

BQE Water

BQE WATER INC.

Interim Management's Discussion and Analysis (Quarterly Highlights)

For the three and six months ended June 30, 2020 and 2019

INTERIM MANAGEMENT'S DISCUSSION AND ANALYSIS

Quarterly Highlights – for the three and six months ended June 30, 2020 and 2019

The following Management's Discussion and Analysis ("MD&A") provides information that management believes is relevant to an assessment and understanding of our consolidated results of operations and financial condition. Management of the Company have prepared this document in conjunction with their broader responsibilities for reasonable assurance regarding the reliability of the financial reporting and the establishment and maintenance of adequate information systems and internal controls to ensure that the financial information is complete and reliable. Management also believes that any internal controls and procedures for financial reporting, no matter how well conceived and operated, can provide only reasonable, not absolute, assurance that the objectives of the control systems are met. The Audit Committee of the Board of Directors, consisting of independent directors, has reviewed this document and all other publicly reported financial information, for integrity, usefulness, reliability and consistency.

This Q2 2020 Interim MD&A updates disclosure previously provided in our Annual MD&A, up to the date of this Interim MD&A, and should be read in conjunction with our unaudited condensed consolidated interim financial statements for the three and six months ended June 30, 2020 and 2019 (our "Interim Financial Statements"), our audited consolidated financial statements for the years ended December 31, 2019 and 2018 (our "Audited Financial Statements") and our Annual MD&A for the year ended December 31, 2019.

Our Interim Financial Statements have been prepared in accordance with International Accounting Standard ("IAS") 34, *Interim Financial Reporting*, as issued by the International Accounting Standards Board ("IASB") and interpretations of the IFRS Interpretations Committee ("IFRIC"), effective as of June 30, 2020. Our accounting policies are described in note 3 of our Audited Financial Statements. All financial information is presented in **Canadian dollars** unless otherwise noted. This MD&A has been prepared as at August 27, 2020.

Certain statements contained in the MD&A constitute forward-looking statements. Such forward-looking statements involve a number of known and unknown risks, uncertainties and other factors which may cause the actual results, performance or achievements of the Company to be materially different from any future results, performance or achievements expressed or implied by such forward-looking statements. Readers are cautioned not to place undue reliance on these forward-looking statements, which speak only as of the date the statements were made and readers are advised to consider such forward-looking statements in light of the risks.

OUR BUSINESS

BQE Water Inc. ("BQE Water" or the "Company") is helping to make the mining and metallurgical industry more environmentally sustainable and profitable by implementing innovative water management and treatment solutions that support and improve operations in this sector. Central to our business model is that BQE Water produces clean water and stable residues (or saleable by-products) and that we monetize the value of our unique process know-how through recurring revenues generated from plant operations services.

BQE Water is headquartered in Vancouver, British Columbia, Canada. The Company has regional offices in Chile and China, which are two key geographical markets in our business. BQE Water is listed on the TSX Venture Exchange under the symbol BQE. Additional information may be found on our website at www.bqewater.com and on SEDAR at www.sedar.com.

NON-GAAP MEASURES

We use non-GAAP financial measures to supplement our consolidated financial statements presented in accordance with generally accepted accounting principles, or GAAP, to enhance investors' and observers' overall understanding of the Company's current financial performance. Non-GAAP financial measures have limitations in that they do not reflect all amounts associated with our operational results as determined in accordance with GAAP. In addition, non-GAAP financial measures do not have any standardized meaning prescribed by GAAP and are likely to be comparable to similar non-GAAP

financial measures presented by other companies. Non-GAAP financial measures should only be used to evaluate our operational results in conjunction with the corresponding GAAP measures.

Proportional Results

To provide additional insight into our financial results, certain statements in this MD&A disclose the effective portion of results that we would have reported if our joint venture operations had been proportionately integrated into our results and are referred to as BQE Water’s proportional share (“Proportional”). All Proportional financial measures disclosed in this MD&A are non-GAAP measures.

Proportional Revenue

This non-GAAP financial measure of Proportional Revenue adds BQE Water’s share of joint venture revenues to the Company’s revenues reported under GAAP. Proportional Revenues for the three and six months ended June 30, 2020 and 2019 are as follows:

<i>(in \$’000s)</i>	3 months ended Jun. 30		6 months ended Jun. 30	
	2020	2019	2020	2019
	\$	\$	\$	\$
Reported revenues under GAAP	1,414	1,216	3,350	1,932
Share of reported revenues from joint ventures	1,357	1,922	1,777	3,262
Proportional Revenues for the period	2,771	3,138	5,127	5,194

Adjusted EBITDA

Adjusted EBITDA (“earnings before interest, taxes, depreciation and amortization”) is intended to provide additional information only and does not have any standardized meaning under IFRS and may not be comparable to similar measures presented by other companies. It should not be considered in isolation or as a substitute for measures of performance prepared in accordance with IFRS. Consequently, the presentation of Adjusted EBITDA enables shareholders to better understand the underlying financial performance of our business through the eyes of management. Adjusted EBITDA includes adjustments of the Company’s Proportional share of joint venture results. The following table reconciles this non-GAAP measure to the most directly comparable IFRS measure of net income (loss):

<i>(in \$’000s)</i>	3 months ended Jun. 30		6 months ended Jun. 30	
	2020	2019	2020	2019
	\$	\$	\$	\$
GAAP: Net (loss) income	(55)	345	(71)	18
Add/Deduct: interest (income) expense	(2)	10	(6)	11
Add: income taxes	61	140	49	156
Add: depreciation and amortization	199	190	390	381
EBITDA	203	685	362	566
Add: share-based payment expense	118	64	167	86
Add/Deduct: net foreign exchange loss (gain)	91	7	(26)	25
Adjusted EBITDA	412	756	503	677

COMMENTARY AND OUTLOOK

Although our year-to-date financial results are lower than those recorded in the prior year, they reflect necessary upfront investments in the Company's next growth phase and provide an indication of our stronger financial position. This new growth phase is being driven by the ramp-up of six water treatment plants that will require ongoing operational services, as well as a growing number of new projects requiring the addition of new staff. As a result, in the first six months of 2020, our gross margin was 37%, which was a decrease from 46% in the same period of 2019. The underlying increase in operating expenses is attributed to the following:

- Hiring and training of the Kemess plant operations team prior to the recognition of new recurring revenue;
- Hiring and training of new staff in China to commission and provide ongoing operations support for the new SART plants prior the recognition of recurring revenue; and
- Hiring of new engineers and project-specific staff to support the current and anticipated increase in project activity.

Our net income for the first half of the year decreased by \$89,000 when compared to net income of \$18,000 recorded in the same period in 2019. This decrease was modest when considered against the following factors:

- A prolonged six-month draught at Dexing Mine, which reduced our share of income from the JCC joint venture by approximately \$450,000;
- A delayed start to the water treatment season at Raglan Mine, resulting in a decrease of approximately \$100,000 in net income; and
- The granting of new stock options in accordance with the approved stock option plan, leading to an additional non-cash expense of \$80,000 in share-based payment expenses.

While the decrease in our overall profitability in the first half of the year may be notable in the short-term, the long-term impact ranges from neutral to positive:

- The lack of rain at Dexing Mine over the first half of 2020 does not change the total tonnage of copper that is present at site and available for recovery. Copper is recovered from waste rock and the rain acts as the transport medium that brings the copper to the treatment plants. Since Q3 2020, precipitation levels have increased and exceeded last year's rainfall. We currently expect copper production at our JCC joint venture to catch up in the second half of 2020.
- The later start to the treatment season at Raglan Mine does not cancel the revenue flow, but simply delays the recognition of the revenues to the remaining months in 2020.
- Expenses from expanding our Canadian and Chinese operations teams and share-based payments represent an investment that is a precursor to generating new long-term recurring revenues with a capable team vested in the Company's success.

In light of all of the foregoing, our year-to-date financial results demonstrate that we are now able to finance the Company's growth without depleting our working capital or relying on proceeds from external financing. At the end of Q2 2020, we had working capital of \$2.2 million (up \$341,000 from December 31, 2019) and cash of \$1.9 million (down \$154,000 from December 31, 2019). Proportional Cash, which includes our share held in joint ventures, as of June 30, 2020 was \$3.4 million compared to \$4.2 million at December 31, 2019. Overall, we are pleased to report that BQE Water is in a more mature and stable financial position.

Looking ahead, we are optimistic about the second half of 2020. Whether or not our annual financial results improve over 2019 will depend on the timing of completing the commissioning of the Selen-IX™ plant at Kemess and the two SART plants in China, as these milestones will mark the start of new recurring revenues. We also remain positive about our long-term outlook. At present, we have a backlog of technical services contracts that stretches into 2021 and our pipeline of potential new future projects has not seen any deterioration. However, we must continue to caution that uncertainties about the future of the global economy and commodity prices due to COVID-19, and its impact on the resource industry, as well as geopolitical issues, represent ongoing risks that may negatively impact our business and longer term performance, particularly in China.

FINANCIAL HIGHLIGHTS

- Adjusted EBITDA of \$412,000 in Q2 2020 compared to \$756,000 in Q2 2019;
- Proportional Revenues of \$2.8 million in Q2 2020 compared to \$3.1 million in Q2 2019;
- Technical services revenues increased over 35% year-over-year, from \$942,000 in Q2 2019 to \$1.3 million in Q2 2020, indicating the potential for future operations revenues and continued growth over and above the six treatment plants currently in development;
- Net loss of \$55,000 in Q2 2020 compared to a net income of \$345,000 in Q2 2019;
- Working capital increased by 19% over the six-month period, from \$1.8 million at the end of 2019 to \$2.2 million at the end of Q2 2020; and
- Proportional Cash, which includes our share held in joint ventures, as of June 30, 2020 was \$3.4 million compared to \$2.9 million at March 31, 2020.

OPERATIONAL SERVICES HIGHLIGHTS

Our operational services consist of the operation of water treatment plants, which generate recurring revenues for the Company from two main sources: sales of recovered metals and water treatment fees.

Revenues from Sales of Recovered Metals

The Company operates four water treatment plants that generate revenues from the sale of recovered metals, three plants from the JCC-BQE Joint Venture (“JCC-BQE”) and one plant from the MWT-BQE Joint Venture (“MWT-BQE”).

JCC-BQE Joint Venture

Our 50/50 joint venture with partner Jiangxi Copper Company (“JCC”) operates water treatment plants at Dexing Mine and at Yinshan Mine in Jiangxi province of China. The volume of water treated and pounds of copper recovered by the plants fluctuate seasonally depending on precipitation levels in the region. The operating results are as follows:

<i>(in '000s)</i>	3 months ended Jun. 30		6 months ended Jun. 30	
	2020	2019	2020	2019
Water treated (cubic metres)	5,561	7,347	8,270	13,086
Copper produced (pounds)	909	1,189	1,166	1,971

During Q2 2020, all three plants met or exceeded mechanical availability and process performance. However, both the volume of water treated and the mass of copper recovered decreased by 24% over the same period in 2019. The Dexing Mine continued to experience an unusually low volume of precipitation until the middle of Q2 2020, with only approximately half of the total rainfall compared to the same period of the prior year. Lower rainfall not only limited the volume of water flowing into the treatment plants, but also affected copper leaching from waste rock, which lowers the copper concentration in the plant feed. Changes in water volume and feed grade are largely the result of environmental conditions beyond the control of the joint venture and will fluctuate from period to period.

MWT-BQE Joint Venture

Our 20% share of MWT-BQE is with our 80% partner Beijing MWT Water Treatment Project Limited Company (“MWT”) and together we operate a water treatment plant at a smelter in Shandong province. MWT-BQE generates the majority of its revenues from the sale of zinc recovered from smelter wastewater, along with small traces of copper found in the stream. The operating results are as follows:

<i>(in '000s)</i>	3 months ended Jun. 30		6 months ended Jun. 30	
	2020	2019	2020	2019
Zinc recovered (pounds)	536	240	719	764
Copper recovered (pounds)	72	51	100	104

During the second quarter, the smelter adjusted their production lines with a higher-grade ore, which led to a higher concentration of copper and zinc in the feed composition and also an increase in the volume of water into the plant. The joint venture has no control in the volume and feed composition that flows into the plant. The changes made by the smelter are believed to be temporary and are expected to allow for the resumption of regular production in the latter part of 2020.

Revenues from Water Treatment Fees

The Company is contracted to operate and provide technical support for water treatment plants that generate recurring revenues in the form of water treatment and operations support fees. They include four plants operated by BQE Water for Glencore at Raglan Mine and one plant operated by the MWT-BQE joint venture but supported and supervised by BQE Water in China. Operating fees from the Glencore operations are primarily based on the volume of water treated and discharged in accordance with strict regulatory requirements. The MWT-BQE plant generates fixed operations support fees for the achievement of operational targets that rely on the Company’s technical expertise.

During Q2 2020, we mobilized our operations team to site to commence our 17th operating season at Raglan Mine. The team began operations at the Katinniq plant in April 2020 and at the ChemSulphide® plant in May 2020. Although we operated the ChemSulphide® plant during Q2, water was not discharged from the plant until late July due to the replacement of a discharge pump.

The MWT-BQE plant in Shandong generates an operation support fee paid to the Company by MWT-BQE. This fee is not linked to the volume of water treated but to the achievement of operational targets which rely on the Company’s expertise delivered through ongoing operations services.

The volume of water treated and discharged are as follows:

<i>(in '000s)</i>	3 months ended Jun. 30		6 months ended Jun. 30	
	2020	2019	2020	2019
4 Treatment plants at Raglan Mine (cubic metres)	94	341	94	341
Treatment plant at MWT-BQE (cubic metres)	179	131	332	282

TECHNICAL SERVICES HIGHLIGHTS

BQE Water’s technical expertise and IP are applicable globally across broad areas of water management. The highlights of technical services provided to clients and technical innovation projects during Q2 2020 are summarized below.

Commercial Deployment of Selen-IX™ and Direct Selenium Electro-Reduction (“ERC”) Technology

- Hired and initiated training of the operations team for the Selen-IX™ plant at Kemess Mine in Northern BC.
- Initiated commissioning of the Selen-IX™ plant at Kemess Mine in Northern BC.
- Initiated engineering design of the first commercial scale Direct Selenium ERC plant at a mine in North America.

Cyanide Management/Recovery for Precious Metals Extraction Projects using SART

- Preparations for commissioning of the SART plant for Shandong Zhongkuang Group in China.
- Hired and initiated training of SART operations team in China.
- Continued engineering design for the SART plant being constructed for Zhaojin Mining Industry in China.

Water Consulting Services – Management, Treatability, Permitting Assistance, Toxicity Mitigation

- Engineering design for improvements to an existing water treatment plant at El Mirador, a copper mine in Ecuador.
- Technical assessment of water treatment requirements to introduce a flotation circuit upstream of an existing cyanide leaching process for an existing gold mine in North America.
- Treatability assessment for selenium removal from tailings reclaim water at a project in the US.

- Treatability assessment for the simultaneous removal of sulphate and selenium from mine impacted water in the US.
- Pilot demonstration of selenium removal to support the permitting of a new mine in North America.
- Preliminary technical assessment for selective thiocyanate removal combined with cyanide recovery from carbon-in-pulp tailings at a project site in North America.

SELECTED FINANCIAL INFORMATION

(in \$'000 except for per share amounts)

	3 months ended Jun. 30		6 months ended Jun. 30	
	2020	2019	2020	2019
	\$	\$	\$	\$
Revenues	1,414	1,216	3,350	1,932
Operating expenses	921	607	2,116	1,051
	493	609	1,234	881
General and administration expenses	435	362	867	745
Sales and development expenses	239	274	468	593
Share-based payment expenses	118	64	167	86
Depreciation	36	50	72	100
Share of earnings from joint ventures	(380)	(507)	(253)	(709)
Income (loss) from operations and joint ventures	45	366	(87)	66
Other expenses, net	(100)	(21)	16	(48)
Net (loss) income for the period	(55)	345	(71)	18
Other comprehensive (loss) income				
Translation (loss) gain on foreign operations	(191)	(241)	195	(214)
Comprehensive (loss) income for the period	(246)	104	124	(196)
Net (loss) earnings per share (basic and diluted)	(0.04)	0.29	(0.06)	0.01
Proportional Revenues ¹	2,771	3,138	5,127	5,194
Adjusted EBITDA ¹	412	756	503	677

	at Jun. 30,	at Dec. 31,
	2020	2019
Working capital	2,170	1,829
Total assets	9,049	8,376
Total long term liabilities	736	331
Shareholders' equity	6,679	6,405

Notes:

1. See Non-GAAP measures

COMPARISON OF QUARTERS

Financial data for the last eight quarters:

(in \$'000s)

Quarters ended	Jun-20	Mar-20	Dec-19	Sept-19	Jun-19	Mar-19	Dec-18	Sept-18
	\$	\$	\$	\$	\$	\$	\$	\$
Revenues	1,414	1,936	1,382	2,326	1,216	716	1,310	1,893
Operating expenses	921	1,195	882	857	607	444	557	573
	493	741	500	1,469	609	272	753	1,320
General and administration	435	433	480	405	362	383	427	369
Sales and development	239	229	230	241	274	319	257	211
Share-based payment expenses	118	49	13	55	64	22	10	37
Depreciation	36	36	(23)	54	50	50	7	4
Share of (earnings) loss from joint ventures	(380)	127	263	(402)	(507)	(202)	198	(302)
Income (loss) from operations and joint ventures	45	(133)	(463)	1,116	366	(300)	(146)	1,001
Other (expenses) income, net	(95)	115	21	37	(17)	(27)	15	(57)
Bad debt expense	-	-	(95)	(287)	(1)	-	-	-
Income tax expense	(5)	-	(91)	(17)	(3)	-	(125)	-
Net (loss) income	(55)	(18)	(628)	849	345	(327)	(256)	944
Translation (loss) gain	(191)	387	70	(140)	(241)	27	257	(318)
Comprehensive (loss) income	(246)	369	(558)	709	104	(300)	(1)	626
Non-GAAP Measures:								
Proportional Revenue	2,771	2,356	2,005	3,991	3,138	2,057	2,198	3,488
Adjusted EBITDA	412	91	(451)	1,495	756	(80)	(100)	1,272

Quarterly results can fluctuate based on the number of plants operating in the quarter, variation in the volume and grade of water treated, and movements in commodity prices. Seasonality at each operation also impacts the timing of revenues. Operations at Raglan Mine typically run from May to October of each year. Copper production at the Dexing operations increase between April and September of each year and decline during the winter months due to lower seasonal precipitation and the annual maintenance schedule. Revenues from contracts for technical services relating to water management and technical innovation projects occur based on the timing of client requirements.

SUMMARY OF Q2 2020 FINANCIAL RESULTS

The following is a summary of selected financial results for the three-month periods ended June 30, 2020 and 2019.

Proportional Revenue

The change in Proportional Revenue from each revenue source is shown in the table below:

<i>(in \$'000s)</i>	Q2 2020		Q2 2019		
Revenue source	\$	% of total	\$	% of total	% Change
Sale of recovered metals from operations	1,357	49%	1,922	61%	(29%)
Water treatment fee from operations	144	5%	274	9%	(47%)
Technical services	1,270	46%	942	30%	35%
Total Proportional Revenue	2,771	100%	3,138	100%	(12%)

Revenues from the sale of base metals of value recovered comprises the Company's share of revenues from its joint ventures in China. The sale of copper and zinc recovered during the operation of water treatment plants is impacted by the amount and market price of metal concentrate sold. During Q2 2020, the Company's share of revenue from the JCC-BQE joint venture decreased from the comparable period in 2019 due to a 24% decrease in the quantity of copper recovered and an 8% decrease in average copper prices. The Company's share of revenue from the MWT-BQE joint venture was \$46,000 compared to \$50,000 at Q2 2020.

Water treatment fee revenues include the tolling fees earned from each cubic metre of water discharged at Raglan Mine and operations support fees from the new MWT-BQE plant in Shandong, China. The \$130,000 decrease in water treatment fee revenues was mainly due to the late start of the ChemSulphide® plant at Raglan Mine when water was not being discharged due to the late shipment of a discharge pump requiring replacement. The Company continues to provide ongoing operation support at the MWT-BQE water treatment plant and earned \$48,000 in revenues from operations support fees.

Revenues from technical services incurred the largest increase of \$328,000 in Q2 2020 when compared to Q2 2019. These revenues are non-recurring in nature and relate to water management services such as treatability assessments, permitting assistance, engineering and plant design, construction and commissioning of water treatment plants, laboratory testing and pilot demonstrations. It represents the sum of multiple contracts from various clients of varying contract values. In Q2 2020, there was an increase in project activity across the full spectrum of Company services, most notably in the areas of engineering and plant design for three US-based water treatment plants utilizing the Company's Selen-IX™ technology.

Operating Expenses

Total operating expenses during Q2 2020 were \$921,000 compared to \$607,000 in Q2 2019, an increase of \$314,000. The increase in operating expenses is mainly attributable to the additional staff hired for training during the commissioning of the water treatment plant at Kemess. The rest of the variance is due to the 35% increase in project activity related to technical services completed in the quarter. Each individual project requires varying levels of technical expertise and resources depending on the specific mine conditions and treatment requirements.

Expenses

In Q2 2020, general and administration costs were \$435,000 compared to \$362,000 in Q2 2019. The increase of \$73,000 in general and administration costs was mainly due to increases in payroll expenses, insurance premiums, and fees for professional services during Q2 2020.

Sales and development costs during Q2 2020 were \$239,000 compared to \$274,000 in Q2 2019, a decrease of \$35,000. The variance was due to internal labour resources being re-allocated from technology development to fulfill technical services contracts during the period.

Depreciation expenses were \$36,000 in Q2 2020 compared to \$50,000 in Q2 2019. With the adoption of IFRS 16 on January 1, 2019, the Company's depreciation expense includes the amortization of right-of-use assets.

Share-based payment expenses were \$118,000 in Q2 2020 compared to \$64,000 in Q2 2019. Share-based payment expenses consist of non-cash compensation expenses relating to stock options and grants of deferred and restricted share units. In January 2020, the Company granted 51,000 stock options, which accounted for \$57,000 of additional share-based payment expenses during the quarter. Other share-based payment expenses were due to fair value adjustments of deferred and restricted share units resulting from the movement of the Company's share price.

Other Income and Expenses

Net finance costs were \$4,000 in Q2 2020 compared to \$10,000 in Q2 2019. As the Company currently does not hold any interest-bearing debt, finance costs arise from the interest accretion of the Company's long-term liabilities, such as the lease obligations.

Foreign exchange loss was \$91,000 in Q2 2020 compared to \$7,000 in Q2 2019. These exchange gains and losses arise mainly from changes in the value of the US dollar, Mexican peso, Chilean peso and Chinese renminbi relative to the Canadian dollar, the Company's reporting currency.

Net Income and Comprehensive Income

Overall net loss for the three months ending in June 30, 2020 was \$55,000 compared to net income of \$345,000 in the same period in 2019. As the Company operates through subsidiaries and joint ventures with functional currencies that differ from the Company's reporting currency, exchange differences on the translation of the net assets of such entities are recognized through other comprehensive income or loss. Net of translation of such foreign entities, total comprehensive loss for the second quarter was a \$246,000 compared to a comprehensive income of \$104,000 in Q2 2019.

SUMMARY OF YEAR-TO-DATE Q2 2020 FINANCIAL RESULTS

The following is a summary of selected financial results for the six-month periods ended June 30, 2020 and 2019.

Proportional Revenues

The change in Proportional Revenues from each revenue source is shown in the table below:

<i>(unaudited, in \$'000s)</i> Revenue source	Year-to-date 2020		Year-to-date 2019		% Change
	\$	% of total	\$	% of total	
Sale of recovered metals from operations	1,777	35%	3,262	63%	(46%)
Water treatment fee from operations	190	4%	320	6%	(41%)
Technical services	3,160	61%	1,612	31%	96%
Total Proportional Revenues	5,127	100%	5,194	100%	(1%)

Total year-to-date revenues from the sale of recovered metals decreased by \$1.5 million over the same period in 2019. The Company's share of revenues from the JCC-BQE joint venture decreased by 46% due to a 41% decrease in copper recovered and a 9% drop in average copper prices during the period. Changes in water volume are largely the result of environmental conditions beyond the control of the joint venture and will fluctuate from period to period. The share of revenue from the water treatment plant at the MWT-BQE joint venture was \$101,000 during the first six months in 2020 when compared to \$158,000 in 2019, with the decrease due to lower zinc prices during the period.

Year-to-date water treatment fee revenues decreased by \$130,000 when compared to 2019, mainly attributable to our operations at Raglan Mine. Unlike the previous year, the Raglan operation began discharging water in late July 2020 due to the delay in receiving a replacement discharge pump, resulting in a decrease in water treatment fees. For our support at the MWT-BQE treatment plant, the Company continued to earn fixed fees of \$94,000 during the first six months of 2020.

Revenues from technical services during the first half of the year increased by \$1.5 million from the same period in 2019. The 96% increase over 2019 was attributable to higher project activity in all areas of technical services, but specifically the engineering and design of several Selen-IX™ treatment plants in the US.

Operating Expenses (excluding depreciation)

Year-to-date operating expenses (excluding depreciation) in 2020 increased by \$1.1 million compared to the same period in 2019. This significant increase is mainly due to the hiring and training of the operations team at the Kemess plant and at the new SART plants in China, both of which are prior to the recognition of new recurring revenue.

Expenses

The year-to-date general and administration expenses increased by \$122,000 compared to the same period in 2019. This increase was due to increases in salary expenses and in fees paid for professional services.

The year-to-date sales and development expenses decreased by \$125,000 compared to 2019. The decrease was due to the increase in reallocating labour resources to complete technical services contracts during 2020.

LIQUIDITY AND CAPITAL RESOURCES

At June 30, 2020, BQE Water had 1,215,435 common shares issued and outstanding (1,210,434 at December 31, 2019), and 84,833 stock options outstanding (39,501 at December 31, 2019). As of August 27, 2020, the Company has 1,217,435 common shares issued and outstanding; and 82,833 stock options outstanding.

On January 8, 2020, the Company granted 51,000 stock options with an exercise price of \$8.75 to the directors and employees of the Company. These options have a term of five years from the grant date and vest over three years with one-third vesting each year on the anniversary of the grant date. The fair value of these options, as determined using the Black-Scholes valuation model, was \$7.36 per option. The significant assumptions in the valuation model were: volatility of 124.2%, an expected option life of five years, and an annual risk-free interest rate of 1.62%.

At June 30, 2020, the Company had Cash of \$1.9 million, a decrease of \$154,000 from December 31, 2019. For the six months ended June 30, 2020, the Company's Cash used in operating activities was \$302,000 compared to \$1.1 million for the same period in 2019.

The Company had a working capital position at the end of the quarter of \$2.2 million, an increase of \$341,000 from December 31, 2019. At June 30, 2020, BQE Water's significant working capital items, aside from Cash, include trade and other receivables of \$1.8 million (\$1.2 million at December 31, 2019) and trade payable and accrued liabilities of \$1.2 million (\$1.4 million at December 31, 2019).

The Company has commitments of \$266,000 until 2023 under operating leases for office and laboratory premises and for office equipment.

The Company believes that it has sufficient working capital resources to finance its current operations beyond the next 12 months, albeit with the continuing potential for a temporary working capital shortfall based on short-term fluctuations in the Company's non-recurring revenues combined with the timing of the annual dividend payment from China.

RELATED PARTY TRANSACTIONS

For the three and six months ended June 30, 2020 and 2019, the compensation awarded to the Company's key management, which includes the Board of Directors and executive management, is as follows:

	3 months ended Jun. 30		6 months ended Jun. 30	
	2020	2019	2020	2019
	\$	\$	\$	\$
Salaries, fees and short-term benefits	170,623	166,514	338,249	322,124
Share-based payments	43,995	6,275	79,663	38,004
	<u>214,618</u>	<u>172,789</u>	<u>417,912</u>	<u>360,128</u>

Included in the trade payables and accrued liabilities as of June 30, 2020 is \$93,352 (\$100,768 at December 31, 2019) of salaries, management consulting service fees with companies owned by the Company's management, director fees and termination benefits. For the three and six months ended June 30, 2020, the consulting services received from companies owned by the Company's management amounted to \$33,750 and \$67,500 (\$30,000 and \$60,000 in 2019).

CRITICAL ACCOUNTING ESTIMATES AND JUDGMENTS

The preparation of the Company's condensed consolidated interim financial statements in conformity with IFRS requires the Company's management to make judgments, estimates and assumptions about future events that affect the amounts reported in the condensed consolidated interim financial statements and related notes to the financial statements. The estimates and associated assumptions are based on historical experience and other factors considered to be relevant. Actual results may differ from these estimates.

Estimates and assumptions are continually evaluated and are based on management's experience and other facts and circumstances. Revisions to estimates and the resulting effects on the carrying amounts of the Company's assets and liabilities are accounted for prospectively. The judgments, estimates and assumptions applied in these condensed consolidated interim financial statements, including key sources of estimation uncertainty were the same as those applied in the Company's last annual audited consolidated financial statements for the year ended December 31, 2019, with the exception of:

COVID-19 Economic Uncertainty

The Company has assessed the economic impacts of the COVID-19 pandemic on its condensed consolidated interim financial statements. As at June 30, 2020, management has determined that the Company's ability to execute its medium- and longer-term plans, the economic viability of its assets and the carrying value of its long-lived assets are not materially impacted. In making this judgment, management has assessed various criteria including, but not limited to, existing laws, regulations, orders, potential hindrances to our supply chain, disruptions in the markets for our services, commodity prices and foreign exchange prices along with the actions the Company has taken at its operations to protect the health and safety of its workforce and local communities. At this time, the full extent of the impact that the COVID-19 outbreak may have on the Company is unknown and will depend on future developments that are highly uncertain and that cannot be predicted with confidence.