants increased by approximately $94,000 compared to the previous fiscal year. The increases in revenue from commercial contracts and federal grants was partially offset by a decrease in revenue generated from government contracts of approximately $3,380,000 reflecting the expiration of six task orders during fiscal year 2021 with no new task orders pursuant to those contracts awarded during the fiscal year.

The $7,036,781 increase in contract operating expenses for fiscal year 2021, primarily reflects increases in expenses incurred of approximately $3,160,000 related to an increase in depreciation expense (resulting from the increase in capital expenditures in the current and previous fiscal years) and contract materials and supplies when compared to similar costs incurred in the previous fiscal year. Additionally, operations labor and related benefits costs increased approximately $4,970,000, reflecting the effect of continued hiring of staff to support the increasingly complex operational and regulatory issues involved in performing services for our clients as well as keeping pace with increased contract activity related to supporting COVID-19 research. The increase in contract operating expenses is partially offset by a decrease in contract related subcontractor costs of approximately $1,166,000 reflecting the fiscal year 2021 expiration of the federal contract which utilized subcontracted services.

The $1,051,818 increase in G&A expenses primarily reflects the increases in administrative labor and related benefits costs, consultants and temporary labor compared to the previous fiscal year. The increased labor costs (both employees and non-employee) reflect the increased administrative effort needed to keep pace with the increased contract activity related to supporting COVID-19 research.

The $3,234,702 increase in operating income primarily reflects the profits earned on a higher volume of commercial contracts during fiscal year 2021 compared to the prior fiscal year.

Liquidity and Capital Resources

During fiscal year 2021, the Company directed approximately $4,408,000 towards capital expenditures, compared to approximately $2,404,000 in fiscal year 2020. These expenditures were necessary to provide additional equipment and nonhuman primate (NHP) and rodent cages for research being performed in the Company's laboratories, including approximately $575,000 for items to support COVID-19 research contracts. The Company has been able to continue to fund all of these expenditures through the use of available cash provided by the Company's operations.

During fiscal year 2022, the Company estimates the aggregate purchase price of equipment to upgrade older equipment, enhance its capabilities, add NHP and small animal caging, and to continue renovating animal housing space will total approximately $1,650,000.

In addition to the $1,650,000 described in the previous paragraph, the Company estimates that it will purchase an additional $350,000 in infrastructure, cage washing, sanitation, and animal care equipment over the next three to nine months in connection with the construction of approximately 10,700 square feet of space in its 9600 Medical Center Dr. facility to be utilized as a vivarium for small animals. The construction phase is on-going. The total construction costs are currently estimated at between $3,500,000 and $4,000,000, of which, the Company incurred approximately $2,395,000 as of May 31, 2021. The estimated construction costs total does not include the $350,000 for equipment mentioned earlier in this paragraph. Management may fund the construction either by using its cash reserves or obtaining a construction loan or a combination of both. To date, all construction related costs have been paid using cash on hand.

The Company is obligated, as lessee, under non-cancelable operating leases covering its facilities and certain equipment at various dates through 2027. Rent expense for fiscal year 2021 was approximately $3,889,000. As of May 31, 2021, the total of the future minimum rental payments is approximately $16,666,000 through 2027.

During the first quarter of fiscal year 2021, the Company entered into a lease for 9,416 square feet of office space located at 9620 Medical Center Drive, Rockville, Maryland for a term of seven years and four months including an option for 5 additional years. The lease commenced on July 1, 2020, and the Company is utilizing this space to accommodate the expected continued growth of its staff and to provide adequate space for social distancing until the end of the COVID-19 pandemic.

Other than the items mentioned above, the Company does not anticipate substantial capital and other expenditures during fiscal year 2022. However, if the Company is awarded new contracts that require additional equipment or animal enclosures during that period, the Company believes it will have sufficient capital resources to provide for the purchase of the equipment.

BIOQUAL has a $2,000,000 line of credit with M&T Bank available to help cover costs of its daily operations. The line of credit is due on demand and renewable annually. As of May 31, 2021, there was no balance due on the line of credit. The interest rate on funds drawn on the line of credit is the prime rate plus .25%, which as of May 31, 2021, was 3.50%. On May 31, 2021, the Company had a balance of cash and cash equivalents of $7,719,702. With the above line of credit and the cash resources expected to be available as a result of collection of accounts receivable, the Company believes it will have sufficient capital resources to provide for daily operations and its capital needs through the end of fiscal year 2022.

The following provides additional information on select balance sheet items: 1) the $5,659,256 increase in accounts receivable primarily reflects the impact of the increased volume of commercial contracts activity compared to the end of the previous fiscal year. The increase in accounts receivable includes an increase in unbilled accounts receivable of $1,473,065 primarily reflecting an increase in services completed as of May 31, 2021, but not yet billed to clients as compared to services completed as of May 31, 2020, but not billed until fiscal year 2021; 2) the $651,597 decrease in cash surrender value of officers' life insurance reflects the collection of the proceeds from the surrender of a life insurance policy held for Dr. John Landon, who passed away on January 10, 2021; 3) the $368,378 decrease in accounts payable primarily reflects a lower amount of outstanding invoices for the purchase of nonhuman primates as compared to similar balances due on May 31, 2020; and 4) the $644,572 increase in accrued compensation and related liabilities primarily reflects bonuses accrued for performance of staff during the COVID-19 pandemic and an increase in accrued payroll for the final payroll in May 2021 compared to the final payroll in May of fiscal year 2020.

Over the past year, to keep up with the increased number of contracts and the increased complexity of the COVID related contracts, the Company has increased its workforce by approximately 25%. Coupled with the increased number of employees, in order to compete with the other laboratories seeking a similar workforce, the Company has had to alter its salary structure by increasing the pay rates of certain labor categories to attract and retain employees needed to enable the Company to meet the increased demand for its services. To date, the Company has been relatively successful in acquiring sufficient staffing to keep up with contract demand. There are, however, no assurances that the Company will be able to continue to hire a sufficient number of employees to meet future contract demand.

In response to the effects on the economy of COVID-19, the Company continues to stay in contact with its critical suppliers to ensure the continued delivery of necessary materials to keep our employees safe and healthy at the workplace as well as to continue to provide animal husbandry and required procedures for its clients. To date, the Company has been able to procure adequate quantities of critical materials and supplies to continue operations. Based on market demand, the Company has had to pay higher prices for certain critical items which may have a short-term negative impact on the results of operations. There are, however, no assurances that BIOQUAL will be able to continue obtaining such critical materials without interruption.

A significant part of the research support services provided by BIOQUAL requires the use of nonhuman primates, which are becoming more and more difficult to procure in adequate quantities to satisfy the demand for continuing COVID-19 vaccine and therapeutics development as well as research of other infectious diseases. The Company is working closely with its suppliers and is committing (providing cash deposits) to the purchase of nonhuman primates as soon as they become available in order to have a pipeline of animals for future studies. China, a major breeder and supplier of nonhuman primates, ceased exporting nonhuman primates in 2020. The resumption of exporting nonhuman primates by China would help alleviate the shortage of this important component of infectious disease research; however, there is no assurance that this will happen, and a continued shortage of nonhuman primates could adversely affect the Company's ability to perform new projects

Refer to the Statements of Cash Flows on pages 7 and 8 of the Audited Financial Statements for the years ended May 31, 2021, and 2020, for further detail related to the changes in cash and cash equivalents.

Forward Looking Information

Statements herein that are not descriptions of historical facts are forward-looking and subject to risks and uncertainties. The forward-looking statements are neither promises nor guarantees, and you should not place undue reliance on these forward-looking statements because they involve known and unknown risks, uncertainties, and other factors, many of which are beyond the Company's control and which could cause actual results to differ materially from those expressed or implied by these forward-looking statements, including risks relating to the ability to continue to extend current government contracts; the Company's ability to obtain new government or commercial contracts; continued demand for the use of animal models in scientific research; the Company's ability to obtain sufficient numbers of animal models; the availability of adequate numbers of employees; the Company's ability to perform under its contracts in accordance with the requirements of the contracts; the actual costs incurred in performing the Company's contracts and its ability to manage its costs, including its capital expenditures; dependence on third parties; future capital needs; the ability to fund its capital needs through the use of its cash on hand and line of credit; and the future availability and cost of financing/capital sources to the Company.