Consolidated Financial Statements
(Expressed in U.S. dollars)

ELECTROFUEL INC.

Nine months ended June 30, 2001, with comparative
figures for nine months ended June 30, 2000
and Balance Sheet for September 30, 2000

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

The following discussion and analysis of our financial condition and results of operations should be read in conjunction with our financial statements and related notes. Our financial statements are presented in U.S. dollars. We prepare our financial statements in accordance with Canadian generally accepted accounting principles. We are transitioning from a late stage development company to an early stage commercial manufacturer.

This Quarterly Report may contain forward-looking statements that involve a number of risks and uncertainties, including statements regarding the outlook for the Company's business and results of operations. By nature, these risks and uncertainties could cause actual results to differ materially from those indicated. Such factors include, without limitation, the various factors set forth in the Management's Discussion and Analysis of this report and as discussed in public disclosure documents filed with Canadian regulatory authorities.

Electrofuel disclaims any intention or obligation to update or revise any forward-looking statements, whether as a result of new information, future events or otherwise.

Results of Operations

Nine months ended June 30, 2001 Compared to the Nine months ended June 30, 2000

Sales

Sales for the nine months ended June 30, 2001 were $635,091, $364,719 for the third quarter (149% greater than the second quarter) and $146,663 for the second quarter, consisting of sales of PowerPad 160 units to corporate customers, distributors, and individuals. This represents the beginning of the ramp up of production. Sales for the nine months ended June 30, 2000 were $11,279. We recognize revenue on the sale of commercial units produced at the time the units are shipped to customers.

Expenses

Start-up and Manufacturing. All of the material and labor costs associated with the production of the commercial units and the start-up costs of the plant have been charged to start-up and manufacturing expenses. The balance has been charged to research and development expenses. Cost of sales and gross margin information will be provided in fiscal 2002 financial reporting.

Research and Development. Research and development expenses consist primarily of compensation and related costs for research and development personnel, including independent contractors and consultants, direct materials and allocated overhead.

Research and development expenses, net of investment tax credits, increased from $759,531 for the nine months ended June 30, 2000 to $1.6 million for the nine months ended June 30, 2001. Research and development expenses were $626,523 for the third quarter and $600,259 for the second quarter of fiscal 2001. This increase in net research and development expenses reflects the higher costs associated with the development of our PowerPad 160 and 120 batteries for portable computers and mobile phone batteries for the communications market and includes the increased allocation of existing personnel to research and development efforts.

General and Administrative. General and administrative expenses include salaries and benefits for corporate personnel, professional fees and facilities expenses, net of any allocation to research and development activities. Our corporate administrative staff includes our executive officers and employees engaged in business development, financial planning and control, legal, human resources and corporate administration.

General and administrative expenses increased from $1.7 million for the nine months ended June 30, 2000 to $3.6 million for the nine months ended June 30, 2001. This increase reflects an increase in corporate staff, legal and consulting fees, depreciation expense and the settlement paid to a former officer upon surrender of his vested and unvested stock options. General and administrative expenses were $1.0 million for the third quarter and $1.7 million for the second quarter of fiscal 2001.

Sales and Marketing. Sales and marketing expenses increased from $484,710 for the nine months ended June 30, 2000 to $1.1 million for the nine months ended June 30, 2001. This reflects an increase in marketing, personnel, trade shows, advertising and other costs associated with marketing activities of our PowerPad 160 and 120 products and increasing the awareness of our products and technology. Sales and marketing expenses were $394,751 for the third quarter and $350,604 for the second quarter of fiscal 2001.

Other Expense (Income)

Our other expense (income) has been derived primarily from the provision of consulting, development and engineering support services to third parties net of related expenses.

Interest Income

Interest income increased from $760,199 for the nine months ended June 30, 2000 to $1.5 million for the nine months ended June 30, 2001. We derived interest in both periods from cash and short-term investments. This increase primarily reflects the additional interest derived from the unused portion of the proceeds from our January 2000 special warrant financing and the November 2000 public offering of shares.

Foreign Exchange Gain or Loss

The foreign exchange gain decreased from $501,943 for the nine months ended June 30, 2000 to $134,634 for the nine months ended June 30, 2001. This was due primarily to the US dollar increasing relative to the Canadian dollar from June 2000 to June 2001. The exchange rate as at June 30, 2000 was $1.4798 and as at June 30, 2001 was $1.5175. In the third quarter there was an exchange loss of $372,780 reflecting a drop in the exchange rate from $1.5784 in March to $1.5175 in June.

Liquidity and Capital Resources

As of June 30, 2001, we had $35.0 million in cash, cash equivalents and short-term investments.

Net cash used in operating activities was $1.6 million for the nine months ended June 30, 2000 and $4.0 million for the nine months ended June 30, 2001. Net cash used in operating activities for the nine months ended June 30, 2001 reflects the operating loss of $4.8 million offset by amortization of $397,788 and a decrease in non-cash working capital of $346,175. The decrease in non-cash operating working capital was principally attributable to a decrease in deferred finance charges relating to the public offering of shares, partly offset by a decrease in accounts payable and accrued liabilities and an increase in inventory. Net cash used in operating activities was $2.7 million in the third quarter of fiscal 2001 and $888,350 in the second quarter. Net cash used in operating activities for the third quarter reflects the operating loss for the period of $2.2 million offset by amortization of $142,210 and an increase in non-cash working capital of $712,796. The increase in non-cash operating working capital is attributable to increases in goods and services tax receivable, inventories and accounts receivable offset by decreases in prepaid expenses and other.

Cash provided by financing activities was $28.3 million for the nine months ended June 30, 2001, compared to $28.4 million for the nine months ended June 30, 2000. These financing activities consisted primarily of private placements of our securities in January 2000 and the public offering of shares in November 2000.

Cash used in investing activities was $18.2 million for the nine months ended June 30, 2000 as compared to $25.1 million for the nine months ended June 30, 2001. Cash used in investing activities reflects $8.9 million of spending for building improvements, and machinery and equipment for the Mississauga plant and net additions to short-term securities of $16.2 million.

We have recorded net losses in every year since our inception. As we continue to make investments in product development and marketing activities, we expect to incur net losses at least through our fiscal year ending September 30, 2001. In the current and future quarters, we expect significant increases in expenses in all categories.

We expect research and development expenses to increase as we continue to develop our portable computer and mobile telephone battery product lines and explore other potential applications for our technology. We also expect our sales and marketing and general and administrative expenses to increase as we expand our capabilities in these areas and increase our corporate infrastructure to support the growth of our business in anticipation of high volume production. We currently plan to fund these expenses with cash on hand.

We have not yet received significant revenue from the sale of our batteries. Since June 2000, we have sold limited quantities of the PowerPad 160. After we begin larger scale commercial production of our PowerPad products, we expect that our principal source of revenue will be the sale of our battery products. Initially, we expect that our sales will be concentrated among a limited number of customers.

We expect we will continue to experience negative cash flow in the future. We expect that our capital expenditures will continue to increase significantly in the future as we expand our manufacturing capability. We will begin to disclose cost of sales in our next fiscal year as revenues and related manufacturing cost increase.

Our future liquidity and capital requirements will principally depend on our rate of growth and the means by which we achieve our growth. We believe that the cash on hand, will be sufficient to meet our requirements until at least December 2002. However, we could require additional cash if we encounter unanticipated expenses or cost overruns, if our products do not achieve market acceptance, or if we decide to engage in acquisitions or joint ventures. Our capital needs in future periods will depend principally on our ability to generate sales of our products, the extent and timing of future increases in manufacturing capacity and the extent to which we engage in acquisitions and joint ventures. We expect to need additional capital beyond December 2002, which we may not be able to raise on favorable terms, or at all.

Qualitative and Quantitative Disclosures about Risks and Uncertainties

Interest Rate Risk

As of June 30, 2001, we had cash, cash equivalents and short-term investments totaling $35.0 million. As a result of short-term maturities, we do not believe these investments are subject to significant interest rate risk. Declines in interest rates over time will, however, reduce the interest income earned on these investments.

Foreign Currency Exchange Rate Risk

We expect that the majority of our sales will, in the future, be made in U.S. dollars and that in the short term, the majority of our expenses will be denominated in Canadian dollars. As of June 30, 2001, $26.4 million of our cash, cash equivalents and short-term investments are denominated in Canadian dollars. Fluctuations in the exchange rate between the Canadian dollar and the U.S. dollar may therefore have a material effect on our results of operations. We do not currently engage in currency hedging activities.

Credit Risk

We manage our credit risk with respect to accounts receivable by establishing and implementing credit limits, approval policies, and primarily dealing with creditworthy customers. We have also insured all our foreign accounts receivable with the Export Development Corporation to the extent of 90% of coverage.

Other Risks and Uncertainties

We are a late stage development company facing corresponding risks, expenses and difficulties that may affect our outlook and eventual results of our business and commercialization plan.

We may not be able to establish high-volume manufacturing facilities on a timely, cost-effective basis or at all. We have never manufactured batteries in large quantities and we may not be able to maintain future commercial production at planned levels. Additionally, if we are unable to secure an adequate supply of raw materials or components, our costs could increase or our production could be limited.

We plan to offset these risks in a number of ways:

- Our manufacturing process is modular and flexible.
- Our high-volume facility will utilize machinery and equipment that is similar to the machinery and equipment that we have already designed, built and used in our current pilot production plant. Since the introduction of our PowerPad in 1999 we have successfully produced finished products in our pilot plant, resulting in sales.
- We are in the process of formalizing supply arrangements with suppliers to ensure that raw materials required for high-volume production are available at a reasonable cost and on a timely basis.
- We intend to ensure we have more than one supplier for critical raw materials and components.

Until the establishment of multiple plants, we will be dependent upon the operation of a single manufacturing facility and accidents or other operational problems at this facility could affect our ability to deliver product to our customers and therefore our ability to generate revenues. In addition, we may be subject to environmental liabilities at our facilities, which could result in material expense and adversely affect our ability to sell or finance our facilities.

We have addressed these risks by designing and building our high-volume facility with worker safety in mind. In addition, we are adopting a formal environmental policy that requires compliance with environmental legislation and an ongoing program of monitoring our environmental compliance**.**

We do not have a collaborative partner to assist us in the development of our batteries, which may limit our ability to develop and commercialize our products on a timely basis, if at all. Furthermore, we may incur significant costs and invest considerable resources designing and testing batteries for use with, or incorporation into, specific products without significant return.

We believe that the formation of strategic partnerships will be critical for the Company to meet its business objectives. We will continue to seek arrangements with potential partners to mitigate the development and commercialization risk going forward, balanced by our objective to maximize market share and penetration by not entering into exclusivity arrangements with a single partner. In addition, we are reviewing options to work with multiple partners on OEM programs for internally designed applications, sales and distribution arrangements, outsourcing parts of our manufacturing process, and for development of specialized applications in industry segments other than laptop computers and cell phones.

We may not be able to compete effectively with other manufacturers of compact rechargeable batteries. There is also the possibility our competitors may develop portable power technologies that match or outperform our SuperPolymer technology, which may diminish the demand for our products. In addition, innovations in the design of portable computers, mobile telephones and other wireless devices may reduce the need for our batteries.

We believe Electrofuel is well positioned to compete in the market for compact rechargeable batteries, which is already very large and growing rapidly. There are currently five to seven principal competitors, primarily well capitalized companies based in Japan, which have in aggregate a dominant market position in the lithium ion and lithium ion polymer battery sector. By leveraging our technological advantage, moving quickly to penetrate the market, initially targeting the underserved aftermarket, and emphasizing our higher energy density to create brand differentiation, we believe we can achieve revenue generation in the near term. Additionally, we believe that design innovations in the wireless sector will either not materially extend the run time of existing battery technologies or will be more than offset by the addition of new, enhanced, power-hungry features, which will increase the energy requirements of these wireless devices.

While our energy density is currently superior to that of our competitors in commercial production, we will continue to invest in research and development to utilize latest generation advanced materials and improve the process and design of our batteries to maintain or widen the technological gap between our technology and our closest competitors. However, we have limited knowledge of our competitors' activities in this area.

All lithium ion polymer batteries can become hazardous under some circumstances. In the event of a short circuit or other physical, electrical or thermal damage to these batteries, chemical reactions may occur that release excess heat or gases, which could create dangerous situations, including fire, explosions and releases of toxic fumes. Our batteries may emit smoke, catch fire or emit gas, any of which may expose us to product liability litigation. In addition, these batteries incorporate potentially hazardous materials that may require special handling, and safety problems may develop in the future. Product failure or improper use of lithium ion polymer battery products, such as the improper management of the charging/discharging system, may also result in dangerous situations. The raising of any health or safety issues could impact our reputation and sales. Moreover, changes in environmental or other regulations affecting the manufacture, transportation or sale of our products could adversely affect our ability to manufacture or sell our products or result in increased costs or liability. Finally, we may be required to devote significant financial and management resources to processing and remedying warranty claims. If product liability issues arise, we could incur significant expenses and suffer damage to our reputation and the market acceptance of our products.

To mitigate these risks of product liability, we undertake extensive internal and external product and safety testing. We believe that there are currently no regulations in North America that would prevent us from the manufacture, sale or transportation of our batteries, and we are fully committed to ensuring our products are environmentally friendly. In certain situations or applications, battery power may be a more attractive environmental solution than other energy sources utilizing fossil fuels or creating emissions.

We may not be able to successfully market our battery technology and products, and because our SuperPolymer technology is entirely new, our batteries may not perform as well as we anticipate. We expect to sell our products directly to corporate customers and through value-added resellers and distributors. But if these parties do not purchase our products or purchase them in lower quantities or over longer time periods than we expect, our revenue profile and cash flows may be severely impacted. Initially we expect to rely upon a limited number of customers for a significant portion of our sales and the loss of any customer could have a material adverse effect on our sales and operating results, and make it more difficult to attract and retain other customers.

Our PowerPad 160 product has undergone extensive user testing. We have now sold limited quantities of our products to well established corporate users with positive early results. We have an aggressive marketing program in place, including trade shows, advertising, etc. We have hired a dedicated sales team to aggressively market and sell our products. We are adopting a multi-channel distribution strategy to reduce our reliance on a single customer or distributor. We are targeting different types of users, applications, and industries to mitigate the risk if our products do not achieve acceptance in a single market and to ensure we minimize reliance on one customer.

If we fail to manage growth successfully, we could experience delays, cost overruns or other problems. Similarly, if we are unable to hire or retain qualified, key personnel, our business may be jeopardized.

We have identified and are acting on the need to hire additional staff for our manufacturing facility, at the senior management levels and for specialized personnel in various disciplines or areas of expertise, to help ensure the Company continues to effectively manage its rapid growth. Additionally, our senior management team has significant breadth and depth of expertise in managing start-up situations, which will assist the Company in making a smooth transition from a small private company to a large public company. We are currently implementing a market driven compensation structure and benefits plan with the assistance of a third party, to assist us in attracting and retaining key personnel.

If we fail to protect our proprietary technology, we may lose any competitive advantage it provides. Others may claim that our products infringe on their intellectual property rights, which could result in significant expenses for litigation, developing new technology or licensing existing technologies from third parties. If we are unable to register our trademarks, or our trademarks or trade name are found to violate the rights of others, we may have to change our trademarks or name and lose the goodwill we have created in them.

We will continue to register patents resulting from ongoing research and development activity, acquire or license patents from third parties if appropriate and further develop the trade secrets related to our manufacturing process and the design and operation of the equipment used to manufacture our products.

Outlook

To date, we have successfully developed our technology, financed our expansion, pre-marketed our products, purchased machine-making equipment and acquired a manufacturing facility. Our manufacturing facility has just come on stream in the second calendar quarter of 2001, and a well-defined production ramp up has started. We expect to begin generating ongoing revenue from commercial production in the near future, at which time our focus will be on growth. We believe that our output will be taken up quickly as the performance, reliability and value of our products become known in our target markets. We are therefore confident that the risks inherent in our business and markets are mitigated by the proprietary nature of our technology, the quality of our products, and the capabilities of our management and staff.

ELECTROFUEL INC.

Consolidated Balance Sheets
(Expressed in U.S. dollars)

June 30, 2001 and September 30, 2000

	June 30, 2001 (Unaudited)	September 30, 2000 (Audited)
Assets		
Current assets:		
Cash and cash equivalents	$ 5,886,844	$ 6,337,345
Short-term investments	29,109,756	12,999,585
Accounts receivable	304,181	184,920
Investment tax credits recoverable	589,632	593,740
Goods and Services Tax receivable	472,861	255,007
Inventories	749,369	81,418
Prepaid expenses and other	233,356	460,647
	37,345,998	20,912,662
Deferred finance charges	-	1,838,870
Capital assets	16,624,846	8,143,340
	$ 53,970,844	$ 30,894,872
Liabilities and Shareholders' Equity		
Current liabilities:		
Accounts payable and accrued liabilities	$ 1,112,951	$ 1,767,024
Income taxes payable	-	64,956
	1,112,951	1,831,980
Shareholders' equity:		
Share capital	63,675,765	35,385,197
Cumulative translation adjustment	(759,276)	(1,045,673)
Deficit accumulated during development stage	(10,058,596)	(5,276,632)
	52,857,893	29,062,892
	$ 53,970,844	$ 30,894,872

See accompanying notes to consolidated financial statements.

ELECTROFUEL INC.

Consolidated Statements of Operations and Deficit
(Expressed in U.S. dollars)

Three and nine months ended June 30, 2001, with comparative figures for
three and nine months ended June 30, 2000

(Unaudited)

	Three months ended June 30		Nine months ended June 30	
	2001	2000	2001	2000
Revenue	364,719	11,279	635,091	11,279
Expenses:				
Start-up and manufacturing	489,268	-	799,011	-
Research and development	626,523	246,553	1,638,675	759,531
Sales and marketing	394,750	231,875	1,089,322	484,710
General and administrative	1,029,756	738,143	3,570,320	1,692,720
	2,540,297	1,216,571	7,097,328	2,936,961
Loss from operations	2,175,578	1,205,292	6,462,237	2,925,682
Other expense (income)	25,396	(29,679)	(56,371)	(60,412)
Interest income	(406,198)	(380,228)	(1,489,268)	(760,199)
Loss (gain) from foreign exchange	372,780	(428,386)	(134,634)	(501,943)
	2,167,556	366,999	4,781,964	1,603,128
Loss for the period	2,167,556	366,999	4,781,964	1,603,128
Deficit accumulated during development stage, beginning of period	7,891,040	4,530,013	5,276,632	3,293,884
Deficit accumulated during development stage, end of period	10,058,596	4,897,012	10,058,596	4,897,012
Loss per common share (notes 3)	0.03	0.01	0.07	0.03

ELECTROFUEL INC.

Consolidated Statements of Cash Flows
(Expressed in U.S. dollars)

Three and nine months ended June 30, 2001, with comparative figures for
three and nine months ended June 30, 2000

(Unaudited)

	Three months ended June 30 2001	Three months ended June 30 2000	Nine months ended June 30 2001	Nine months ended June 30 2000
Cash provided by (used in):				
Operating activities:				
Loss for the period	$ (2,167,556)	$ (366,999)	$ (4,781,964)	$ (1,603,128)
Amortization which does not involve cash	142,210	165,721	397,788	317,397
Common shares issued for services	-	21,366	-	176,042
Change in non-cash operating working capital	(712,796)	(168,051)	346,175	(489,952)
	(2,738,142)	(347,963)	(4,038,001)	(1,599,641)
Financing activities:				
Proceeds from issue of common shares	(2,190)	-	28,291,077	28,439,215
	(2,190)	-	28,291,077	28,439,215
Investing activities:				
Additions to capital assets	(2,415,469)	(4,431,637)	(8,938,785)	(5,260,315)
Net additions to short-term investments	(29,109,756)	(12,973,230)	(16,200,118)	(12,973,230)
	(31,525,225)	(17,404,867)	(25,138,903)	(18,233,545)
Increase (decrease) in cash and cash equivalents	(34,265,557)	(17,752,830)	(885,827)	8,606,029
Effect of currency translation adjustments on cash and cash equivalents	1,805,655	(486,432)	435,326	(459,274)
Cash and cash equivalents, beginning of period	38,346,746	28,763,998	6,337,345	2,377,981
Cash and cash equivalents, end of period	$ 5,886,844	$ 10,524,736	$ 5,886,844	$ 10,524,736

See accompanying notes to consolidated financial statements.

ELECTROFUEL INC.

Notes to Consolidated Financial Statements
(Expressed in U.S. dollars)

Nine months ended June, 2001 and 2000
and for the year ended September 30, 2000
(Unaudited)

1. Comparative Figures:

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

2. Share capital:

On August 2, 2000, the Company's shareholders authorized a three-for-one stock split, which became effective on September 18, 2000. All references to common shares, common shares outstanding, stock options and per share amounts in these financial statements have been restated to reflect this three-for-one stock split on a retroactive basis.

(a) On November 10, 2000, the Company issued 6,250,000 common shares at Cdn $8.00 per common share for gross proceeds of $32.4 million (Cdn $50,000,000) and net proceeds of $28.3 million after deducting underwriting commissions and expenses of the offering.

(b) On November 9, 2000, the Company issued, for no consideration, a total of 25,000 charitable warrants to three charitable organizations. Each charitable warrant entitles the holder to receive, for cash consideration of $5.24 (Cdn $8.00), one common share. The charitable warrants are fully vested, non-transferable and will expire 10 years from the date of closing of the offering of common shares.

(c) During the period 525,000 options, with an exercise price of $5.33 were surrendered.

(d) During the period 162,000 options were exercised at a price of $1.08.

3. Loss per share:

The net loss per share has been calculated using the weighted average number of common shares outstanding during the periods, which are as follows:

June 30, 2001	67,170,297
June 30, 2000	54,535,287

Common share purchase options or other potential dilutive common shares were not considered for each of the periods presented since their effect would be anti-dilutive.

4. Startup and manufacturing expenses

In mid April 2001, the Company commenced production of commercial units at its new manufacturing facility in Mississauga. All of the materials, labour and overhead costs associated with the production of commercial units and the start up of the plant are included in Start-up and manufacturing expenses.