

Condensed Interim Unaudited Financial Statements of

KARNALYTE RESOURCES INC.

Three months ended March 31, 2018 and 2017

KARNALYTE RESOURCES INC.

Interim Statements of Financial Position (unaudited)

(CAD \$ thousands)

	March 31, 2018	December 31, 2017
ASSETS		
Current assets:		
Cash	\$ 11,342	\$ 12,265
Trade and other receivables	105	122
Prepaid expenses	563	370
	<u>12,010</u>	<u>12,757</u>
Restricted cash	375	375
Capital assets (note 3)	410	426
Exploration and evaluation and other assets (note 4)	5,044	5,044
ASSETS	\$ 17,839	\$ 18,602
LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities:		
Trade and other payables	\$ 608	\$ 691
	<u>608</u>	<u>691</u>
Decommissioning liability	182	155
Total liabilities	<u>790</u>	<u>846</u>
Shareholders' equity:		
Share capital (note 5)	129,879	129,879
Contributed surplus	9,255	9,217
Deficit	(122,085)	(121,340)
Total shareholders' equity	<u>17,049</u>	<u>17,756</u>
LIABILITIES AND SHAREHOLDERS' EQUITY	\$ 17,839	\$ 18,602

Commitments (note 7), Contingent liability (note 9)

See accompanying notes to the financial statements.

Approved on behalf of the Board:

"signed"
W. Todd Rowan, Director

"signed"
Peter Matson, Director

KARNALYTE RESOURCES INC.

Interim Statements of Comprehensive Loss (unaudited)

For the three months ended March 31, 2018 and 2017
(CAD \$ thousands)

	2018	2017
Expenses:		
General and administrative	\$ 616	\$ 786
Depreciation and amortization (note 3)	16	71
Share-based compensation expense (note 5 (c))	38	2
Restructuring expenses	10	360
Recovery of provision	-	(1,316)
Impairment expenses (note 4)	99	169
Other income and expenses	(27)	(19)
	752	53
Finance income	(7)	(46)
Net finance income	(7)	(46)
Comprehensive (loss)	\$ (745)	\$ (7)
Loss per share (note 5(b)) Basic and diluted	\$ (0.03)	\$ (0.00)

See accompanying notes to the financial statements.

KARNALYTE RESOURCES INC.

Interim Statements of Cash Flows (unaudited)

For the three months ended March 31, 2018 and 2017
(CAD \$ thousands)

	2018	2017
Cash Flows from (used in) Operating Activities:		
Net loss for the period	\$ (745)	\$ (7)
Add/deduct:		
Depreciation and amortization (note 3)	16	71
Stock-based compensation expense (note 5(c))	38	2
Impairment expense (note 4)	99	169
Recovery of provision	-	(1,316)
Net finance income	(7)	(46)
Interest income received	39	47
Unrealized foreign exchange gain/(loss)	-	25
Changes in non-cash working capital (note 6)	(264)	(437)
	(824)	(1,492)
Cash Flows from (used in) Investing Activities:		
Additions to intangible assets (note 4)	(99)	(169)
	(99)	(169)
Change in cash	(923)	(1,661)
Cash, beginning of period	12,265	16,752
Cash and cash equivalents, end of period	\$ 11,342	\$ 15,091

See accompanying notes to the financial statements.

KARNALYTE RESOURCES INC.

Interim Statements of Changes in Equity (unaudited)

For the three months ended March 31, 2018 and 2017
(CAD \$ thousands)

	2018		2017	
	Number	Amount	Number	Amount
Share Capital:				
Balance, beginning of period	28,116	\$ 129,879	28,116	\$ 129,879
Balance, end of period	28,116	129,879	28,116	129,879
Contributed Surplus:				
Balance, beginning of period		9,217		9,204
Stock-based compensation expense (note 5(c))		38		2
Balance, end of period		9,255		9,206
Deficit:				
Balance, beginning of period		(121,340)		(117,945)
Comprehensive loss for the period		(745)		(7)
Balance, end of period		(122,085)		(117,952)
Balance, end of period		\$ 17,049		\$ 21,133

See accompanying notes to the financial statements.

KARNALYTE RESOURCES INC.

Notes to Condensed Interim Financial Statements (unaudited)

For the years three months ended March 31, 2018 and 2017
(All tabular amounts are in CAD thousands except per share amounts)

1. Reporting entity

Karnalyte Resources Inc. (the “Company” or “Karnalyte”) is incorporated under the laws of the province of Alberta. As at the date of the financial statements, the business of Karnalyte consisted of the exploration and development of its property and planned construction of a production facility and development of a potash mine. The property is situated in Saskatchewan, south of Wynyard and contains a dominant zone of potash and magnesium minerals. The recoverability of amounts recorded as mineral properties and deferred exploration and development costs is dependent upon the discovery of economically recoverable reserves, the ability of the Company to obtain necessary financing to develop the property and upon future profitable production and the sale thereof.

As of the date of these financial statements, the Company was in its pre-development phase and therefore there is no certainty that the Company will be able to raise additional funds to obtain the necessary capital to move forward to the production stage. While the Company has sufficient cash to meet its short-term corporate operating and capital requirements for at least the next twelve months, it does not currently have adequate funds to proceed with full-scale development of the solution mining facility.

The Company’s operating segments have been identified as the individual mineral reserve streams. As at the date of these financial statements, the Company identified two operating segments, potash and magnesium; however as investment in the magnesium segment is negligible they are grouped as one reporting segment for financial reporting purposes.

The Company’s address is 3150B Faithfull Ave. Saskatoon, SK S7K 8H3.

2. Basis of preparation

(a) Statement of compliance

These condensed interim unaudited financial statements have been prepared by management in accordance with International Accounting Standard (“IAS”) 34, Interim Financial Reporting, as issued by the International Accounting Standards Board. In preparing these interim financial statements the Company applied the same accounting policies as disclosed in the year-end financial statements dated December 31, 2017 except as noted below. These statements do not include all information or disclosures normally provided in annual statements. These interim statements should be read in conjunction with the audit annual financial statements and related notes.

This is the first set of financial statements for the Company where IFRS 9, Financial Instruments (IFRS 9) and IFRS 15, Revenue from Contracts with Customers (IFRS 15) have been applied. Changes to significant accounting policies are described in note 2(b).

These financial statements were authorized for issue by the Board of Directors on May 9, 2018.

KARNALYTE RESOURCES INC.

Notes to Condensed Interim Financial Statements (unaudited)

For the three months ended March 31, 2018 and 2017

(All tabular amounts are in CAD thousands except per share amounts)

2. Basis of preparation (continued)

(b) Changes in accounting policy

On January 1, 2018, the Company adopted the new standards, IFRS 15 and IFRS 9, as issued by the IASB.

(i) IFRS 9 - Financial instruments

IFRS 9 includes revised guidance on the classification and measurement of financial assets. While the new standard largely retains the existing requirements for the classification and measurement of financial liabilities, it changes the previous categories for financial assets. Upon adoption, the Company reclassified its financial assets from the previous category “loans and receivable” to the new category “amortized cost”. There was no impact on the measurement of these instruments. (Note 8).

The new standard also includes a new expected credit loss model for calculating impairment on financial assets. This change did not have an impact on the financial statements.

(ii) IFRS 15 - Revenue

IFRS 15 clarifies the principles for recognizing revenue from contracts with customers. As the Company does not have any contracts with customers there was no impact on the financial statements as a result of the adoption of this standard.

(c) New standards and interpretations not yet adopted

(i) IFRS 16 – Leases

IFRS 16 “Leases” introduces a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term greater than 12 months, unless the underlying asset is of a low value. A lessee is required to recognize a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. IFRS 16 will replace IAS 17, Leases and is effective for annual periods beginning on or after January 1, 2019. Earlier application is permitted. The Company is currently evaluating the impact of adopting IFRS 16 on its financial statements.

(ii) IFRIC 23 – Uncertainty over Income Tax Treatments

IFRIC 23 provides guidance on the accounting for current and deferred tax liabilities and assets in circumstances in which there is uncertainty over income tax treatments. IFRIC 23 is effective for periods beginning on or after January 1, 2019 with early adoption permitted. The Company is currently evaluating the impact of adopting IFRIC 23 on its financial statements

KARNALYTE RESOURCES INC.

Notes to Condensed Interim Financial Statements (unaudited)

For the three months ended March 31, 2018 and 2017

(All tabular amounts are in CAD thousands except per share amounts)

3. Capital assets

	Land and Buildings	Vehicles	Processing and other Equipment	Assets Under Construction	Total
Cost:					
Balance at January 1, 2017	\$ 497	\$ 117	\$ 3,707	\$ 18,711	\$ 23,032
Additions	-	-	-	-	-
Dispositions	-	-	(50)	-	(50)
Balance at December 31, 2017	497	117	3,657	18,711	22,982
Additions	-	-	-	-	-
Balance at March 31, 2018	\$ 497	\$ 117	\$ 3,657	\$ 18,711	\$ 22,982
Accumulated depreciation:					
Balance at January 1, 2017	\$ 169	\$ 84	\$ 3,358	\$ 18,711	\$ 22,322
Depreciation	13	15	256	-	284
Dispositions	-	-	(50)	-	(50)
Impairment	-	-	-	-	-
Balance at December 31, 2017	182	99	3,564	18,711	22,556
Depreciation	3	4	9	-	16
Balance at March 31, 2018	\$ 185	\$ 103	\$ 3,573	\$ 18,711	\$ 22,572
Carrying amounts:					
December 31, 2017	\$ 315	\$ 18	\$ 93	\$ -	\$ 426
March 31, 2018	\$ 312	\$ 14	\$ 84	\$ -	\$ 410

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Notes to Condensed Interim Financial Statements (unaudited)

For the three months ended March 31, 2018 and 2017

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4. Exploration and evaluation assets and other assets

	Mineral Properties	Process Patents	Computer Software	Total
Cost:				
Balance at January 1, 2017	\$ 48,004	\$ 170	\$ 277	\$ 48,451
Additions	879	-	-	879
Sale of assets	(21)	-	-	(21)
Balance at December 31, 2017	48,862	170	277	49,309
Additions	99	-	-	99
Balance at March 31, 2018	\$ 48,961	\$ 170	\$ 277	\$ 49,408
Amortization and impairment losses:				
Balance at January 1, 2017	\$ 43,221	\$ 170	\$ 277	\$ 43,668
Impairment	597	-	-	597
Balance at December 31, 2017	43,818	170	277	44,265
Impairment	99	-	-	99
Balance at March 31, 2018	\$ 43,917	\$ 170	\$ 277	\$ 44,364
Carrying amounts:				
December 31, 2017	\$ 5,044	\$ -	\$ -	\$ 5,044
March 31, 2018	\$ 5,044	\$ -	\$ -	\$ 5,044

5. Share capital

(a) Authorized

As at March 31, 2018 and 2017 the Company was authorized to issue an unlimited number of common shares. The holders of common shares are entitled to receive dividends as declared by the Company and are entitled to one vote per share. Since its inception, the Company has not declared a dividend. No common shares were issued throughout the three months ended March 31, 2018.

The Company is also entitled to issue an unlimited number of preferred shares. There were no preferred shares issued throughout the three months ended March 31, 2018.

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5. Share capital (continued)

(b) Earnings per share

Basic earnings per share were calculated as follows:

	2018	2017
Loss for the year ending March 31,	\$ (745)	\$ (7)
Weighted average number of common shares (thousands) outstanding:		
Weighted average issued common shares at beginning of period	28,116	27,672
Weighted average common shares issued	-	158
Weighted average number of common shares outstanding	28,116	27,830
Basic loss per share	\$ (0.03)	\$ (0.00)

Basic loss per share is calculated using the weighted average number of shares outstanding during the year. Diluted per share amounts are equal to basic per share amounts due to the Company incurring a net loss for the period. Excluded from the diluted per share calculations were 800,000 (2017 - 1,943,000) options as their effect would have been anti-dilutive.

(c) Stock-based compensation expense

The Company has a stock option plan under which directors, officers and non-employees of the Company are eligible to receive stock options. The aggregate number of common shares to be issued upon the exercise of all stock options granted under the plan shall not exceed 10% of the issued common shares of the Company at the time of granting of the options. Options granted under the plan generally have a term of two to five years and vest at terms to be determined by the directors at the time of grant. The exercise price of each option shall be determined by the directors at the time of grant but shall not be less than the price permitted by the policies of the stock exchange on which the Company's common shares are then listed.

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5. Share capital (continued)

(c) Stock-based compensation expense (continued)

The number (thousands) and weighted average exercise prices of share options are as follows:

	2018		2017	
	Number of options	Weighted average exercise price	Number of options	Weighted average exercise price
Outstanding at January 1,	1,045	\$ 0.98	1,943	\$ 0.87
Issued during the period	-	-	-	-
Cancelled during the period	225	1.81	-	-
Expired during the period	-	-	-	-
Forfeited during the period	20	0.88	-	-
Outstanding at March 31,	800	0.75	1,943	0.87
Exercisable at March 31,	270	\$ 0.75	1,898	\$ 0.87

Number of Options Outstanding	Exercise Price	Remaining Life (yrs)	Exercisable Options	Exercisable Price
210	\$ 0.75	2.29	210	\$ 0.75
60	0.75	4.70	60	0.75
530	0.75	6.72	-	0.75
800	\$ 0.75	4.57	270	\$ 0.75

Share based compensation of \$38 (2017 - \$2) was expensed during the three month period ended March 31, 2018.

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6. Supplemental cash flow information

Changes in non-cash working capital are as follows:

March 31,	2018	2017
Accounts receivable	\$ 11	\$ 2
Prepaid expenses	(193)	(237)
Trade and other payables	(82)	(202)
	<u>\$ (264)</u>	<u>\$ (437)</u>
Relating to:		
Operating activities	\$ (264)	\$ (437)
	<u>\$ (264)</u>	<u>\$ (437)</u>

7. Commitments

	Contractual cash flows	Less than one year	Two - three years	Four - five years	More than five years
Trade and other payables	\$ 507	\$ 507	\$ -	\$ -	\$ -
Office lease	171	121	50	-	-
Permit/lease on mineral property	6,601	40	738	738	5,085
Project contracts	120	120	-	-	-
	<u>\$ 7,399</u>	<u>\$ 788</u>	<u>\$ 788</u>	<u>\$ 738</u>	<u>\$ 5,085</u>

8. Financial instruments and related risk management

Financial instruments included in the statements of financial position consist of cash, trade and other receivables, restricted cash, and trades and other payables. As required by IFRS 9, trade and other receivable has been reclassified as measured at amortized cost. Accordingly, all financial instruments included in the statements of financial position are classified as measured at amortized cost. The fair values of these financial instruments approximate their carrying amounts due to the short-term maturity of the instruments.

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9. Contingent liability

Following its annual general meeting on May 5th, 2017, the Company reviewed its strategy and restructured its operations. The restructuring resulted in the terminations and resignations of certain officers and employees.

In the fourth quarter of 2017, the Company received a statement of claim filed at the Court of Queen's Bench of Alberta by Mr. Siu Ma, the Company's former Executive Vice-president and Chief Operating Officer, in the amount of \$728,750. Mr. Ma's claim is for an alleged breach of contract for the Company's failure to provide payments to Mr. Ma after he terminated the employment agreement alleging a change of control had occurred. The Company has denied Mr. Ma's allegations and filed a statement of defense and has recorded an estimate of all amounts payable to Mr. Ma under his contract. Actual amounts payable may vary from amounts estimated.