



H-SOURCE HOLDINGS LTD.
CONSOLIDATED FINANCIAL STATEMENTS
FOR THE PERIOD ENDED JUNE 30, 2018
(EXPRESSED IN US DOLLARS)

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

	Notes	June 30, 2018 \$	December 31, 2017 \$
ASSETS			
Current Assets			
Cash		390,613	56,426
Short-term investments	5	94,925	94,058
Prepaid expenses		96,090	167,632
Accounts receivable		84,326	41,275
Inventory		150,983	12,592
Total Current Assets		816,937	371,983
Patents	7	98,618	95,964
Software development costs	7	287,777	380,043
TOTAL ASSETS		1,203,332	847,990
LIABILITIES			
Current Liabilities			
Accounts payable and accrued liabilities	8	508,016	242,475
Due to related parties	12	47,925	-
Loan payable	9	187,377	-
TOTAL LIABILITIES		743,318	242,475
SHAREHOLDERS' EQUITY			
Common shares	10	9,004,767	7,924,721
Reserves		621,117	570,305
Deficit		(9,197,138)	(7,865,984)
Accumulative other comprehensive (loss)		31,268	(23,527)
Total Shareholders' Equity		460,014	605,515
TOTAL LIABILITIES AND SHAREHOLDERS' EQUITY		1,203,332	847,990

Nature and continuance of operations (Note 2)
Subsequent Events (Note 13)

On behalf of the board:

“John Kupice” Director
John Kupice

“Murray Walden” Director
Murray Walden

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

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

		Three Months Ended		Six Months Ended	
	Notes	June 30, 2018	June 30, 2017	June 30, 2018	June 30, 2017
		\$	\$	\$	\$
Revenue		440,900	7,439	682,261	7,439
Cost of Sales		(256,502)	-	(444,182)	-
		184,398	7,439	238,079	7,439
Commission revenue (net)		30,212	-	83,309	-
		214,610	7,439	321,388	7,439
Expenses					
Advertising and promotion		12,843	65,755	38,300	99,205
Amortization	7	49,005	-	97,859	-
Consulting fees		50,716	73,109	125,874	168,516
General and administration expenses	6	206,194	136,087	475,808	294,635
Professional fees		50,055	6,976	93,501	5,690
Salaries and benefits		538,213	296,431	809,659	515,098
		(907,026)	(578,358)	(1,641,001)	(1,083,144)
Income Before Other Income (Expenses)					
Interest income		680	5,718	2,143	6,715
Interest and other finance costs, net		(13,265)	(316)	(13,684)	(632)
Net Loss for the Period		(705,001)	(565,517)	(1,331,154)	(1,069,622)
Other Comprehensive Loss					
Foreign exchange gain		(4,612)	20,935	54,795	37,263
Net and Comprehensive Loss for the Period		(709,613)	(544,582)	(1,276,359)	(1,032,359)
Basic and Diluted Loss Per Share		(0.01)	(0.01)	(0.01)	(0.01)
Weighted Average Number of Common Shares Outstanding		105,924,705	87,978,505	105,637,205	81,915,783

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

H-SOURCE HOLDINGS LTD.

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

	Common Shares			Accumulative Other Comprehensive Income (Loss)	Accumulated Deficit	Shareholders' Equity
	Number of Shares	\$	Reserves \$	\$	\$	\$
Balance – December 31, 2016	70,088,505	5,782,979	467,039	(84,739)	(5,198,310)	966,969
Shares issued for cash on private placement, net of issuance costs	17,890,000	2,012,385	150,107	-	-	2,167,441
Net loss and comprehensive loss for the period	-	-	-	37,263	(1,069,622)	(1,032,359)
Balance – June 30, 2017	87,978,505	7,795,364	617,416	(47,476)	(6,267,932)	2,097,102
Shares issued for cash on private placement, net of issuance costs	17,250,000	1,080,046	50,812	-	-	1,130,858
Shares issued from warrants exercise	520,200	93,902	(32,512)	-	-	61,390
Shares issued from options exercise	176,000	35,455	(14,329)	-	-	21,126
Net loss and comprehensive loss for the period	-	-	-	78,744	(2,929,206)	(2,850,462)
Balance – June 30, 2018	105,924,705	9,004,767	621,117	31,268	(9,197,138)	460,014

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)

	June 30, 2018	June 30, 2017
	\$	\$
Cash provided by (used in):		
Operating activities		
Net loss for the period	(1,331,154)	(1,069,622)
Items not involving cash:		
Amortization	97,859	-
Changes in non-cash operating working capital:		
Accounts receivable	(43,595)	(44,201)
Prepaid expenses	71,073	(55,592)
Inventory	(138,391)	-
Accounts payable and accrued liabilities	269,743	10,934
Interest accrual	13,073	-
Due to related parties	47,925	-
Net cash used in operating activities	(1,013,467)	(1,158,481)
Cash flows from investing activities:		
Short-term investments	(5,316)	(745,941)
Patents	(8,247)	(3,723)
Software development	-	(142,253)
Net cash (used in) provided by investing activities	(13,563)	(891,917)
Cash flows from financing activities:		
Proceeds from share issuances, net share issuance costs	1,080,046	2,171,236
Loan	174,304	-
Net cash provided by financing activities	1,254,350	2,171,236
Effect of foreign exchange	106,867	36,883
Change in cash	227,320	120,838
Cash, beginning of the period	56,426	62,933
Cash, end of the period	390,613	220,654

Supplemental Cash Flow Information (Note 11)

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

H-SOURCE HOLDINGS LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Period Ended June 30, 2018
(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”. On August 9, 2017, H-Source, Inc. formed a new wholly owned subsidiary, H-Source Distribution-US, Inc. in the State of Washington.

This Transaction was accounted for as a reverse acquisition as the former shareholders of HSI 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”. As the Company did not qualify as a business according to the definition in IFRS 3, this Transaction did 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 September 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 consolidated financial statements of the Company were approved and authorized for issue by the Board of Directors on August 29, 2018.

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES

Statement of compliance with International Financial Reporting Standards

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, 2017 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.

H-SOURCE HOLDINGS LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Period Ended June 30, 2018
(Expressed in US Dollars)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CON'T

These consolidated financial statements include the accounts of H-Source Holdings Ltd., H-Source, Inc., and H-Source Distribution-US, 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 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 started realizing revenue during the year and has experienced net losses since inception. As of June 30, 2018, and December 31, 2017, the Company had an accumulated deficit of \$9,197,138 and \$7,865,984, respectively. For the periods ended June 30, 2018 and 2017, the Company had cash outflows from cash used in operating activities of \$1,013,467 and \$1,158,481, 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, generation of revenues, dependence on outside sources of capital, 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 additional cash resources to support infrastructure, network infrastructure, and sales and marketing efforts of its software platform. 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 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 the 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 CONSOLIDATED FINANCIAL STATEMENTS
For the Period Ended June 30, 2018
(Expressed in US Dollars)

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, 2018, the patents were in service and amortization of patents commenced in fiscal year 2017 using the straight-line method over a 10-year period.

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 fiscal year 2017 when commercial sales of the products commenced. 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 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).

Inventory

Inventory is stated at the lower of cost and net realizable value. Cost is determined on an average cost basis. Inventory costs include the purchase price and other costs directly related to the acquisition on of materials, and other costs incurred in bringing the inventories to their present location and condition. Net realizable value is the estimated selling price in the ordinary course of business less selling expenses.

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.

H-SOURCE HOLDINGS LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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(Expressed in US Dollars)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CON'T

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, 2018 and June 30, 2017.

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.

H-SOURCE HOLDINGS LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Period Ended June 30, 2018
(Expressed in US Dollars)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CON'T

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 loans and receivables as of June 30, 2018 and December 31, 2017.

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, 2018 and December 31, 2017.

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.

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.

Revenue

The Company recognizes revenue from product sales or services rendered when the following four criteria are met: persuasive evidence of an arrangement exists, shipping or delivery and acceptance has occurred, or service has been rendered, the selling price is fixed or determinable, and collectability is reasonably assured.

The Company evaluates whether it is appropriate to record the gross amount of product sales and related costs or the net amount earned as commissions. When the Company is primarily obligated in a transaction, are subject to inventory risk, have latitude in establishing prices and selecting suppliers, or have several but not all of these indicators, revenue is recorded at the gross sale price at the time of shipping. The Company records the net amounts as commissions earned if it is not primarily obligated and do not have latitude in establishing prices. Such amounts earned are determined using a percentage of seller revenues.

Product sales represent revenue from the sale of products and related shipping fees where the Company records revenue of gross sales price. Product sales and shipping revenues are recorded when the products are shipped and title passes to customers.

Service sales represent commissions earned. Service sales are recognized when service has been rendered.

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, 2018 and December 31, 2017.

H-SOURCE HOLDINGS LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Period Ended June 30, 2018
(Expressed in US Dollars)

NOTE 2 - SUMMARY OF SIGNIFICANT ACCOUNTING POLICIES-CON'T

Standards issued but not yet applied

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. The effective date for IFRS 9 is January 1, 2018. The Company has determined that the adoption of this standard has no impact 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 annual periods beginning on or after January 1, 2018, with early adoption permitted. The Company has determined that the adoption of this standard has no impact on its 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. As the Company does not have any leases, this standard is not expected to impact the 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 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.

H-SOURCE HOLDINGS LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
For the Period Ended June 30, 2018
(Expressed in US Dollars)

NOTE 3 – CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS-CON’T

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.

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, due to related parties, and loan payable.

	June 30, 2018	December 31, 2017
Financial Assets		
Cash	\$390,613	\$ 56,426
Accounts receivable	84,326	41,275
Short-term investments	94,925	94,058
Total financial assets	\$569,864	\$ 191,759
Financial Liabilities		
Accounts payable and other accrued liabilities	\$508,016	\$ 242,475
Due to related parties	47,925	-
Interest accrual	13,073	-
Loan payable	174,304	-
Total financial liabilities	\$743,318	\$ 242,475

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

H-SOURCE HOLDINGS LTD.
NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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(Expressed in US Dollars)

NOTE 4 – FINANCIAL RISK AND CAPITAL MANAGEMENT-CON'T

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.

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 exchanges 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, 2018 or the year ended December 31, 2017.

NOTE 5 - SHORT TERM INVESTMENT

As at June 30, 2018, the Company has a short-term investment of \$94,925 (2017 - \$94,058) with a major financial institution and \$480.48 interest receivable due on January 16, 2019. The short-term investment has an annual yield of prime minus 2.15%.

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 6 – GENERAL AND ADMINISTRIVE EXPENSES

	Three months June 30, 2018	Three months June 30, 2017	Six months June 30, 2018	Six months June 30, 2017
Office	\$(8,297)	\$49,660	\$106,610	\$88,795
Rent	15,448	10,490	30,897	20,980
Revenue tax	2,134	-	2,134	-
Software expense	148,623	43,609	245,791	89,677
Transfer agent and regulatory fees	9,800	8,068	21,611	31,847
Travel	38,486	24,260	68,765	63,336
	\$206,194	\$136,087	\$475,808	\$294,635

NOTE 7 – INTANGIBLE ASSETS

Cost	Patents	Software development costs
At December 31, 2016	97,063	553,599
Additions	9,563	-
Amortization	(10,662)	(173,556)
At December 31, 2017	\$ 95,964	\$ 380,043
Additions	8,247	-
Amortization	(5,593)	(92,266)
At June 30, 2018	\$ 98,618	\$287,777

NOTE 8 – ACCOUNTS PAYABLE AND ACCRUED LIABILITIES

	June 30, 2018	December 31, 2017
Accounts payable	\$471,986	\$ 181,123
Accrued payroll and taxes	36,030	61,352
	\$508,016	\$ 242,475

NOTE 9 – LOAN

On April 16, 2018, the Company entered into a term sheet whereby certain non-arm's length parties (the "Lenders") advanced \$174,304 to the Company as a loan (the "Loan"). The Loan bears an interest rate of 3% per month (36% per annum), calculated and payable monthly in arrears. The term of the Loan is 120 days commencing on the date on which the principal amount is advanced to the Company. As at June 30, 2018, \$13,073 was accrued as interest.

On April 16, 2018, the Company entered into a memorandum of understanding with the same Lenders as the Loan whereby the Loan is to be used by the Company to purchase certain assets. If the sale of the assets occurs on or before 60 days after the purchase, 15% of the net proceeds shall be paid to the Lenders and the Company will retain the remainder. If the sale of the assets occurs 60 days after, 50% of the net proceeds shall be paid to the Lenders and the Company will retain the remainder.

NOTE 10 – SHARE CAPITAL

Authorized common shares

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

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NOTES TO CONSOLIDATED FINANCIAL STATEMENTS
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NOTE 10 – SHARE CAPITAL-CON’T

Issued shares

- a) On March 31, 2016, the Company issued 700,000 common shares at C\$0.15 for advisory services that amounted to \$80,611 (C\$105,000).
- b) On April 1, 2016, the Company issued 700,000 common shares at C\$0.20 to settle \$107,950 (C\$140,000) for advisory services. As a result of the settlement, the Company recognized \$26,987 in loss from settlement.
- c) On April 1, 2016, the Company issued 2,000,000 common shares at C\$0.15 to settle \$308,428 (C\$400,000) for termination fees. As a result of the settlement, the Company recognized \$77,107 in loss from settlement.
- d) On April 18, 2016, the Company completed a non-brokered private placement of 18,753,141 common shares at a price of C\$0.15 per common share for net proceeds of \$2,177,253 (C\$2,804,872).
- e) On March 3, 2017, the Company completed a brokered private placement of 17,890,000 common shares at a price of C\$0.18 per share for gross proceeds of \$2,410,400 (C\$3,220,200). The Company paid the agent a cash commission of \$247,908 and issued 1,304,141 agent compensation options. Each compensation option is exercisable into one common share of the Company at C\$0.18 for a period of 18 months from the closing of the offering. The fair value of the options was determined to be \$150,107.
- f) During fiscal year 2017, 520,200 warrants and 176,000 stock options were exercised at C\$0.15 each.
- g) On January 4, 2018, the Company completed a brokered private placement of 17,250,000 common shares at a price of C\$0.10 per share for gross proceeds of \$1,286,850 (C\$1,725,000). The Company paid the agent a cash commission of \$95,814 and issued 1,284,376 agent compensation options. Each compensation option is exercisable into one common share of the Company at C\$0.10 for a period of 18 months from the closing of the offering. The fair value of the options was determined to be \$50,812.

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, 2018 and year ended December 31, 2017 is as follows:

	June 30, 2018		December 31, 2017	
	Number of	Weighted Average	Number of	Weighted Average
	Options	Exercise Price	Options	Exercise Price
		C\$		C\$
Options outstanding, beginning of the period	3,902,500	\$0.18	4,371,520	\$0.18
Exercised	-	-	(176,000)	\$0.15
Cancelled	-	-	(293,020)	\$0.15
Options outstanding, end of the period	3,902,500	\$0.18	3,902,500	\$0.18
Options exercisable, end of the period	3,902,500	\$0.18	3,902,500	\$0.18

The options outstanding at June 30, 2018 are as follows:

Number Outstanding	Weighted Average Life	Expiry Date
1,680,000	2.17 years	August 31, 2020
400,000	2.51 years	January 1, 2021
300,000	3.11 years	August 9, 2021
1,522,500	1.34 years	October 31, 2019

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NOTE 10 – SHARE CAPITAL-CON’T

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. As at December 31, 2016, the options were fully vested and valued at \$25,671 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 and the Company recorded a share based payment amount of \$11,133. 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.

On August 9, 2016, the Company granted 300,000 options to a director of the Company. The options are exercisable at C\$0.15, vested immediately and expire on August 9, 2021. The Company recorded a share based payment amount of \$25,479. 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 0.54%; dividend yield of 0%; expected volatility of 100%; and expected option life of 5 years.

On October 31, 2016, the Company granted 1,272,500 stock options and 250,000 stock options to a director, employees and consultants of the Company at an exercise price of C\$0.205 and C\$0.325 respectively. The options expire on October 31, 2019 and the Company recorded a total share-based payment amount of \$140,875. 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 0.55%; dividend yield of 0%; expected volatility of 100%; and expected option life of 3 years.

During the year ended December 31, 2016, the Company also recorded a share-based payment amount of \$18,532 for options granted in fiscal year 2015 which vested in fiscal year 2016.

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.

Share purchase warrants

The following table summarizes the continuity of share purchase warrants:

	June 30, 2018		December 31, 2017	
	Number of Warrants	Weighted Average Exercise Price C\$	Number of Warrants	Weighted Average Exercise Price C\$
Warrants outstanding, beginning of the period	-	-	1,319,050	\$0.15
Exercised	-	-	(520,200)	\$0.15
Expired	-	-	(798,850)	\$0.15
Warrants outstanding, end of the period	-	-	-	-

Compensation options

On March 3, 2017, the Company issued 1,304,141 agent compensation options. Each compensation option is exercisable into one common share of the Company at C\$0.18 to September 3, 2018. The fair value of the compensation options of \$150,107 included in share issuance cost was estimated using the Black-Scholes Option Pricing Model with the following assumptions at the issue date: risk free interest rate of 0.76%; dividend yield of 0%; expected volatility of 100%; and expected life of 1.5 years.

On January 4, 2018, the Company issued 1,284,375 agent compensation options. Each compensation option is exercisable into one common share of the Company at C\$0.10 to July 4, 2019. The fair value of the compensation options of \$50,812

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NOTE 10 – SHARE CAPITAL-CON’T

included in share issuance cost was estimated using the Black-Scholes Option Pricing Model with the following assumptions at the issue date: risk free interest rate of 1.68%; dividend yield of 0%; expected volatility of 49.15%; and expected life of 1.5 years.

	June 30, 2018		December 31, 2017	
	Number of options	Weighted Average Exercise Price C\$	Number of options	Weighted Average Exercise Price C\$
Options outstanding, beginning of the period	1,304,141	\$0.09	-	-
Issued	1,284,375	\$0.05	1,304,141	\$0.18
Options outstanding, end of the period	2,588,515	\$0.14	1,304,141	\$0.18

Escrow shares

As at June 30, 2018, the Company had 1,477,824 common shares held in escrow (2017 – 2,955,649).

NOTE 11 – SUPPLEMENTAL CASH FLOW INFORMATION

	June 30, 2018	June 30, 2017
Interest paid in cash	\$ -	\$ -
Income taxes paid in cash	\$ -	\$ -

Investing and financing non-cash transactions

	June 30, 2018	June 30, 2017
Agent compensation options issued as share issuance cost	\$ 50,812	\$ 150,107

NOTE 12 – RELATED PARTY TRANSACTIONS

Related party transactions are as follows:

Key management (officers and directors) personnel compensation including share-based payments for the period ended June 30, 2018 was \$150,000 (2017 - \$150,000).

As of June 30, 2018, \$31,950 (2017 - \$nil) and \$15,975 (2017 - \$nil) were accrued as bonuses for the Company’s CEO and president respectively.

NOTE 13 – SUBSEQUENT EVENTS

1. On July 12, 2018, the Company completed a brokered private placement of 7,666,667 common shares at a price of C\$0.15 per share for gross proceeds of \$873,425 (C\$1,150,000). The Company paid the agent a cash commission of \$ and issued 575,000 agent compensation options. Each compensation option is exercisable into one common share of the Company at C\$0.15 for a period of 18 months from the closing of the offering. The fair value of the options was determined to be \$38,932.
2. On August 1, 2018, the Company granted 1,770,000 stock options to directors, officers, and employees of the Company with an exercise price of \$0.16. The stock options shall have a term of 3 years. In addition, 1,050,000 restricted share units were awarded to officers and an employee. The restricted share units shall vest with respect to one-third on each anniversary of the date of each grant.