



H-SOURCE HOLDINGS LTD.

CONSOLIDATED INTERIM FINANCIAL STATEMENTS

For the Period Ended June 30, 2016

(EXPRESSED IN US DOLLARS)

H-SOURCE HOLDINGS LTD.
Consolidated Statements of Financial Position
(Expressed in US Dollars)

	Notes	June 30, 2016 \$	December 31, 2015 \$ (Audited)
ASSETS			
Current Assets			
Cash		152,876	62,933
Short-term investments	6	1,376,170	546,543
Prepaid expenses		14,510	33,847
Accounts receivable		13,500	31,561
Total Current Assets		1,557,056	674,884
Patents	8	89,447	72,142
Software development costs	8	297,453	297,453
TOTAL ASSETS		1,943,956	1,044,479
LIABILITIES			
Current Liabilities			
Accounts payable and accrued liabilities	9	116,109	142,399
SHAREHOLDERS' EQUITY			
Common shares	12	5,782,979	3,108,738
Reserves		284,903	245,349
Obligation to issue shares		-	216,300
Deficit		(4,174,335)	(2,653,501)
Accumulative other comprehensive income		(65,700)	(14,806)
Total Shareholders' Equity		1,827,847	902,080
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		1,943,956	1,044,479

Nature and continuance of operations (Note 1)

Commitments (Note 15)

Subsequent events (Note 16)

On behalf of the board:

“John Kupice” Director
John Kupice

“Murray Walden” Director
Murray Walden

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

H-SOURCE HOLDINGS LTD.
Consolidated Statements of Comprehensive Loss
(Expressed in US Dollars)

	Notes	Three Months Ended June 30 June 30, 2016 \$	Six Months Ended June 30 June 30, 2016 \$	Three Months Ended June 30 June 30, 2015 \$	Six Months Ended June 30 June 30, 2015 \$
Expenses					
Advertising and promotion		64,759	136,255	4,921	5,214
Consulting fees		214,515	397,154	-	-
General and administration expenses	7	185,660	260,976	50,681	68,625
Professional fees		28,325	40,990	176,986	236,615
Salaries and benefits		358,928	543,920	97,469	234,463
Share-based payments	12	11,001	39,554	-	-
		(863,188)	(1,418,849)	(330,057)	(544,917)
Other Income (Expenses)					
Interest income		2,148	2,631	-	-
Interest and other finance costs, net		(228)	(522)	12,934	166,285
Loss on debt settlement		(104,094)	(104,094)	-	-
Net Loss for the Period		(965,362)	(1,520,834)	(342,991)	(711,202)
Other Comprehensive Income					
Foreign exchange on translation of subsidiary		(31,446)	(50,894)	-	-
Net and Comprehensive Loss for the Period		(996,808)	(1,571,728)	(342,991)	(711,202)
Basic and Diluted Loss Per Share					
		(0.01)	(0.03)	(0.02)	(0.05)
Weighted Average Number of Common Shares Outstanding					
		66,516,575	57,142,393	17,577,779	15,722,042

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

H-SOURCE HOLDINGS LTD.

Consolidated Statements of Changes in Shareholders' Equity (Deficiency) (Expressed in US Dollars)

	Common Shares		Reserves	Obligation to Issue Common Shares	Accumulative Other Comprehensive Income	Accumulated Deficit	Shareholders' Equity (Deficiency)
	Number of Shares	\$					
Balance – December 31, 2014	2,657,250	15,349	9,276	-	-	(229,661)	(205,036)
Shares issued for cash	281,326	186,050	-	-	-	-	186,050
Shares issued for services	694,732	463,110	-	-	-	-	463,110
Net loss and comprehensive loss for the period	-	-	-	-	-	(711,202)	(711,202)
Balance – June 30, 2015	3,633,308	664,509	9,276	-	-	(940,863)	(267,078)
Balance – December 31, 2015	47,935,364	3,108,738	245,349	216,300	(14,806)	(2,653,501)	902,080
Shares issued for services and termination fees	3,400,000	496,989	-	(216,300)	-	-	280,689
Stock options granted	-	-	42,427	-	-	-	42,427
Stock options cancelled	-	-	(2,873)	-	-	-	(2,873)
Shares issued pursuant to private placement, net share issuance costs	18,753,141	2,177,253	-	-	-	-	2,177,253
Net loss and comprehensive loss for the period	-	-	-	-	(50,894)	(1,520,834)	(1,571,728)
Balance – June 30, 2016	70,088,505	5,782,979	284,903	-	(65,700)	(4,174,335)	1,827,847

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

H-SOURCE HOLDINGS LTD.

Consolidated Statements of Cash Flows

(Expressed in US Dollars)

	Six Months Ended June 30, 2016 \$	Six Months Ended June 30, 2015 \$
Cash provided by (used in):		
Operating activities		
Net loss for the period	(1,520,834)	(368,211)
Items not involving cash:		
Accretion and non-cash interest expense	-	1,846
Foreign exchange	-	5,083
Consulting fees	188,561	211,800
Share-based payments	39,554	-
Loss on debt settlement	104,094	-
Changes in non-cash operating working capital:		
Accounts receivable	19,652	-
Prepaid expenses	20,850	1,821
Accrued interest payable	-	4,467
Accounts payable & accrued liabilities	(34,690)	49,198
Net cash used in operating activities	(1,182,813)	(93,996)
Cash flows from investing activities:		
Short-term investments	(793,412)	-
Patents	(17,305)	-
Software development	-	(13,000)
Net cash (used in) provided by investing activities	(810,717)	(13,000)
Cash flows from financing activities:		
Proceeds from share issuances, net share issuance costs	2,177,253	33,500
Proceeds for share issuance	-	(26,565)
Proceeds from convertible debentures, net	-	211,894
Net cash provided by financing activities	2,177,253	218,829
Effect of foreign exchange	(95,676)	-
Cash, beginning of the period	64,829	-
Cash, end of period	152,876	111,833

Supplemental Cash Flow Information (Note 13)

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

H-SOURCE HOLDINGS LTD.
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS
For the Period Ended June 30, 2016
(Expressed in US Dollars)

NOTE 1 - NATURE OF OPERATIONS

H-Source Holdings Ltd. (the “Company”), was incorporated on November 11, 2014 under the laws of British Columbia, Canada. Its head office is located at 1980-1075 W. Georgia St., Vancouver BC V6E 3C9, Canada and registered office is located at 1500-1055 W. Georgia St., Vancouver, BC, V6E 4N7, Canada.

On August 31, 2015, the Company completed a plan of merger (the “Transaction”) whereby the Company acquired 100% of the issued and outstanding common shares of H-Source, Inc. (“HSI”), a Washington State corporation, through the merger of the Company’s wholly-owned subsidiary, BC Merger Sub. Inc., with HSI as the surviving and wholly-owned subsidiary of the Company, and changed its name to “H-Source Holdings Ltd.” The Company’s common shares commenced trading on the Canadian Securities Exchange (the “CSE”) on October 1, 2015 under the stock symbol “HSI”. The Company also commenced trading on the OTCQB in the USA under the stock symbol “HSCHF” on February 12, 2016. On July 25, 2016, the Company listed on the TSX Venture Exchange (the “Exchange”) and de-listed from the CSE. The Company’s common shares still trade under the ticker symbol “HSI”.

This Transaction was accounted for as a reverse acquisition as the former shareholders of HSI, as well as new investors, acquired control of the Company. The Transaction is considered a purchase of the Company’s operations by the shareholders of HSI. The Transaction is recorded in accordance with guidance provided in IFRS 2 “Share Based Payments” and IFRS 3 “Business Combinations”. As the Company did not qualify as a business according to the definition in IFRS 3, this Transaction does not constitute a business combination; rather it is treated as an issuance of shares by HSI for the net assets of the Company and the listing status.

HSI was incorporated under the laws of the State of Washington, USA on May 27, 2014 and acquired all of the assets and assumed all of the liabilities of H-Source LLC, effective June 1, 2014. This transaction was accounted for as an acquisition of an entity under common control and as such the transaction was recorded at historical cost. Upon acquisition, H-Source LLC was dissolved. HSI has developed a digital platform and network to operate in the healthcare industry and offers a private, hospital-to-hospital marketplace that allows members to buy/sell/transfer supplies and capital equipment with each other. Members can conduct secure transactions within Integrated Delivery Networks (IDNs), Group Purchasing Organizations (GPOs), the complete HSI network, or customize their own group of hospitals using the Company’s built-in filters. This network is designed specifically to reduce health care costs and medical products waste.

These condensed interim consolidated financial statements of the Company were approved and authorized for issue by the Board of Directors on August 29, 2016.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance

These condensed interim consolidated financial statements are prepared in accordance with International Accounting Standards (“IAS”) 34, Interim Financial Reporting, as issued by the International Accounting Standards Board (“IASB”) on a basis consistent with the significant accounting policies disclosed in note 2 of the most recent annual financial statements as at and for the year ended December 31, 2015 as filed on SEDAR at www.sedar.com. The condensed interim consolidated financial statements do not include all of the information required for full annual financial statements.

Basis of presentation and going concern

These consolidated financial statements have been prepared on a historical cost basis except for financial instruments classified as financial instruments at fair value through profit or loss that have been measured at fair value. In addition, these consolidated financial statements have been prepared using the accrual basis of accounting and are presented in United States dollars unless otherwise noted.

The principal accounting policies applied in the preparation of the consolidated financial statements are set out below. These policies have been consistently applied to all of the periods presented, unless otherwise stated.

These consolidated financial statements include the accounts of H-Source Holdings Ltd. and H-Source, Inc. Control is achieved when the Company has the power to govern the financial and operating policies of an entity so as to obtain benefits

H-SOURCE HOLDINGS LTD.
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS
For the Period Ended June 30, 2016
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NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CONT

from its activities. The subsidiary is fully consolidated from the date on which control is acquired by the Company. Inter-company transactions and balances are eliminated upon consolidation. They are de-consolidated from the date that control by the Company ceases. Inter-company balances and transactions and any unrealized income and expenses arising from inter-company transactions are eliminated in preparing the consolidated financial statements.

The Company has not realized any revenues to date and has experienced net losses since inception. As of December 31, 2015 and June 30, 2016, the Company had an accumulated deficit of \$2,653,501 and \$4,174,335, respectively. For the period ended June 30, 2015 and June 30, 2016, the Company had cash outflows from cash used in operating activities of \$252,170 and \$1,182,813, respectively. The Company expects to continue to incur net losses and have significant cash outflows for the foreseeable future. The Company is subject to a number of risks similar to those of other pre-commercial stage companies, including its dependence on key individuals, uncertainty of product development and generation of revenues, dependence on outside sources of capital, risks associated with research, development, testing, successful protection of intellectual property, competition with larger, better-capitalized companies, and successful completion of the Company's development programs. Ultimately, the attainment of profitable operations is dependent on future events, including obtaining adequate financing to fulfill its development activities and generating a level of revenues adequate to support the Company's cost structure.

The Company requires significant additional cash resources to continue development and marketing of its software platform, support infrastructure, network infrastructure, and sales and marketing efforts. These conditions, among others, raise substantial doubt about the Company's ability to continue as a going concern. The accompanying consolidated financial statements have been prepared assuming that the Company will continue as a going concern. This basis of accounting contemplates the recovery of the Company's assets and the satisfaction of liabilities in the normal course of business. A successful transition to attaining profitable operations is dependent upon achieving a level of positive cash flows adequate to support the Company's cost structure.

The future viability of the Company is dependent on its ability to generate cash from operating activities, and to raise additional capital to finance its operations. The Company's failure to raise capital as and when needed could have a negative impact on its financial condition and ability to pursue its business strategies.

The interim consolidated financial statements do not include any adjustments due to this uncertainty relating to the recoverability and classification of recorded asset amounts and classification of liabilities.

Foreign currency translation

The functional currency of an entity is the currency of the primary economic environment in which the entity operates. The functional currency of H-Source Holdings Ltd. is the Canadian dollar ("C\$") and of HSI is United States dollar. The reporting currency of the Company is the United States dollar. The functional currency determinations were conducted through an analysis of the consideration factors identified in IAS 21, "The Effects of Changes in Foreign Exchange Rates".

Foreign currency transactions are translated into functional currency using the exchange rates prevailing at the date of the transaction. Foreign currency monetary items are translated at the period-end exchange rate. Non-monetary items measured at historical cost continue to be carried at the exchange rate at the date of the transaction. Non-monetary items measured at fair value are reported at the exchange rate at the date when fair values were determined.

Exchange differences arising on the translation of monetary items or on settlement of monetary items are recognized in the statement of comprehensive loss in the period in which they arise, except where deferred in equity as a qualifying cash flow or net investment hedge.

H-SOURCE HOLDINGS LTD.
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CONT

Patents

Patents are capitalized if it is probable that the future economic benefits that are attributable to the patent will flow to the Company and the cost of the patent can be measured reliably. Patents have finite lives and are measured at cost less accumulated amortization and accumulated impairment losses over their useful lives. Patents are assessed for impairment whenever there is an indication that they may be impaired. If any such indication exists, the recoverable amount is estimated and an impairment loss is recognized whenever the carrying amount exceed their recoverable amount. At June 30, 2016 the patents were not yet in service, therefore an impairment analysis was performed in accordance with IAS 36. No impairment was recognized as a result of this analysis.

Patents will be amortized using the straight-line method over a 10 year period upon commencement of commercial operations.

Deferred software development costs

Research costs are expensed as incurred. Costs related to the development of software are expensed as incurred unless such costs meet the criteria for deferral and amortization under IFRS. The criteria include identifiable costs attributable to a clearly defined product, the establishment of technical feasibility, identification of a market for the software, the Company's intent to market the software, and the existence of adequate resources to complete the project. Directly attributable costs that are capitalized as part of the software application include internal costs. Software development costs are amortized over an estimated useful life of three years, commencing in the year when commercial sales of the products commence. Capitalized software development is evaluated in each reporting period to determine whether it continues to meet the criteria for continued deferral and amortization.

Foreign currency translation

Transactions denominated in foreign currencies are converted to their functional currencies at exchange rates prevailing at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies are translated to their functional currencies at the exchange rate prevailing at the reporting date. Non-monetary assets and liabilities are translated at historical exchange rates prevailing at each transaction date. Revenues and expenses are translated at exchange rates prevailing on the date of transactions. All exchange gains and losses are included in determination of earning. Financial statements of each entity is prepared under their functional currencies are translated into United States dollars for consolidation purposes as follows: assets and liabilities are translated using the exchange rate prevailing at the reporting date; expenses are translated using the average rates of exchange for the period. Gains and losses resulting from translation adjustments are recorded as other comprehensive income (loss) and accumulated in a separate component of shareholders' equity, described as foreign currency translation adjustment.

Loss per share

Basic loss per share is calculated by dividing the loss attributable to common shareholders by the weighted average number of common shares outstanding in the period. For all periods presented, the loss attributable to common shareholders equals the reported loss attributable to owners of the Company. Diluted loss per share is calculated using the treasury stock method. Under the treasury stock method, the weighted average number of common shares outstanding for the calculation of diluted loss per share assumes that the proceeds to be received on the exercise of dilutive share options and warrants are used to repurchase common shares at the average market price during the period. Diluted loss per share is not presented as there are no dilutive securities outstanding.

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NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CONT

Impairment of assets

The carrying amount of long-lived assets, specifically intangible assets, is reviewed at each reporting date to determine whether there is any indication of impairment. If such indication exists, the recoverable amount of the asset is estimated in order to determine the extent of the impairment loss. Long-lived assets under construction are evaluated for impairment annually. An impairment loss is recognized whenever the carrying amount of an asset or its cash generating unit exceeds its recoverable amount. Impairment losses are recognized in the statement of comprehensive loss.

The recoverable amount of assets is the greater of an asset's fair value less cost to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects the current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs. There were no impairments recognized in the periods ended June 30, 2016 and December 31, 2015.

An impairment loss is only reversed if there is an indication that the impairment loss may no longer exist and there has been a change in the estimates used to determine the recoverable amount. Any reversal of impairment cannot increase the carrying value of the asset to an amount higher than the carrying amount that would have been determined had no impairment loss been recognized in previous years.

Share Capital

Common shares issued for non-cash consideration are recorded at the fair value of the shares at the time, or if the fair value of shares is not measurable, then the fair value of the services provided.

Share-based payment transactions

The stock option plan allows Company directors, officers, employees and consultants to acquire shares of the Company. The fair value of share purchase options granted is recognized as an employee or consultant expense with a corresponding increase in equity. An individual is classified as an employee when the individual is an employee for legal or tax purposes (direct employee) or provides services similar to those performed by a direct employee. The fair value is measured at grant date and the share based compensation is expensed based on graded vesting. When the value of goods or services received in exchange for the share-based payment cannot be reliably estimated, the fair value of the share purchase options granted is measured using the Black-Scholes Option Pricing Model taking into account the terms and conditions upon which the share purchase options were granted. Forfeiture rates are estimated in advance and are used in the estimate of the share-based expense for the financial statement period. Equity-settled share-based payment transactions with non-employees are measured at the fair value of the goods or services received. However, if the fair value cannot be estimated reliably, the share-based payment transaction is measured at the fair value of the equity instruments granted at the date the Company receives the goods or the services.

Warrants

Proceeds from issuances by the Company of units consisting of shares and warrants are allocated based on the residual method, whereby the carrying amount of the warrants is determined based on any difference between gross proceeds and the estimated fair market value of the shares. If the proceeds from the offering are less than or equal to the estimated fair market value of shares issued, a nil carrying amount is assigned to the warrants.

Financial instruments

The Company classifies its financial instruments in the following categories: financial assets at fair value through profit or loss ("FVTPL"), held to maturity, available for sale, loans and receivables, and financial liabilities. The classification depends on the purpose for which the financial instruments were acquired. Management determines the classification of its financial instruments at initial recognition.

Financial assets are classified as FVTPL when they are either held for trading for the purpose of short-term profit taking, derivatives not held for hedging purposes, or when they are designated as such to avoid an accounting mismatch or to enable performance evaluation where a group of financial assets is managed by key management personnel on a fair value basis in accordance with a documented risk management or investment strategy. Such assets are subsequently measured at fair value with changes in carrying value being included in profit or loss. The Company does not have any financial assets measured through profit or loss.

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NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CONT

Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market and are subsequently measured at amortized cost. They are included in current assets, except for maturities greater than 12 months after the end of the reporting period. These are classified as non-current assets. Cash and short-term investments are included in FVTPL as of June 30, 2016 and December 31, 2015.

Available-for-sale financial assets are non-derivative financial assets that are designated as available-for-sale or are not suitable to be classified as financial assets at fair value through profit or loss, loans and receivables or held-to-maturity investments and are subsequently measured at fair value. These are included in current assets to the extent they are expected to be realized within 12 months after the end of the reporting period. Unrealized gains and losses are recognized in other comprehensive income, except for impairment losses and foreign exchange gains and losses on monetary financial assets. The Company does not have any available-for-sale financial assets as of June 30, 2016 and December 31, 2015.

All financial liabilities are initially recorded at fair value and designated upon inception as FVTPL or other financial liabilities. The Company has not classified any financial liabilities as FVTPL.

Financial liabilities classified as other financial liabilities are initially recognized at fair value less directly attributable transaction costs. After initial recognition, other financial liabilities are subsequently measured at amortized cost using the effective interest rate method. The effective interest rate method is a method of calculating the amortized cost of a financial liability and of allocating interest expense over the relevant period. The effective interest rate is the rate that discounts estimated future cash payments through the expected life of the financial liability, or, where appropriate, a shorter period. Financial liabilities classified as other financial liabilities include accounts payable and other short-term monetary liabilities.

Financial assets are derecognized when the rights to receive cash flows from the investments have expired or have been transferred and the Company has transferred substantially all risks and rewards of ownership.

At each reporting date, the Company assesses whether there is objective evidence that a financial instrument has been impaired. In the case of available-for-sale financial instruments, a significant and prolonged decline in the value of the instrument is considered to determine whether an impairment has arisen.

Provisions

The Company recognizes provisions for liabilities of uncertain timing or amount including those for legal disputes. If applicable, the provision is measured at the best estimate of the expenditure required to settle the obligation at the reporting date, discounted at a pre-tax rate reflecting current market assessments of the time value of money and risks specific to the liability. There were no provisions recognized as of June 30, 2016 and December 31, 2015.

New Standards and Interpretations Not Yet Effective:

Standards issued but not yet effective up to the date of issuance of the Company's financial statements are listed below. This listing is of standards and interpretations issued, which the Company reasonably expects to be applicable at a future date. The Company is currently assessing the impact of the following standards on the consolidated financial statements and intends to adopt these standards when they become effective.

IFRS 9 – Financial Instruments

IFRS 9 replaces the current IAS39 - Financial Instruments Recognition and Measurement. The standard intends to reduce the complexity in the classification and measurement of financial instruments. In February 2014, the IASB tentatively determined that the revised effective date for IFRS 9 would be January 1, 2018. The Company is currently evaluating the impact the final standard is expected to have on its financial statements.

IFRS 15 – Revenue from Contracts with Customers (“IFRS 15”)

In May 2014, the IASB issued IFRS 15 – Revenue from Contracts with Customers ("IFRS 15") which supersedes IAS 11 – Construction Contracts, IAS 18 – Revenue, IFRIC 13 – Customer Loyalty Programs, IFRIC 15 – Agreements for the Construction of Real Estate, IFRIC 18 – Transfers of Assets from Customers, and SIC 31 – Revenue – Barter Transactions involving Advertising Services. IFRS 15 establishes a single five-step model framework for determining the nature, amount, timing and uncertainty of revenue and cash flows arising from a contract with a customer. The standard is effective for

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NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CONT

annual periods beginning on or after January 1, 2018, with early adoption permitted. As the Company has not yet started generating revenue this standard is not expected to impact the financial statements.

IFRS 16 – Leases (“IFRS 16”)

IFRS 16 replaces IAS 17 “Leases” and the related interpretative guidance. IFRS 16 applies a control model to the identification of leases, distinguishing between a lease and a service contract on the basis of whether the customer controls the asset being leased. For those assets determined to meet the definition of a lease, IFRS 16 introduces significant changes to the accounting by lessees, introducing a single, on-balance sheet accounting model that is similar to current finance lease accounting, with limited exceptions for short-term leases or leases of low value assets. Lessor accounting is not substantially changed. The standard is effective for annual periods beginning on or after January 1, 2019, with early adoption permitted for entities that have adopted IFRS 15. The Company has not yet assessed the future impact of this new standard on its financial statements.

NOTE 3 – CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

Estimates and assumptions

The preparation of financial statements in accordance with IFRS requires management to make estimates and assumptions that affect the reported amounts of assets, liabilities and contingent assets and liabilities at the date of the consolidated financial statements and reported amounts of expenses during the reporting period. Estimates and assumptions are based on management’s experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. However, actual outcomes can differ significantly from these estimates.

Areas requiring a significant degree of estimation relate to the determination of the life of patents and software development costs, the recoverability of carrying value of long-term assets, fair value measurements for financial instruments and stock-based compensation and other equity-based payments, and the recoverability and measurement of deferred tax assets and liabilities. Actual results may differ from those estimates and judgments.

Significant judgments

The preparation of financial statements in accordance with IFRS requires management to make judgments, apart from those involving estimates, in applying accounting policies. The most significant judgments applying to the Company’s financial statements include:

- Continuing feasibility of internally developed software;
- Whether there are indications of impairment of the Company’s non-current assets; and
- The assessment of the Company’s ability to continue as a going concern and whether there are events or conditions that may give rise to significant uncertainty.

Fair value measurements

A number of assets and liabilities included in the Company’s financial statements require measurement at, and/or disclosure of, fair value.

The fair value measurement of the Company’s financial and non-financial assets and liabilities utilizes market observable inputs and data as far as possible. Inputs used in determining fair value measurements are categorized into different levels based on how observable the inputs used in the valuation technique utilized are (the ‘fair value hierarchy’):

- *Level 1:* Quoted prices in active markets for identical items (unadjusted)
- *Level 2:* Observable direct or indirect inputs other than Level 1 inputs
- *Level 3:* Unobservable inputs (i.e. not derived from market data).

The classification of an item into the above levels is based on the lowest level of the inputs used that has a significant effect on the fair value measurement of the item. Transfers of items between levels are recognized in the period they occur.

The Company measures below market rate debt at fair value at inception and amortized cost over the remaining life of the notes.

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NOTE 3 – CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS-CONT

Recoverability of long-lived assets

The recoverable amount of assets is the greater of an asset's fair value less cost to sell and value in use. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects the current market assessments of the time value of money and the risks specific to the asset. For an asset that does not generate cash inflows largely independent of those from other assets, the recoverable amount is determined for the cash-generating unit to which the asset belongs.

NOTE 4 – FINANCIAL RISK AND CAPITAL MANAGEMENT

The Company is exposed in varying degrees to a variety of financial instrument related risks. The Board of Directors approves and monitors the risk management processes, inclusive of documented investment policies, counterparty limits, and controlling and reporting structures.

The principal financial instruments used by the Company, from which financial instrument risk arises, are cash, short-term investments, accounts payable and other accrued liabilities and fixed rate notes payable which is carried at amortized cost.

	June 30, 2016	December 31, 2015
Financial Assets		
Cash	\$ 152,876	\$ 62,933
Accounts receivable	13,500	31,561
Short-term investments	1,376,170	546,543
Total financial assets	\$ 1,542,546	\$ 641,037
Financial Liabilities		
Total accounts payable	\$ 116,109	\$ 142,399
Total financial liabilities	\$ 116,109	\$ 142,399

Due to their short-term nature, the carrying value of cash and accounts payable and other accrued liabilities approximates their fair value.

The type of risk exposure and the way in which such exposure is managed is provided as follows:

a) Credit risk

Credit risk is the risk of loss associated with a counter party's inability to fulfill its payment obligations. The Company's primary exposure to credit risk is on its cash accounts. Cash accounts are held with a major bank in the United States. The Company has deposited the cash with its bank from which management believes the risk of loss is remote.

b) Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company's approach to managing liquidity is to ensure that it will have sufficient liquid assets to meet liabilities when they become due. The Company is exposed to liquidity risk as it does not have sufficient cash to settle its current liabilities, refer to Note 2 and the going concern discussion for further information about the Company's plans to manage liquidity risk.

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NOTE 4 – FINANCIAL RISK AND CAPITAL MANAGEMENT-CONT

c) Market risk

Market risk is the risk that changes in market prices, such as interest rates and foreign exchange rates will affect the Company's value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return.

Interest rate risk

The Company has cash and cash equivalents balances and interest-bearing debt. The Company's current policy is to invest excess cash in investment-grade short-term deposit certificates issued by its banking institutions. The Company periodically monitors the investments it makes and is satisfied with the credit ratings of its banks. All debt bears fixed interest rates.

Foreign currency risk

Currency risk refers to the risk that the fair value of future cash flows of a financial instrument will fluctuate because of changes in foreign exchange rates. The Company has certain expenditures that are denominated in US dollars and other operating expenses that are in Canadian dollars. The Company's exposure to foreign currency risk arises primarily on fluctuations between the Canadian dollar and the US dollar.

d) Capital management

The Company considers its cash and share capital as capital. The Company's objectives when managing capital are to safeguard the Company's ability to continue as a going concern in order to maintain a flexible capital structure which optimizes the costs of capital at an acceptable risk.

The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, the Company may attempt to issue new shares, issue new debt, acquire or dispose of assets or adjust the amount of cash. There was no change in the Company's approach to capital management during the period ended June 30, 2016 or the year ended December 31, 2015.

NOTE 5 – REVERSE TAKE-OVER

On March 3, 2015, HSI entered into a non-binding letter of intent with the Company whereby the Company would acquire all of the issued and outstanding common shares in the capital of HSI and to list the resulting issuer on the Canadian Stock Exchange. This letter of intent was replaced and superseded by the Merger Agreement and Plan of Reorganization dated July 9, 2015.

On March 24, 2015, HSI entered into an Agency Agreement with BayFront Capital Partners Ltd. to act as exclusive agent for HSI to raise up to C\$2.5 million on a best efforts basis and to assist in the private placement.

On August 31, 2015, as part of the Transaction, 1,010,549 common shares were issued to the shareholders of the Company's former parent company at a nominal value.

On August 31, 2015, the Company completed the Transaction by acquiring all of the issued and outstanding common shares of HSI in consideration for 20,000,000 common shares of the Company. The Company issued 1,000,000 shares as finder's fee in connection with the completion of the Transaction.

In connection with the Transaction, the Company completed a non-brokered private placement financing (the "Concurrent Financing") of an aggregate of 17,587,333 subscription receipts (each, a "Subscription Receipt") at a price of C\$0.15 per Subscription Receipt for aggregate gross proceeds of \$1,993,348 (C\$2,638,100) on May 14, 2015. Upon closing of the Transaction, each Subscription Receipt was automatically exercised into one common share of the Company, for no additional consideration.

H-SOURCE HOLDINGS LTD.
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NOTE 5 – REVERSE TAKE-OVER-CONT

In relation to the Concurrent Financing, the Company paid an aggregate of \$183,178 (C\$241,891) in finders’ fees and issued an aggregate of 1,319,050 finders’ warrants, each of which is exercisable into one share at a price of C\$0.15 per share for a period of two years, expiring August 31, 2017. The fair value of the warrants is \$78,023 (C\$103,260).

As a result of the Transaction, the shareholders of H-Source, Inc. owned approximately 40% of the issued and outstanding common shares of H-Source Holdings Ltd. on a diluted basis. The acquisition of H-Source, Inc. by H-Source Holdings Ltd. constitutes a reverse asset acquisition (“RTO”) as H-Source Holdings Ltd. does not meet the definition of a business, as defined by IFRS 3, Business Combinations. For accounting and reporting purposes, H-Source, Inc. is the accounting acquirer and H-Source Holdings Ltd. is the accounting acquiree. Accordingly, the acquisition of the net assets and listing status of H-Source Holdings Ltd. is accounted for as a share-based payment as follows:

Net asset acquired:		
Cash and cash equivalents	\$	83,289
Accounts payable and accrued liabilities		(4,682)
	\$	78,607
Consideration paid:		
Fair value of shares of H-Source Holdings Ltd.	\$	125,593
Listing cost		(46,986)
	\$	78,607

The fair value of the shares was based on the most recent private placement completed prior to the Transaction valued, or \$125,593.

Under RTO accounting, the existing share capital and deficit balances of H-Source Holdings Ltd. are eliminated.

In connection with the Transaction, additional costs of \$558,438 were incurred for professional fees and finders’ fees for a total of \$605,424. The finders’ fees were paid in shares with a fair value of \$113,340.

NOTE 6- SHORT TERM INVESTMENT

As at June 30, 2016, the Company has a short term investment of \$1,376,170 (2015 - \$546,543) within a major financial institution and \$2,106 interest receivable due on April 21, 2017. The short-term investment has an annual yield of prime minus 1.9%.

H-SOURCE HOLDINGS LTD.

NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS

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(Expressed in US Dollars)

NOTE 7- GENERAL AND ADMINISTRIVE EXPENSES

	Three months ended June 30, 2016	Six months ended June 30, 2016	Three months ended June 30, 2015	Six months ended June 30, 2015
Foreign exchange	\$ -	\$ -	\$ 4,134	\$ 9,217
Office	44,992	70,358	28,126	36,741
Rent	7,790	15,370	4,300	4,900
Software expense	64,824	67,672	6,755	6,755
Transfer agent and regulatory fees	41,345	49,150	-	-
Travel	26,709	58,426	7,366	11,012
	<u>\$ 185,660</u>	<u>\$ 260,976</u>	<u>\$ 50,681</u>	<u>\$ 68,625</u>

NOTE 8- INTANGIBLE ASSETS

<u>Cost</u>	<u>Patents</u>	<u>Software development costs</u>
At December 31, 2014	\$ 57,411	\$ 182,068
Additions	14,731	115,385
At December 31, 2015	\$ 72,142	\$ 297,453
Additions	17,305	-
At June 30, 2016	<u>\$ 89,447</u>	<u>\$ 297,453</u>

Software development costs are still in development as of June 30, 2016 and December 31, 2015, there was no amortization recorded. There were no contractual commitments for development costs as of June 30, 2016 and December 31, 2015.

NOTE 9 - ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	June 30, 2016	December 31, 2015
Accounts payable	\$ 116,109	\$ 113,131
Accrued payroll taxes	-	29,268
	<u>\$ 116,109</u>	<u>\$ 142,399</u>

H-SOURCE HOLDINGS LTD.
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 10 – PROMISSORY NOTES PAYABLE

	June 30, 2016	December 31, 2015
Beginning balance	\$ -	\$ 77,864
Repayment of promissory notes	-	(83,000)
Accretion expense	-	5,136
Long term portion of promissory notes payable	\$ -	\$ -

HSI issued various unsecured promissory notes with face values totaling \$83,000 (December 31, 2014 - \$83,000). The promissory notes have terms of between 3 months and 3 years and bear interest rates between 0.25% and 8% per annum. Certain of the notes included a “kicker” provision for an additional \$6,000 which has been recorded as interest. HSI determined the fair value of certain below-market rate notes with a face value of \$63,000 to be \$53,724 based on an estimated market interest rate of 15% and as a result a total of \$9,276 has been recorded as a reserve in equity under the residual method.

As of December 31, 2014 the carrying value of the promissory notes payable approximated fair value due to the short term nature of the notes. Significant inputs include the market interest rate which varies from the stated rate and is a level 1 input.

On July 31, 2015, prior to the Transaction, HSI settled these notes payable by issuing 87,681 common shares with a fair value of \$58,264 and cash of \$20,500.

NOTE 11 – CONVERTIBLE NOTES PAYABLE

During the year ended December 31, 2014, HSI issued \$85,000 of unsecured convertible promissory notes, which are convertible as follows: into one share of the HSI's common stock and one warrant for every two dollars of convertible promissory notes, exercisable for 3 years at \$1.50 share, from date of conversion; or in the event the note is not repaid within the 2 year term the note is convertible into 1 share of common stock and 1 warrant for every two dollars of convertible promissory note, exercisable for 3 years at \$1.50 per share, from date of conversion.

The convertible promissory notes have a term of 2 years and bear an interest rate of 10% per annum, paid on a quarterly basis, beginning October 1, 2014.

HSI classified these notes into debt and derivative components as a result of the ability to convert at a variable number of shares. As HSI was unable to reliably determine the fair value the derivative liability, the fair value of the debt component was calculated as the present value of the required interest and principal payments that would have been applicable to non-convertible debt using a market rate of 15% per annum. The value of the derivative liability was determined to be insignificant and the debt has been recorded at its face value at initial recognition and at December 31, 2015 and 2014.

On August 21, 2015, prior to the Transaction, HSI settled the \$85,000 unsecured convertible promissory notes and accrued interest by issuing 140,931 common shares with a fair value of \$93,586.

During the year ended December 31, 2015, HSI issued \$5,000 and \$210,317 (C\$265,000) of unsecured convertible promissory notes. The \$5,000 note bears interest at 8% per annum, is due 30 days from a capital raise of \$1,500,000 and is convertible into one share of HSI's common stock at \$0.67 per share or the same term as the Concurrent Financing (see Note 5). The C\$265,000 convertible promissory notes have a term of 8 months, bear an interest rate of 10% per annum, and are convertible at C\$0.10 per share. These notes were classified as derivative liabilities as the exercise price differs from the functional currency of HSI. Issuance costs of C\$26,565 were paid relating to the C\$ notes and are being accreted over the life of the notes. During the year ended December 31, 2015, HSI recognized \$9,276 in accretion of the issuance costs.

H-SOURCE HOLDINGS LTD.
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 11 – CONVERTIBLE NOTES PAYABLE-CONT

The Company classified these notes into debt and derivative components. As the Company was unable to reliably determine the fair value of the derivative liability, the fair value of the debt component was calculated as the present value of the required interest and principal payments that would have been applicable to non-convertible debt using a market rate of 15% per annum. The fair value of the derivative liability was determined to be insignificant and the debt has been recorded at its amortized cost.

On July 31, 2015, prior to the Transaction, HSI settled the \$5,000 convertible promissory notes by issuing 7,842 common shares.

On August 31, 2015, the \$210,317 (C\$265,000) convertible promissory notes and accrued interest of \$13,699 were converted into 2,774,149 common shares of the Company.

On September 3, 2015, the Company entered into two promissory notes for a total of \$55,629 (C\$75,000). The promissory notes are unsecured, non-interest bearing and payable on demand at any time after October 28, 2015. In consideration, a total of 200,000 bonus shares with a fair value of \$17,305 were issued. As at December 31, 2015, the promissory notes were repaid in full.

NOTE 12 – SHARE CAPITAL

Authorized common shares

The authorized share capital of the Company is unlimited number of common shares without par value.

Issued shares

- a) Prior to the Transaction, HSI issued 281,325 shares for \$186,050 cash, 699,041 shares for services valued at \$465,984, settled a convertible promissory note on July 31, 2015 valued at \$5,000 with 7,842 shares (Note 11), settled a promissory note on July 31, 2015 with 87,681 shares that is valued at \$58,264 (Note 10), and settled a convertible promissory note on August 21, 2015 for 140,391 shares that is valued at \$93,586 (Note 11).
- b) On August 31, 2015, the Company completed the Transaction by acquiring all of the issued and outstanding common shares of HSI in consideration for 20,000,000 common shares of the Company with a value of C\$0.15 per share. The Company paid 1,000,000 shares as finder's fee in connection with the completion of the Transaction at a deemed price of C\$0.15 per share (Note 5).
- c) On August 31, 2015, the Company completed its private placement of an aggregate of 17,587,333 common shares at a price of C\$0.15 per share for aggregate gross proceeds of \$1,993,348 (C\$2,638,100). The Company paid an aggregate of \$180,671 (C\$239,109) in finder's fee and issued an aggregate of 1,319,050 finders' warrants, each of which is exercisable into one share at a price of C\$0.15 per share for a period of two years, expiring August 31, 2017. The warrants were valued at fair value of \$78,023 (C\$103,260) and was estimated using the Black-Scholes Option Pricing Model with the following assumptions at the issue date: risk free interest rate of 0.58%; dividend yield of 0%; expected volatility of 100%; and expected life of 2 years.
- d) On August 31, 2015, convertible promissory notes with a face value of \$260,317 (C\$265,000) and accrued interest of \$9,565 were converted into 2,774,149 common shares of the Company (Note 11).
- e) On December 31, 2015, the Company issued 200,000 common shares valued at \$17,305 as bonus shares in relation to the promissory note entered on September 3, 2015 (Note 11).
- f) On December 31, 2015, the Company issued 833,333 common shares at C\$0.12 to settle \$208,987 debt payable for legal services relating to the Transaction. As a result of the settlement, the Company recognized \$136,883 in gain from settlement that offset listing cost.
- g) On March 31, 2016, the Company issued 700,000 common shares at C\$0.15 for advisory services that amounted to \$80,611.

H-SOURCE HOLDINGS LTD.
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 12 – SHARE CAPITAL-CONT

- h) On April 1, 2016, the Company issued 700,000 common shares at C\$0.20 to settle \$107,950 for advisory services. As a result of the settlement, the Company recognized \$26,987 in loss from settlement.
- i) On April 1, 2016, the Company issued 2,000,000 common shares at C\$0.15 to settle \$308,428 for termination fees. As a result of the settlement, the Company recognized \$77,107 in loss from settlement.
- j) On April 18, 2016, the Company completed a non-brokered private placement of 18,753,141 common shares priced C\$0.15 per common share for net proceeds of \$2,177,253.

Share purchase option compensation plan

The Company has adopted a Stock Option Plan (the “Plan”) pursuant to which options may be granted to directors, officers, employees and consultants of the Company. Under the terms of the Plan, the Company can issue a maximum of 10% of the issued and outstanding common shares at the time of the grant, and the exercise price of each option is equal to or above the market price of the common shares on the grant date. Options granted under the Plan including vesting and the term, are determined by, and at the discretion of, the Board of Directors.

The continuity of stock options for the period ended June 30, 2016 is as follows:

	June 30, 2016		December 31, 2015	
	Number of Options	Weighted Average Exercise Price C\$	Number of Options	Weighted Average Exercise Price C\$
Options outstanding, beginning of the year	2,149,020	\$0.15	-	-
Granted	600,000	\$0.15	2,149,020	\$0.15
Cancelled	(50,000)	\$0.15	-	-
Options outstanding, end of the period	2,699,020	\$0.15	2,149,020	\$0.15
Options exercisable, end of the period	2,381,765	\$0.15	1,797,255	\$0.15

The options outstanding at June 30, 2016 are as follows:

Number Outstanding	Weighted Average Life	Expiry Date
2,149,020	4.17 years	August 31, 2020
400,000	4.51 years	January 1, 2021
150,000	4.58 years	January 28, 2021

On August 31, 2015, the Company granted 1,680,000 options to directors, officers, and a consultant of the Company. The options are exercisable at C\$0.15, vested immediately and expire on August 31, 2020. The Company recorded a share based payment amount of \$140,383. The Company used the Black-Scholes Option Pricing Model to estimate the fair value of the options using the following assumptions: risk free interest rate of 0.58%; dividend yield of 0%; expected volatility of 100%; and expected option life of 5 years.

On August 31, 2015, the Company granted 469,020 options to a consultant of the Company. The options are exercisable at C\$0.15 and expire on August 31, 2020. The options vest as to ¼ on November 30, 2015 and ¼ every quarter thereafter. As at June 30, 2016, the vested options are valued at \$35,347 using the Black-Scholes Option Pricing Model to estimate the fair value of the options using the following assumptions: risk free interest rate of 0.58%; dividend yield of 0%; expected volatility of 100%; and expected option life of 5 years.

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NOTE 12 – SHARE CAPITAL-CONT

On January 1, 2016, the Company granted 400,000 options to employees of the Company. The options are exercisable at C\$0.15 and expire on January 1, 2021. The options vest every quarterly. As at June 30, 2015, the options are valued at \$12,564 using the Black-Scholes Option Pricing Model to estimate the fair value of the options using the following assumptions: risk free interest rate of 0.61%; dividend yield of 0%; expected volatility of 100%; and expected option life of 5 years.

On January 28, 2016, the Company granted 200,000 options to consultants of the Company. The options are exercisable at C\$0.15, vested immediately and expire on January 28, 2021. As at June 30, 2016, 50,000 options were cancelled. The Company recorded a share based payment amount of \$8,353. The Company used the Black-Scholes Option Pricing Model to estimate the fair value of the options using the following assumptions: risk free interest rate of 0.61%; dividend yield of 0%; expected volatility of 100%; and expected option life of 5 years.

Option pricing models require the use of highly subjective estimates and assumptions including the expected stock price volatility. Changes in the underlying assumptions can materially affect the fair value estimates and therefore, in management’s opinion, existing models do not necessarily provide reliable measure of the fair value of the Company’s stock options.

D. Share Purchase Warrants

The following table summarizes the continuity of share purchase warrants:

	June 30, 2016		December 31, 2015	
	Number of Warrants	Weighted Average Exercise Price C\$	Number of Warrants	Weighted Average Exercise Price
Warrants outstanding, beginning of the year	1,319,050	\$0.15	-	-
Issued	-	-	1,319,050	\$0.15
Warrants outstanding, end of the period	1,319,050	\$0.15	1,319,050	\$0.15

	Exercise Price C\$	Weighted Average Remaining Life	Expiration Date
Number of Warrants outstanding	\$0.15	1.42	August 31, 2017

The fair value of warrants issued during the year as finder’s fee for the private placement that closed on August 31, 2015 was estimated using the Black-Scholes Option Pricing Model with the following assumptions at the issue date: risk free interest rate of 0.58%; dividend yield of 0%; expected volatility of 100%; and expected life of 2 years. The warrants are valued at \$78,023 and was included in share issuance cost.

E. Escrow shares

As at June 30, 2016, the Company had 7,389,124 common shares held in escrow (2015 – 8,866,949).

H-SOURCE HOLDINGS LTD.
NOTES TO INTERIM CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 13 – SUPPLEMENTAL CASH FLOW INFORMATION

	June 30, 2016	June 30, 2015
Interest paid in cash	\$ -	\$ -
Income taxes paid in cash	-	-

INVESTING AND FINANCING NON-CASH TRANSACTIONS

	June 30, 2016	June 30, 2015
Shares issued for services and termination fees	\$ 496,989	\$ -
Share-based payments	39,554	-
Shares issued for software development costs	-	36,085
Shares issued for settlement of accounts payable	-	203,738
Shares issue costs incurred but not paid	-	172,835

NOTE 14 – RELATED PARTY TRANSACTIONS

Related party transactions are as follows:

Summary of key management (officers and directors) personnel compensation:

	June 30, 2016	June 30, 2015
<u>Key management compensation</u>	<u>\$ 112,500</u>	<u>\$ 154,753</u>

Key management compensation includes the following:

In fiscal year 2015, a total of 1,918,358 shares with a fair value of \$233,310 were issued by the Company for settlement of fees and wages owing to the CEO and Director and President and Director for services provided.

In fiscal year 2015, \$36,157 has been capitalized to deferred software development costs for the CEO and Director and President and Director.

In fiscal year 2015, one of the Directors of the Company settled his convertible debenture and interest accrued of \$5,000 for 7,842 common shares of the Company.

In fiscal year 2015, the President of the Company settled his promissory note and interest accrued of \$11,150 for 86,366 common shares of the Company.

NOTE 15 – COMMITMENTS

On January 15, 2016, the Company entered into a termination fee and advisory agreement (the “Agreement”) with BayFront Capital Holdings, Ltd. (“BayFront”). Pursuant to the Agreement, on April 1, 2016, the Company paid BayFront \$308,428 settled in common shares at C\$0.20 per common share, in connection with the provision of certain advisory services and the termination of a prior agreement between the parties. In addition, the Company engaged BayFront to provide additional advisory and document preparation services to June 30, 2016 for a fee in the amount of \$188,561, which was also settled with common shares at C\$0.15 and C\$0.20 per common share (Note 12).

As at June 30, 2016, 3,400,000 common shares in total were issued to BayFront in connection with the Agreement with a value of \$496,989.

H-SOURCE HOLDINGS LTD.
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NOTE 16 – SUBSEQUENT EVENTS

- a) On July 25, 2016, the Company listed on the TSX Venture Exchange and de-listed from the CSE. The Company's common shares still trade under the ticker symbol "HSP".
- b) On August 9, 2016, the Company granted 300,000 stock options to a director. The options are exercisable at C\$0.15 and expire on August 9, 2021.