

Unaudited Condensed Interim Consolidated Financial Statements

HLS Therapeutics Inc.

For the Three Months Ended March 31, 2018

HLS THERAPEUTICS INC.**CONDENSED INTERIM CONSOLIDATED STATEMENTS OF FINANCIAL POSITION****Unaudited**

[in thousands of U.S. dollars]

	Notes	As at March 31, 2018	As at December 31, 2017
ASSETS			
Current			
Cash and cash equivalents		53,825	36,219
Accounts receivable	5	13,057	25,846
Inventories		1,088	1,354
Prepaid expenses and other current assets		1,563	1,617
Total current assets		69,533	65,036
Property, plant and equipment		421	441
Intangible assets		300,396	312,659
Restricted assets	6	14,635	5,555
Deferred tax asset		862	955
Total assets		385,847	384,646
LIABILITIES AND SHAREHOLDERS' EQUITY			
Current			
Accounts payable and accrued liabilities		11,029	12,596
Provisions	7	5,697	6,976
Other financial liabilities	8	12,724	14,160
Income taxes payable		153	870
Total current liabilities		29,603	34,602
Other financial liabilities	8	156,768	158,114
Deferred tax liability		9,757	11,548
Total liabilities		196,128	204,264
Shareholders' equity			
Share capital	9	211,482	192,743
Contributed surplus		12,424	12,330
Accumulated other comprehensive income		1,321	5,941
Deficit		(35,508)	(30,632)
Total shareholders' equity		189,719	180,382
Total liabilities and shareholders' equity		385,847	384,646

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

HLS THERAPEUTICS INC.
CONDENSED INTERIM CONSOLIDATED STATEMENTS OF LOSS
Unaudited

[in thousands of U.S. dollars, except per share amounts]

	Notes	Three months ended	
		March 31, 2018	March 31, 2017
Revenues	12	13,166	15,553
Expenses			
Cost of product sales		580	425
Selling and marketing		964	786
Medical, regulatory and patient support		977	906
General and administrative		2,053	1,888
Stock-based compensation	9	94	76
Amortization and depreciation		8,141	7,931
Operating income		357	3,541
Acquisition and transaction costs		435	—
Finance and related costs, net	8, 13	5,567	5,705
Loss before income taxes		(5,645)	(2,164)
Income tax expense (recovery)	11	(769)	868
Net loss for the period		(4,876)	(3,032)
Net loss per share:			
Basic and diluted	9	\$(0.19)	\$(0.12)

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HLS THERAPEUTICS INC.**CONDENSED INTERIM CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS****Unaudited**

[in thousands of U.S. dollars]

	Three months ended	
	March 31, 2018	March 31, 2017
Net loss for the period	(4,876)	(3,032)
Item that may be reclassified subsequently to net loss		
Unrealized foreign currency translation adjustment	(4,620)	1,362
Comprehensive loss for the period	(9,496)	(1,670)

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

HLS THERAPEUTICS INC.

CONDENSED INTERIM CONSOLIDATED STATEMENTS OF CHANGES IN SHAREHOLDERS' EQUITY

Unaudited

[in thousands of U.S. dollars]

	Note	Share capital	Contributed surplus	Accumulated other comprehensive income (loss)	Deficit	Total
Balance, December 31, 2017		192,743	12,330	5,941	(30,632)	180,382
Common shares issued	3	19,905	—	—	—	19,905
Share issuance costs		(1,166)	—	—	—	(1,166)
Stock-based compensation	9	—	94	—	—	94
Net loss for the period		—	—	—	(4,876)	(4,876)
Unrealized foreign currency translation adjustment		—	—	(4,620)	—	(4,620)
Balance, March 31, 2018		211,482	12,424	1,321	(35,508)	189,719
Balance, December 31, 2016		192,743	11,967	(4,611)	(24,535)	175,564
Stock-based compensation	9	—	76	—	—	76
Net loss for the period		—	—	—	(3,032)	(3,032)
Unrealized foreign currency translation adjustment		—	—	1,362	—	1,362
Balance, March 31, 2017		192,743	12,043	(3,249)	(27,567)	173,970

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

HLS THERAPEUTICS INC.
INTERIM CONSOLIDATED STATEMENTS OF CASH FLOWS
Unaudited

[in thousands of U.S. dollars]

		Three months ended	
	Notes	March 31, 2018	March 31, 2017
OPERATING ACTIVITIES			
Net loss for the period		(4,876)	(3,032)
Add (deduct) items not involving cash			
Stock-based compensation		94	76
Amortization and depreciation		8,141	7,931
Accrued interest	8	1,629	1,728
Fair value adjustment on financial assets and liabilities		(450)	10
Listing expense	3	435	—
Deferred income taxes	11	(889)	2
Net change in non-cash working capital balances	14	9,416	(3,379)
Cash provided by operating activities		13,500	3,336
INVESTING ACTIVITIES			
Additions to property, plant and equipment		(24)	—
Acquisitions	4, 8	(4,325)	(1,825)
Cash used in investing activities		(4,349)	(1,825)
FINANCING ACTIVITIES			
Common shares issued	3	19,470	—
Share issuance costs		(1,576)	—
Repayment of senior secured term loan	8	(7,104)	(3,870)
Increase in restricted cash		(2,000)	(700)
Lender royalty payment	8	(112)	(105)
Cash provided by (used in) financing activities		8,678	(4,675)
Net increase (decrease) in cash and cash equivalents during the period		17,829	(3,164)
Foreign exchange		(223)	(72)
Cash and cash equivalents, beginning of period		36,219	37,763
Cash and cash equivalents, end of period		53,825	34,527

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

HLS THERAPEUTICS INC.

Notes to the unaudited condensed interim consolidated financial statements

March 31, 2018

(all amounts are in thousands of U.S. dollars, except per share information, and unless otherwise noted)

1. CORPORATE INFORMATION

HLS Therapeutics Inc. (“HLS” or the “Company”) is a specialty pharmaceutical company, which acquires and commercializes pharmaceutical products for the North American markets.

The Company was incorporated as Heritage Life Sciences Inc. on June 5, 2014 under the *Business Corporations Act* (British Columbia). On December 18, 2014, the Company amended its articles to change its name to HLS Therapeutics Inc. As a result of the amalgamation described in note 3, on March 12, 2018, the Company continued under the *Business Corporations Act* (Ontario). The Company’s common shares are listed on the TSX Venture Exchange (the “Exchange”) under the symbol HLS.

The registered office, head office and principal address of the Company is located at 10 Carlson Court, Suite 410, Toronto, Ontario, M9W 6L2.

These unaudited condensed interim consolidated financial statements were authorized for issuance by the Board of Directors on May 15, 2018.

2. BASIS OF PREPARATION

Statement of compliance

These unaudited condensed interim consolidated financial statements have been prepared in accordance with International Accounting Standard 34, *Interim Financial Reporting* as issued by the International Accounting Standards Board (“IASB”). The IASB has not issued any significant new accounting standards that impact the Company since the preparation of the Company’s audited consolidated financial statements for the year ended December 31, 2017.

The accounting policies used in the preparation of these unaudited condensed interim consolidated financial statements conform with those used in the preparation of the Company’s audited consolidated financial statements for the year ended December 31, 2017, except for the newly adopted accounting policies discussed below.

These unaudited condensed interim consolidated financial statements do not include all the information and disclosures required in annual financial statements and, accordingly, should be read in conjunction with the Company’s audited consolidated financial statements for the year ended December 31, 2017.

Basis of measurement

These unaudited condensed interim consolidated financial statements have been prepared on a historical cost basis, except for certain financial instruments that are measured at fair value. The Company’s presentation currency is the United States dollar. All values are rounded to the nearest thousand (\$000), except where otherwise indicated.

Accounting standards adopted in the period

IFRS 9, *Financial Instruments* (“IFRS 9”)

The Company has adopted IFRS 9 on a modified retroactive basis in accordance with the transitional provisions of IFRS 9. Results for reporting periods beginning after January 1, 2018 are presented under IFRS 9, while prior reporting period amounts have not been restated.

HLS THERAPEUTICS INC.

Notes to the unaudited condensed interim consolidated financial statements

March 31, 2018

(all amounts are in thousands of U.S. dollars, except per share information, and unless otherwise noted)

IFRS 9 introduces new requirements for classifying and measuring financial instruments, the recognition of expected credit losses, and hedge accounting. The adoption of IFRS 9 had no impact on the Company's financial position or results of operations, and the Company's financial assets and financial liabilities continue to be measured on the same basis as was previously applied under IAS 39, *Financial Instruments: Recognition and Measurement*.

The classification of financial assets and liabilities (collectively, financial instruments) is typically determined at the time of initial recognition, within the following categories:

- Amortized cost
- Fair value through income or loss
- Fair value through other comprehensive income

Financial instruments carried at fair value through income or loss

Financial instruments in this category include lender warrants, preferred shares and foreign currency forward contracts.

Financial instruments carried at amortized cost

Financial instruments in this category include cash and cash equivalents, restricted cash, trade and other accounts receivable, accounts payable, purchase consideration, the senior secured term loan and the lender royalty.

Financial instruments in this category are recorded initially at fair value, and adjusted for directly attributable transaction costs and when material, a discount to reduce the payables to fair value. Financial instruments in this category are subsequently measured at amortized cost using the effective interest rate method. The effective interest rate accretion is included in *Finance and related costs, net* in the consolidated statement of loss.

IFRS 15, Revenue from Contracts with Customers ("IFRS 15")

The Company has adopted IFRS 15 effective January 1, 2018 on a modified retrospective basis in accordance with the transitional provisions of IFRS 15. Results for reporting periods beginning after January 1, 2018 are presented under IFRS 15, while prior reporting period amounts have not been restated and continue to be reported under IAS 18, *Revenue*.

IFRS 15 establishes a five-step model to account for revenue arising from contracts with customers and outlines two approaches to recognizing revenue: at a point in time or over time. New estimates and judgmental thresholds have been introduced, which may affect the amount and/or timing of revenue recognized. Under IFRS 15, revenue is recognized at an amount that reflects the consideration to which an entity expects to be entitled in exchange for transferring goods or services to a customer. The Company has adopted the new standard using the modified retrospective application method with no restatement of comparative information. The adoption did not have an impact on the Company's financial position or results of operations.

Revenue is recognized to the extent that it is probable that the economic benefits will flow to the Company and the revenue can be reliably measured, regardless of when the payment is received. Revenue is measured at the fair value of the consideration received or receivable, taking into account contractually defined terms of payment and excluding taxes or duties.

HLS THERAPEUTICS INC.

Notes to the unaudited condensed interim consolidated financial statements

March 31, 2018

(all amounts are in thousands of U.S. dollars, except per share information, and unless otherwise noted)

In the case of product sales, the determination of the fair value of consideration received or receivable includes a deduction for discounts, allowances given, provisions for chargebacks, other price adjustments and accruals for estimated future rebates and returns. The methodology and assumptions used to estimate rebates and returns include consideration of factors such as contractual terms and historical trends.

3. AMALGAMATION

On March 12, 2018, the Company completed a plan of arrangement (the "Arrangement") with Automodular Corporation ("AMD") in accordance with Section 183 of the *Business Corporations Act* (Ontario). Pursuant to the Arrangement, the Company and AMD amalgamated to form a new entity named HLS Therapeutics Inc. ("new HLS"), operating in the life sciences industry. The completion of the Arrangement resulted in a reverse takeover of AMD as defined in the policies of the Exchange. New HLS common shares commenced trading on the Exchange on March 14, 2018.

Under the Arrangement, AMD shareholders received, for each AMD share, one preferred share of new HLS and 0.165834 common share of new HLS, and HLS shareholders received, for each HLS share, one new HLS common share. At the completion of the Arrangement, former shareholders of HLS held approximately 92% of the outstanding common shares of new HLS. As a result, HLS is considered the acquiring company for accounting purposes.

HLS preferred shares were issued to former AMD shareholders to allow them to receive their pro rata share of proceeds from the settlement of AMD's pre-existing litigation and any residual funds that were in excess of AMD's commitment to deliver C\$25,000 to HLS on closing of the Arrangement. Prior to closing the Arrangement, AMD announced that it had reached a settlement related to the litigation. The settlement proceeds were then received by AMD on March 8, 2018 and such funds, along with the residual funds, are being held in escrow as at March 31, 2018.

The following table represents the fair value of the share-based consideration provided and net assets acquired in the Arrangement:

Consideration provided	
Fair value of 2,151,900 common shares at \$9.25 per share	19,905
Net assets acquired	
Net assets of AMD	26,581
Less escrow funds	7,111
Closing cash amount	19,470
Listing expense	435

The net assets acquired have been translated from Canadian dollars into United States dollars at an exchange rate of 0.7788.

HLS THERAPEUTICS INC.**Notes to the unaudited condensed interim consolidated financial statements****March 31, 2018**

(all amounts are in thousands of U.S. dollars, except per share information, and unless otherwise noted)

4. ASSET ACQUISITIONS**Trinomia®**

On November 20, 2017, the Company entered into an exclusive agreement with Ferrer Internacional SA ("Ferrer") for the rights to distribute and commercialize Trinomia® capsules in Canada. Trinomia® has been approved for use outside of Canada for the secondary prevention of cardiovascular events but is not approved for use in Canada. The Company paid C\$200 on signing with further obligations of up to an aggregate of C\$31,075 contingent upon achieving regulatory and sales-based milestones. The Company will also pay a royalty on the net sales of Trinomia® in Canada. Ferrer is obligated to supply finished product to the Company under negotiated supply terms.

The transaction has been accounted for as an asset purchase. The Company has capitalized \$208 to distribution rights in respect of this transaction.

Vascepa®

Effective September 25, 2017, the Company entered into an exclusive agreement with Amarin Corporation plc ("Amarin") to register, commercialize and distribute Vascepa® capsules in Canada. Vascepa® capsules are a single-molecule prescription product for the treatment of cardiovascular disease. Vascepa® is not approved for use in Canada, and the Company anticipates submitting an application to Canadian regulatory authorities to seek approval to commercialize Vascepa® in Canada.

Under the agreement, the Company will be responsible for regulatory and commercialization activities and associated costs. In addition to an initial payment of \$5,000 (of which \$2,500 was paid in March 2018), terms of the agreement include regulatory and sales-based milestone payments of up to an additional \$60,000, the timing and achievability of which cannot be determined at this time. Amarin is also entitled to a tiered double-digit royalty on net sales of Vascepa® in Canada. Amarin is obligated to supply finished product to the Company under negotiated supply terms.

The transaction has been accounted for as an asset purchase. The Company has capitalized \$5,346 to distribution rights in respect of this transaction.

5. ACCOUNTS RECEIVABLE

	March 31, 2018	December 31, 2017
Trade accounts receivable	8,368	13,671
Royalty receivable	1,535	8,699
Other receivables	3,154	3,476
	13,057	25,846

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(all amounts are in thousands of U.S. dollars, except per share information, and unless otherwise noted)

6. RESTRICTED ASSETS

	March 31, 2018	December 31, 2017
Restricted cash for collateral	7,555	5,555
Escrow funds	7,080	—
	14,635	5,555

As described in note 3, escrow funds represent the net assets of AMD in excess of AMD's commitment to deliver C\$25,000 to HLS on closing of the Arrangement. The escrow funds consist of cash as well as other legacy working capital items. The payment of expenses related to escrow activity will be funded by the escrow funds. The holders of the preferred shares are only entitled to distributions from the escrow funds.

7. PROVISIONS

	Chargebacks and rebates	Returns	Total
As at December 31, 2017	4,187	2,789	6,976
Charges	670	152	822
Utilization	(1,851)	(250)	(2,101)
As at March 31, 2018	3,006	2,691	5,697

8. OTHER FINANCIAL LIABILITIES

	March 31, 2018	December 31, 2017
Current		
Lender warrants	3,288	2,875
Foreign currency forward contract	213	991
Purchase consideration	9,223	10,294
	12,724	14,160
Non-current		
Foreign currency forward contract	—	85
Senior secured term loan	130,563	136,706
Lender royalty	3,468	3,507
Purchase consideration	15,657	17,816
Preferred shares	7,080	—
	156,768	158,114
	169,492	172,274

Lender warrants

On August 11, 2015, the Company issued lender warrants to the lenders under the senior secured term loan. These lender warrants give the lenders the right to acquire 1,164,000 common shares at an exercise price of \$11 per share until August 11, 2020. On April 1, 2016, an additional 100,008 lender warrants were issued and the exercise price of all the lender warrants was reduced to \$10.13 per share. As a result of the amalgamation described in note 3, the term of the lender

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(all amounts are in thousands of U.S. dollars, except per share information, and unless otherwise noted)

warrants was extended to August 11, 2021 and an additional 32,000 lender warrants were issued for no consideration.

The terms of the lender warrants include a net settlement provision and thus are presented as a liability.

As at March 31, 2018, the total fair value of the 1,296,008 lender warrants was determined to be \$3,288 and the Company recorded an expense of \$413 in fiscal 2018 (2017 – income of \$134) related to the revaluation of the lender warrants. Fair value at issuance and at subsequent remeasurement dates was determined using the Black-Scholes option pricing model with a volatility assumption of 42%.

Fair value as at December 31, 2017	2,875
Change in fair value	413
Fair value as at March 31, 2018	3,288

Foreign currency forward contract

In May 2017, the Company entered an agreement with a bank to sell Cdn\$18,000 to the bank at the specified Canadian to U.S. forward rate of \$1.3700 on various settlement dates through July 2018, unless the spot rate on a settlement date is between \$1.3197 and \$1.3700 in which case the Company is relieved of its obligation for that settlement date. In November 2017, this agreement was extended to March 2019. In each month from August 2018 to March 2019, the Company will sell to the bank at the specified Canadian to U.S. forward rate of \$1.2672 either C\$1,500 or C\$2,000, depending on whether the spot rate on the settlement date is above or below \$1.2672.

This contract is not designated as a hedge for accounting purposes and is measured at fair value at each reporting date. Fair value is determined using prices referenced by the counterparty to the contract, taking into account the credit quality of the counterparty.

The Company recognized a realized loss of \$276 and an unrealized gain of \$863 for the period ended March 31, 2018 in respect of this foreign currency forward contract (2017 – realized gain of \$86 and unrealized loss of \$144). Both the realized loss and unrealized gain are included in finance and related costs in the consolidated statement of net loss.

The maturities of the foreign currency forward contract as at March 31, 2018 are as follows:

	Forward rate	Cdn\$	Fair value
April to July 2018	1.3700	6,000	267
August 2018 to March 2019	1.2672	12,000 to 16,000	(54)
			213

Senior secured term loan

On August 11, 2015, the Company entered into a senior secured term loan with a syndicate of private lenders. The aggregate principal amount of the initial term loan was \$185,000. The Company may request to be provided with incremental loans, for a maximum additional loan amount of \$150,000. The maturity date is August 11, 2021. Interest on the loan accrues at a rate per annum equal to the sum of (i) 9.0% plus (ii) the higher of (a) the LIBOR rate for the applicable interest period and (b) 1.0%.

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(all amounts are in thousands of U.S. dollars, except per share information, and unless otherwise noted)

Under the terms of the senior secured term loan, the lenders have security over substantially all of the assets of the Company. At the discretion of the lenders, the Company may be required to make quarterly principal repayments based on the operating cash flows received in the previous quarter. The Company may make additional principal repayments subject to a repayment premium.

Under the terms of the senior secured term loan, the Company is required to comply with financial covenants related to the maintenance of minimum revenue, liquidity and leverage ratios, and to place a maximum on capital expenditures. Throughout the period ended March 31, 2018, the Company was in compliance with the financial covenants.

The fair value of lender warrants issued and transaction costs associated with the senior secured term loan has been included as a reduction to the carrying amount of the liability and will be amortized through interest expense using the effective interest rate method.

Carrying amount as at December 31, 2017	136,706
Repayment	(7,104)
Accreted interest	961
Carrying amount as at March 31, 2018	130,563

The terms of the senior secured term loan include an interest rate floor and a prepayment option, both of which are considered to be embedded derivatives. Management has determined that the interest rate floor is closely related to the contract and therefore bifurcation of the fair value of the interest rate floor is not required. Management has determined that the fair value of the prepayment option is not significant and thus has not accounted for it separately.

Lender royalty

On August 11, 2015, the Company entered into a royalty agreement with an investor who was both a member of the lending syndicate and a participant in the private placement. This agreement entitles the investor to receive a royalty on net sales for a period of up to 14 years commencing in August 2016.

The Company ascribed a fair value of \$3,481 to this agreement, which amount was accounted for as a proportionate reduction to (i) the carrying amount of the senior secured term loan; and (ii) the proceeds of the private placement. Fair value was determined by using a discounted cash flow methodology.

Carrying amount as at December 31, 2017	3,507
Payment	(112)
Accreted interest	73
Carrying amount as at March 31, 2018	3,468

Purchase consideration

As part of the consideration for the acquisition of Absorica[®], the Company is obligated to make fixed quarterly and semi-annual payments of approximately \$38,850 during the period from July 2016 through 2020. This obligation has been recorded at the present value of deferred payments using a discount rate of 10%. Interest expense on this obligation amounted to \$595 for the period ended March 31, 2018 (2017 – \$711).

HLS THERAPEUTICS INC.**Notes to the unaudited condensed interim consolidated financial statements****March 31, 2018**

(all amounts are in thousands of U.S. dollars, except per share information, and unless otherwise noted)

As part of the consideration for the acquisition of the Vascepa® rights in fiscal 2017, the Company made a further non-refundable upfront payment of \$2,500 in March 2018.

Carrying amount as at December 31, 2017	28,110
Additions	500
Payment	(4,325)
Accreted interest	595
Carrying amount as at March 31, 2018	24,880
Less current portion	9,223
Non-current portion	15,657

Preferred shares

Under the Arrangement described in note 3, the Company issued 12,976,227 preferred shares to the former shareholders of AMD.

As a condition to closing the Arrangement, the parties to the Arrangement entered into a claims administration and escrow agreement, the purpose of which is to establish the administration of the escrow funds, the funding of AMD litigation and any other AMD legacy matters. Escrow funds on closing of the Arrangement were defined to include AMD cash in excess of the closing cash amount (defined to be C\$25,000), as well as the receivables and payables of AMD at the date of closing. The escrow funds are available and intended to redeem the preferred shares, and as a result the preferred shares are presented as a liability.

The preferred shares are not entitled to receive any dividends and have no voting rights. The preferred shares are measured at fair value, which is estimated to be the net balance of the escrow funds.

9. SHARE CAPITAL

The Company is authorized to issue an unlimited number of common shares.

Issued and outstanding

The issued and outstanding common shares as at March 31, 2018 are as follows:

	#	\$
Balance as at December 31, 2017	25,277,997	192,743
Common shares issued on amalgamation	2,151,900	18,739
Balance as at March 31, 2018	27,429,897	211,482

Performance share units ("PSUs")

The Company issued 1,040,000 PSUs to members of senior management. Each PSU entitles the holder to receive one common share if the terms and conditions of the PSU plan are met. These terms include share price targets to be achieved prior to expiry on the fifth anniversary of the date of grant on June 25, 2020. Management has determined that the fair value of this grant on the issuance date is not significant, and thus has recorded no expense in respect of these PSUs.

As a result of the amalgamation described in note 3, the ability of the holders to exercise the PSUs is suspended while the Company is listed on an exchange that does not permit price-based vesting.

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(all amounts are in thousands of U.S. dollars, except per share information, and unless otherwise noted)

Stock option plan

Under the Company's Stock Option Plan (the "Plan"), the Company may grant options to purchase common shares to eligible officers, directors and employees of, or consultants to, the Company. The number of common shares that the Company is authorized to issue under the Plan is 2,328,000. All options granted are for terms not to exceed 10 years from the grant date. Options granted under the Plan vest over four years from the date of grant, with the exception of certain options granted to senior management in fiscal 2015, which vested immediately upon grant.

A summary of the changes to the stock options outstanding is presented as follows:

	Number of options (#)	Weighted average exercise price per share (\$)
Outstanding as at December 31, 2017	1,299,475	10.00
Granted	90,995	9.25
Outstanding as at March 31, 2018	1,390,470	9.95

As at March 31, 2018, the options outstanding and exercisable consist of the following:

Exercise price (\$)	Options outstanding		Options exercisable	
	Number outstanding (#)	Weighted average remaining contractual life (years)	Number outstanding (#)	Weighted average exercise price (\$)
9.25	90,995	10.0	—	—
10.00	1,299,475	7.5	1,114,709	10.00
	1,390,470	7.7	1,114,709	10.00

The fair value of each option granted since inception of the Plan was estimated on the date of the grant using the Black-Scholes option pricing model. The estimated fair value of the options is amortized to income over the options' vesting period on a straight-line basis. In fiscal 2018, the Company has recorded stock-based compensation expense of \$94 (2017 – \$76). This charge has been credited to contributed surplus. Unrecognized stock-based compensation expense as at March 31, 2018 related to the Plan was \$779.

Warrants

On August 11, 2015, the Company issued additional lender warrants to a member of the lending syndicate. These lender warrants give the lender the right to acquire 1,164,000 common shares at an exercise price of \$0.01 per share if the share price hits certain targets prior to their expiry on August 11, 2020. On April 1, 2016, an additional 99,844 lender warrants were issued and the exercise price of the total 1,263,844 additional lender warrants was reduced to \$0.009 per share.

HLS THERAPEUTICS INC.**Notes to the unaudited condensed interim consolidated financial statements****March 31, 2018**

(all amounts are in thousands of U.S. dollars, except per share information, and unless otherwise noted)

The additional lender warrants are exercisable as follows:

Number of additional lender warrants (#)	Share price target (\$)	Expiry date
315,961	12.50	August 11, 2020
315,961	15.00	August 11, 2020
315,961	17.50	August 11, 2020
315,961	20.00	August 11, 2020
1,263,844		

As a result of the amalgamation described in note 3, the ability of lenders to exercise the additional lender warrants is suspended while the Company is listed on an exchange that does not permit price-based vesting. The expiry date of the additional lender warrants is to be extended by one year, to August 11, 2021, if the Company is still listed on the Exchange on August 11, 2020.

Dividends

The holders of common shares are entitled to receive such dividends as the Board of Directors determines to declare on a share-for-share basis, as and when any such dividends are declared or paid.

Notwithstanding the above, under the terms of the senior secured term loan, the Company is prohibited from declaring or paying dividends, except for intercompany dividends.

No dividends were declared or paid in fiscal 2018 or 2017.

Loss per share

Basic loss per share is calculated by dividing net loss for the period by the weighted average number of common shares outstanding during the period.

Diluted loss per share is calculated by dividing the net loss for the period by the weighted average number of common shares outstanding during the period plus the weighted average number of common shares that would be issued on conversion of all dilutive potential securities into common shares.

The following is a reconciliation of the numerator and denominator used for the computation of the basic and diluted loss per share amounts:

	Three months ended	
	March 31, 2018	March 31, 2017
Net loss for the period	(4,876)	(3,032)
Weighted average number of common shares		
outstanding – basic	25,732,287	25,277,997
Effect of dilutive securities	—	—
Weighted average number of common shares		
outstanding – diluted	25,732,287	25,277,997

The calculation of diluted loss per share in fiscal 2018 excludes 4,893,293 (2017 – 5,876,671) weighted average number of common shares issuable upon the exercise of lender and broker warrants and options because the effect of their issuance would be anti-dilutive.

HLS THERAPEUTICS INC.**Notes to the unaudited condensed interim consolidated financial statements****March 31, 2018**

(all amounts are in thousands of U.S. dollars, except per share information, and unless otherwise noted)

10. CAPITAL MANAGEMENT

The Company's capital management objectives are to maintain financial flexibility to pursue its acquisitive strategy of creating a portfolio of commercial-stage pharmaceutical products consisting of established brands and promotional stage products in selected therapeutic areas. The Company defines capital as the aggregate of non-current financial liabilities and shareholders' equity.

Managed capital is set out in the following table:

	March 31, 2018	December 31, 2017
Non-current financial liabilities	156,768	158,114
Shareholders' equity	189,719	180,382
	<u>346,487</u>	<u>338,496</u>

The Company manages its capital structure in accordance with changes in economic conditions. In order to maintain or adjust its capital structure, the Company may elect to issue or repay long-term debt, issue shares, repurchase shares, pay dividends (where permitted) or undertake any other activity as deemed appropriate under specific circumstances.

The Company is not subject to any externally imposed capital requirements, other than a prohibition under the senior secured term loan from paying dividends, and there has been no change in the Company's capital management approach during the year.

11. INCOME TAXES

The significant components of the Company's income tax expense (recovery) are as follows:

	Three months ended	
	March 31, 2018	March 31, 2017
Current income tax	120	866
Deferred income tax expense (recovery) resulting from temporary differences	(889)	2
	<u>(769)</u>	<u>868</u>

The difference between the amount of the income tax expense (recovery) and the amount computed by multiplying loss before income taxes by the statutory Canadian, United States, and Barbados income tax rates is reconciled as follows:

	Three months ended	
	March 31, 2018	March 31, 2017
Loss before income taxes	(5,645)	(2,164)
Tax recovery at Canadian corporate tax rate of 26.7%	(1,507)	(578)
Expenses not deductible for tax purposes	182	804
Income subject to tax in foreign jurisdictions	556	642
	<u>(769)</u>	<u>868</u>

HLS THERAPEUTICS INC.**Notes to the unaudited condensed interim consolidated financial statements****March 31, 2018**

(all amounts are in thousands of U.S. dollars, except per share information, and unless otherwise noted)

12. SEGMENTED INFORMATION

The Company is composed of a single reportable segment.

Revenues are generated from the following sources:

	Three months ended	
	March 31, 2018	March 31, 2017
Product sales	11,631	10,624
Royalties	1,535	4,929
	13,166	15,553

Revenues are generated from the following geographic sources, by location of customer:

	Three months ended	
	March 31, 2018	March 31, 2017
Canada	6,759	6,335
United States	6,407	9,218
	13,166	15,553

13. FINANCE AND RELATED COSTS, NET

	Three months ended	
	March 31, 2018	March 31, 2017
Interest on senior secured term loan	4,075	4,155
Accreted interest	1,629	1,728
Total interest expense	5,704	5,883
Interest income	(79)	(23)
Foreign exchange loss (gain)	116	(79)
Realized loss (gain) on foreign currency forward contract	276	(86)
Fair value adjustment on financial assets and liabilities	(450)	10
	5,567	5,705

14. CONSOLIDATED STATEMENTS OF CASH FLOWS

The net change in non-cash working capital balances consists of the following:

	Three months ended	
	March 31, 2018	March 31, 2017
Accounts receivable	12,505	(5,258)
Inventories	240	373
Prepaid expenses and other current assets	34	(62)
Accounts payable and accrued liabilities	(1,367)	295
Provisions	(1,279)	934
Income taxes payable	(717)	339
	9,416	(3,379)

HLS THERAPEUTICS INC.**Notes to the unaudited condensed interim consolidated financial statements****March 31, 2018**

(all amounts are in thousands of U.S. dollars, except per share information, and unless otherwise noted)

Interest of \$4,075 (2017 – \$4,155) and income taxes of \$837 (2017 – \$527) were paid during the three months ended March 31, 2018.

15. RELATED PARTY DISCLOSURES

The following table sets out the compensation of the Company's key management personnel, defined as the four founders of the Company:

	Three months ended	
	March 31, 2018	March 31, 2017
Short-term employee benefits	558	607

16. SUBSEQUENT EVENTS**Partial redemption of preferred shares**

On April 26, 2018, the Company announced that it intends to redeem 9,321,492 (71.83%) of the Company's outstanding preferred shares on May 9, 2018 on a pro rata basis. The preferred shares will be redeemed at a price of C\$0.61149 per preferred share, for a total redemption payment of C\$5,700. The redemption payment will be made from the available escrow funds.

Normal course issuer bid

On May 9, 2018, the Company announced that the Exchange had approved the Company's Notice of Intention to Make a Normal Course Issuer Bid under which the Company may, if considered advisable, purchase for cancellation, from time to time over the next 12 months, up to an aggregate of 1,371,495 of its issued and outstanding common shares, being 5% of the issued and outstanding common shares as of May 7, 2018.