



FALCO RESOURCES LTD.

**CONDENSED INTERIM FINANCIAL STATEMENTS
(UNAUDITED)**

**FOR THE THREE-MONTH PERIODS ENDED
SEPTEMBER 30, 2018 and 2017**

Falco Resources Ltd.

Balance Sheets

(Unaudited)

(Expressed in Canadian Dollars)

	As at September 30, 2018	As at June 30, 2018
	\$	\$
Assets		
Current assets		
Cash	3,356,896	8,932,271
Accounts receivable	5,355,542	4,590,387
Prepaid expenses and other assets	496,896	415,654
	<u>9,209,334</u>	<u>13,938,312</u>
Non-current assets		
Restricted cash	905,000	905,000
Property, plant and equipment (Note 4)	105,985,814	100,691,463
Exploration and evaluation assets (Note 5)	24,863,958	22,308,274
Other non-current assets (Note 7)	500,000	-
	<u>132,254,772</u>	<u>123,904,737</u>
Total assets	<u>141,464,106</u>	<u>137,843,049</u>
Liabilities		
Current liabilities		
Accounts payable and accrued liabilities (Note 6)	20,459,850	25,764,267
Contingently payable liability (Note 7)	10,000,000	10,000,000
Secured loan (Note 9)	9,955,400	-
Deferred premium on flow-through shares (Note 10)	-	489,851
	<u>40,415,250</u>	<u>36,254,118</u>
Non-current liabilities		
Deferred income taxes	9,758,000	9,319,000
	<u>9,758,000</u>	<u>9,319,000</u>
Total liabilities	<u>50,173,250</u>	<u>45,573,118</u>
Equity		
Share capital	103,252,339	103,235,749
Convertible debenture (Note 8)	6,875,000	6,875,000
Warrants (Note 11)	3,226,957	4,800,822
Contributed surplus	10,408,513	8,422,780
Deficit	(32,471,953)	(31,064,420)
Total equity	<u>91,290,856</u>	<u>92,269,931</u>
Total liabilities and equity	<u>141,464,106</u>	<u>137,843,049</u>
Going concern (Note 1)		

Equity is solely attributable to Falco Resources Ltd. shareholders

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

Falco Resources Ltd.

Statements of Loss and Comprehensive Loss

For the three-month periods ended September 30, 2018 and 2017

(Unaudited)

(Expressed in Canadian Dollars)

	2018	2017
	\$	\$
Expenses		
Consulting and compensation	842,866	809,994
Share-based compensation (Note 12)	365,978	238,027
Office and administrative	83,112	114,109
Professional fees	82,827	154,455
Investor and shareholder relations	34,835	53,016
Travel	17,675	60,898
Depreciation	3,190	3,190
Operating loss	(1,430,483)	(1,433,689)
Interest income	25,773	153,455
Interest expense	(53,690)	(189,603)
Foreign exchange gain (loss)	16	(645)
Other income – premium on flow through shares (Note 10)	489,851	1,047,841
Loss before income taxes	(968,533)	(422,641)
Deferred income tax expense	(439,000)	(857,549)
Net loss and comprehensive loss	(1,407,533)	(1,280,190)
Net loss per common share (Note 13)		
Basic and diluted	(0.01)	(0.01)
Weighted average number of common shares outstanding (Note 13)		
Basic and diluted	189,187,691	179,743,170

The net loss and the comprehensive loss are solely attributable to Falco Resources Ltd. shareholders.

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

Falco Resources Ltd.

Statements of Cash Flows

For the three-month periods ended September 30, 2018 and 2017

(Unaudited)

(Expressed in Canadian Dollars)

	<u>2018</u>	<u>2017</u>
	\$	\$
Operating activities		
Net loss	(1,407,533)	(1,280,190)
Adjustments for:		
Share-based compensation (Note 12)	365,978	238,027
Depreciation (Note 4)	3,190	3,190
Other income – premium on flow-through shares (Note 10)	(489,851)	(1,047,841)
Deferred income tax expense	439,000	857,549
Changes in non-cash working capital items:		
Accounts receivable	(765,155)	138,169
Prepaid expenses and other assets	(81,242)	(130,183)
Accounts payable and accrued liabilities	1,104,932	1,050,940
Net cash flows used in operating activities	<u>(830,681)</u>	<u>(170,339)</u>
Investing activities		
Acquisitions of property, plant and equipment	(11,166,583)	(5,371,752)
Investments in exploration and evaluation assets, net of governmental credits received	(3,514,305)	(3,527,433)
Increase in restricted cash	-	(905,000)
Net cash flows used in investing activities	<u>(14,680,888)</u>	<u>(9,804,185)</u>
Financing activities		
Proceeds from the issuance of a secured loan, net of issue costs (Note 9)	9,955,400	-
Proceeds from the exercise of options	9,528	191,167
Payment of share issue costs	(28,734)	(158,523)
Net cash flows provided by financing activities	<u>9,936,194</u>	<u>32,644</u>
Decrease in cash	<u>(5,575,375)</u>	<u>(9,941,880)</u>
Cash, beginning of period	<u>8,932,271</u>	<u>53,395,140</u>
Cash, end of period	<u>3,356,896</u>	<u>43,453,260</u>

Supplemental disclosure (Note 17)

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

Falco Resources Ltd.

Statements of Changes in Equity

For the three-month periods ended September 30, 2018 and 2017

(Unaudited)

(Expressed in Canadian Dollars)

	Number of shares outstanding	Share capital \$	Convertible Debenture \$	Warrants \$	Contributed surplus \$	Deficit \$	Total \$
Balance – July 1, 2018	189,157,863	103,235,749	6,875,000	4,800,822	8,422,780	(31,064,420)	92,269,931
Net loss and comprehensive loss	-	-	-	-	-	(1,407,533)	(1,407,533)
Warrants expired (Note 11)	-	-	-	(1,573,865)	1,573,865	-	-
Share options (Note 12):							
Share-based compensation	-	-	-	-	418,930	-	418,930
Fair value of options exercised	-	7,062	-	-	(7,062)	-	-
Proceeds from exercise of options	38,113	9,528	-	-	-	-	9,528
Balance - September 30, 2018	189,195,976	103,252,339	6,875,000	3,226,957	10,408,513	(32,471,953)	91,290,856
Balance – July 1, 2017	179,644,768	95,306,645	-	8,783,009	3,087,664	(24,479,613)	82,697,705
Net loss and comprehensive loss	-	-	-	-	-	(1,280,190)	(1,280,190)
Share options:							
Share-based compensation	-	-	-	-	248,834	-	248,834
Fair value of options exercised	-	119,394	-	-	(119,394)	-	-
Proceeds from exercise of options	500,476	191,167	-	-	-	-	191,167
Balance – September 30, 2017	180,145,244	95,617,206	-	8,783,009	3,217,104	(25,759,803)	81,857,516

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

Falco Resources Ltd.

Notes to the Condensed Interim Financial Statements

For the three-month periods ended September 30, 2018 and 2017

(Unaudited)

(Expressed in Canadian Dollars)

1. Nature of activities and going concern

Falco Resources Ltd. ("Falco" or the "Company") was incorporated under the Business Corporations Act (British Columbia) on March 16, 2010. The Company's common shares trade under the symbol "FPC" on the TSX Venture Exchange. On June 12, 2015, the Company was continued under the Canada Business Corporations Act. The Company's registered office is 1100, avenue des Canadiens-de-Montréal, Suite 300, Montréal, Québec, Canada.

The Company is in the business of exploring, evaluating and developing its mineral properties in the Rouyn-Noranda region of the Province of Québec (Canada) for base and precious metals.

On October 30, 2017, the Company filed a National Instrument 43-101, *Standards of Disclosure for Mineral Projects* Technical Report, entitled "*Feasibility Study, Horne 5 Gold Project*", dated effective October 5, 2017 on SEDAR (the "Feasibility Study") relating to its Horne 5 Deposit in Rouyn-Noranda (the "Horne 5 Project" or "Horne 5 Deposit"). Management of the Company ("Management") has determined that the technical feasibility and commercial viability of the Horne 5 Project has been established and accordingly, the development phase of the Horne 5 Project has commenced. As such, the Company has reclassified costs capitalized for the Horne 5 Project from exploration and evaluation assets to property, plant and equipment.

Until it is determined that properties contain mineral reserves or resources that can be economically mined, they are classified as exploration and evaluation properties. The recoverability of deferred exploration and evaluation expenses is dependent on the discovery of economically recoverable reserves and resources; securing and maintaining title and beneficial interest in the properties; the ability to obtain necessary financing to continue the exploration, evaluation and development of its properties; and obtaining certain government approvals or proceeds from the disposal of properties. Changes in future conditions could require material impairment of the carrying value of the deferred exploration and evaluation expenses. Although the Company has taken steps to verify title to its mining properties on which it is currently conducting exploration, evaluation and development work, in accordance with industry standards, these procedures do not guarantee the Company's title. Property title may be subject to unregistered prior agreements and non-compliance with regulatory requirements.

These financial statements have been prepared on the basis of accounting principles applicable to a going concern, which contemplates the realization of assets and settlement of liabilities in the normal course of business as they come due. In assessing whether the going concern assumption is appropriate, Management takes into account all available information about the future, which is at least, but not limited to twelve months from the end of the reporting period. As at September 30, 2018, the Company had negative working capital of \$31,205,916 (including a cash balance of \$3,356,896), for which \$21,533,421 is payable to Osisko Gold Royalties Ltd ("Osisko") relating to financing (see Note 9) and stream arrangements (see Note 7).

As at September 30, 2018, the Company had an accumulated deficit of \$32,471,953 and had incurred a loss of \$1,407,533 for the three-month period ended September 30, 2018. As the Company is in the development stage for the Horne 5 Project, it has not recorded any revenues from operations and has no source of operating cash flow.

The working capital as at September, 2018 will not be sufficient to meet the Company's obligations, commitments and budgeted expenditures through September 30, 2019. Management is aware, in making its assessment, of material uncertainties related to events and conditions that may cast a significant doubt upon the Company's ability to continue as a going concern as described in the preceding paragraph, and accordingly, the appropriateness of the use of accounting principles applicable to a going concern. These financial statements do not reflect the adjustment to the carrying values of assets and liabilities, expenses and balance sheet classifications that would be necessary if the going concern assumption was not appropriate. These adjustments could be material.

The Company's ability to continue future operations and fund its planned development activities at the Horne 5 Deposit is dependent on Management's ability to secure third parties' approvals (see also Note 7) and additional financing in the future. Any funding shortfall may be met in the future in a number of ways, including, but not limited to, the completion of stream agreements (see Note 7) and the issuance of debt or equity instruments. While Management has been successful in securing financing in the past (see Notes 8 and 9), there can be no assurance that it will be able to do so in the future or that these sources of funding or initiatives will be available to the Company or that they will be available on terms which are acceptable to the Company. If Management is unable to obtain new funding, the Company may be unable to continue its operations, and amounts realized for assets might be less than amounts reflected in these financial statements.

Falco Resources Ltd.

Notes to the Condensed Interim Financial Statements

For the three-month periods ended September 30, 2018 and 2017

(Unaudited)

(Expressed in Canadian Dollars)

2. Basis of presentation

These unaudited condensed interim financial statements have been prepared in accordance with *International Financial Reporting Standards* (“IFRS”) as issued by the *International Accounting Standards Board* (“IASB”) applicable to the preparation of interim financial statements, including International Accounting Standard (“IAS”) 34, *Interim Financial Reporting*. The condensed interim financial statements should be read in conjunction with the annual audited financial statements of the Company for the year ended June 30, 2018, which have been prepared in accordance with IFRS as issued by the IASB.

These condensed interim financial statements were approved by the Company's Board of Directors (the “Board”) on November 29, 2018.

The policies applied in these condensed interim financial statements are the same accounting policies and methods as those in Falco's most recent audited annual financial statements except as noted below:

Impact on financial statements IFRS 9, Financial Instruments (“IFRS 9”)

Effective July 1, 2018, the Company has adopted IFRS 9 on a retrospective basis with restatement of comparative periods in accordance with the transitional provisions of IFRS 9. IFRS 9 sets out requirements for recognizing financial assets and liabilities and replaces IAS 39, Financial Instruments: Recognition and Measurement. The adoption of IFRS 9 did not result in any change in the carrying values of any of the Company's financial assets and liabilities on the transition date; therefore, comparative figures have not been restated.

3. Judgments, estimates and assumptions

The preparation of financial statements in conformity with IFRS requires the Company to make judgments, estimates and assumptions on reported amounts of assets and liabilities, and reported amounts of expenses. The estimates and assumptions are based on historical experience and various other factors that are believed to be reasonable under the circumstances, the results of which form the basis of making the judgments about carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may be substantially different. The critical accounting, judgments, estimates and assumptions are the same as those in our most recent audited annual financial statements.

Falco Resources Ltd.

Notes to the Condensed Interim Financial Statements

For the three-month periods ended September 30, 2018 and 2017

(Unaudited)

(Expressed in Canadian Dollars)

4. Property, plant and equipment

	Mining equipment	Land and buildings	Construction in progress	Office and other equipment	Total
	\$	\$	\$	\$	\$
Cost					
Balance – June 30, 2017	6,584,471	2,946,900	-	407,469	9,938,840
Additions	10,244,461	34,996,460	8,231,558	26,104	53,498,583
Transfer from exploration and evaluation assets (Note 5)	-	-	37,531,876	-	37,531,876
Balance – June 30, 2018	<u>16,828,932</u>	<u>37,943,360</u>	<u>45,763,434</u>	<u>433,573</u>	<u>100,969,299</u>
Additions	632,338	2,964,680	1,709,955	-	5,306,973
Transfer of Relocation Project costs	-	(22,500,000)	22,500,000	-	-
Balance – September 30, 2018	<u>17,461,270</u>	<u>18,408,040</u>	<u>69,973,389</u>	<u>433,573</u>	<u>106,276,272</u>
Accumulated Depreciation					
Balance – June 30, 2017	-	-	-	209,266	209,266
Depreciation	-	-	-	12,761	12,761
Depreciation capitalized to exploration and evaluation assets	-	-	-	55,809	55,809
Balance – June 30, 2018	<u>-</u>	<u>-</u>	<u>-</u>	<u>277,836</u>	<u>277,836</u>
Depreciation	-	-	-	3,190	3,190
Depreciation capitalized to exploration and evaluation assets	-	-	-	9,432	9,432
Balance – September 30, 2018	<u>-</u>	<u>-</u>	<u>-</u>	<u>290,458</u>	<u>290,458</u>
Carrying Amounts					
At June 30, 2018	16,828,932	37,943,360	45,763,434	155,737	100,691,463
At September 30, 2018	17,461,270	18,408,040	69,973,389	143,115	105,985,814

On September 12, 2017, the Company concluded an agreement (the "Agreement") with the Commission scolaire de Rouyn-Noranda (the "School Board") to acquire a building (the "Quémont Pavilion") located on the site of the Horne 5 Project. As per the Agreement, Falco will become the owner of the Quémont Pavilion upon completion of relocation activities (the "Relocation Project"). As per the Relocation Project, the Company will transfer the Quémont Pavilion's activities to the Complexe La Source-Polymétier (the "Complex"). Falco funded and executed the expansion of the Complex to accommodate these additional activities and transferred the expanded Complex to the School Board on June 28, 2018. As at September 30, 2018, the construction costs for the Relocation Project totaled \$22,500,000 and have been reclassified from land and buildings to construction in progress. The Company has no more obligations towards the School Board.

On March 24, 2017, the Company entered into an initial agreement for the engineering, procurement, supply, performance services and installation of the hoisting systems for the Horne 5 Project (the "Contract"). The hoisting systems will include a production hoist, an auxiliary hoist and a service hoist. The Contract is now estimated at \$28,900,000, of which \$7,825,000 was incurred and paid as at September 30, 2018 and can be terminated at any time, subject to the payment of the approved and executed work performed by the supplier at the termination date. These amounts are recorded in mining equipment.

Falco Resources Ltd.

Notes to the Condensed Interim Financial Statements

For the three-month periods ended September 30, 2018 and 2017

(Unaudited)

(Expressed in Canadian Dollars)

5. Exploration and evaluation assets

On October 30, 2017, Management determined that the technical feasibility and commercial viability of the Horne 5 Project had been established and accordingly, the development phase of the Horne 5 Project had commenced. As such, the Company reclassified costs capitalized for the Horne 5 Project from exploration and evaluation assets to property, plant and equipment.

The Company has incurred the following costs on its exploration and evaluation assets in the Rouyn-Noranda district:

	For the three-month period ended September 30, 2018			
	Horne 5 Project	Central Camp ⁽ⁱⁱ⁾	Other properties ⁽ⁱⁱⁱ⁾	Total
	\$	\$	\$	\$
Balance – July 1, 2018	-	14,009,617	8,298,657	22,308,274
Compensation	-	86,984	46,826	133,810
Drilling and data compilation	-	1,734,044	142,992	1,877,036
Geology	-	14,268	145,606	159,874
Geophysics	-	34,058	285,787	319,845
Environment	-	-	153	153
Administrative and other	-	3,396	61,570	64,966
Total expenditures for the period	-	1,872,750	682,934	2,555,684
Refundable tax credits	-	-	-	-
Total for the period, net of tax credits	-	1,872,750	682,934	2,555,684
Balance – September 30, 2018	-	15,882,367	8,981,591	24,863,958

	For the year ended June 30, 2018			
	Horne 5 Project ⁽ⁱ⁾	Central Camp ⁽ⁱⁱ⁾	Other properties ⁽ⁱⁱⁱ⁾	Total
	\$	\$	\$	\$
Balance – July 1, 2017	32,989,263	3,614,336	5,540,853	42,144,452
Compensation	95,326	477,187	129,834	702,347
Drilling and data compilation	79,455	10,961,448	1,866,463	12,907,366
Geology	2,000	35,179	286,634	323,813
Geophysics	945	344,167	357,404	702,516
Environment	101,486	259,979	177	361,642
Feasibility studies	1,234,971	-	-	1,234,971
Environmental impact assessment	1,194,630	-	-	1,194,630
Administrative and other	652,931	28,057	215,204	896,192
Total expenditures for the period	3,361,744	12,106,017	2,855,716	18,323,477
Refundable tax credits	(15,179)	(514,688)	(97,912)	(627,779)
Total for the period, net of tax credits	3,346,565	11,591,329	2,757,804	17,695,698
Transfer between properties ^(iv)	1,196,048	(1,196,048)	-	-
Transfer to property, plant and equipment ^(iv)	(37,531,876)	-	-	(37,531,876)
Balance – June 30, 2018	-	14,009,617	8,298,657	22,308,274

(i) Includes historical acquisition costs of \$6,496,194 related to the acquisition of exploration rights and/or claims.

(ii) The Central Camp is located north of the Horne 5 Project and covers an area of approximately 289 square kilometers, including many former gold and base metal producers.

(iii) Including the Noranda Camp properties.

(iv) These costs were incurred in establishing the technical feasibility and commercial viability of the Horne 5 Project and were reclassified to property, plant and equipment (see also Note 4).

Falco Resources Ltd.

Notes to the Condensed Interim Financial Statements

For the three-month periods ended September 30, 2018 and 2017

(Unaudited)

(Expressed in Canadian Dollars)

6. Accounts payable and accrued liabilities

	September 30, 2018	June 30, 2018
	\$	\$
Trade payables and accrued liabilities	16,288,035	22,002,670
Holdbacks payable	1,691,494	1,321,550
Short-term payable on the purchase of property	946,900	946,900
Interest payable on the contingently payable liability (Note 7)	1,493,147	1,493,147
Interest payable on the secured loan (Note 9)	40,274	-
	<u>20,459,850</u>	<u>25,764,267</u>

In September 2014, the Company entered into an option agreement with the City of Rouyn-Noranda to acquire surface rights to land above the Horne 5 Deposit (the "Property"). This option agreement provides the Company with a 5-year option to purchase additional land near the Horne 5 Project. On June 29, 2017, the Company exercised this option, purchasing the Property for \$2,946,900. The Company has paid \$2,000,000 and the final payment of \$946,900 is payable by January 1, 2019.

7. Contingently payable liability

On May 30, 2016, the Company closed a financing with Osisko, a shareholder with significant influence over the Company and therefore a related party, whereby Osisko provided a loan for \$10,000,000 (the "Loan"). The Loan had an initial 18-month maturity, which was ultimately extended to December 31, 2018 on May 31, 2018. The interest is payable on the principal amount at a rate per annum that is equal to 7%, compounded quarterly, payable upon repayment of the principal amount.

By December 31, 2018, Falco and Osisko (collectively, the "Parties") shall negotiate in good faith the terms, conditions and form of a silver and/or gold stream agreement (the "Stream Agreement"), whereby Osisko may provide Falco with a portion of the development capital required to build the Horne 5 Project.

At the maturity date, if the Parties have not concluded the Stream Agreement, the principal amount of the Loan will be converted into a 1% net smelter return royalty on the Horne 5 Project, subject to a right of first refusal ("ROFR") in favor of Glencore Canada Corporation ("Glencore Canada") and accrued interest will be paid in cash.

Under certain events of default, Osisko may, at its option, require the repayment of the principal amount and the accrued interest in cash. Events of default include, but are not limited to, the failure to obtain the required permits to advance the development of the Horne 5 Project before the Loan's maturity date and a change of control of the Company.

On June 18, 2018, the Company announced the Stream Agreement with Osisko, whereby Osisko will provide the Company with staged payments totaling up to \$180 million, toward the funding of the development of the Horne 5 Project, payable as follows:

- First deposit of \$25 million on closing of the Stream Agreement, net of any amounts owing by the Company to Osisko;
- Second deposit of \$20 million upon the Company receiving all necessary material third-party approvals, licenses, rights of way, and surface rights;
- Third deposit of \$35 million following receipt of all material permits required for the construction of a mine at the Horne 5 Project, a positive construction decision for the Horne 5 Project, and raising a minimum of \$100 million in equity, joint venture or any other non-debt financing for the construction of the mine;
- Fourth deposit of \$60 million upon the total projected capital expenditure for the Horne 5 Project having been demonstrated to be financed; and
- Optional fifth deposit of \$40 million at the sole election of Osisko to increase the stream percentage, payable concurrently with the fourth deposit.

Under the terms of the Stream Agreement, Osisko will purchase 90% of the payable silver from the Horne 5 Project, increasing to 100% of the payable silver from the Horne 5 Project in the event the optional fifth deposit is paid. In exchange for the silver delivered under the Stream Agreement, Osisko will pay the Company ongoing payments equal to 20% of the spot price of silver on the day of delivery, subject to a maximum payment of USD\$6.00 per silver ounce. The silver produced from the Horne 5 Project and properties within a 5 km area of interest will be subject to the Stream Agreement.

Falco Resources Ltd.

Notes to the Condensed Interim Financial Statements

For the three-month periods ended September 30, 2018 and 2017

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7. Contingently payable liability (*continued*)

Pursuant to the Stream Agreement, the Company has agreed to pay a \$2,000,000 capital commitment fee. The fee is payable upon Osisko funding the third deposit under the Stream Agreement.

Closing of the Stream Agreement is subject to the satisfaction of customary conditions, including obtaining regulatory approvals and approval from a majority of the minority shareholders of Falco (the "Approval"). The special meeting for shareholders of Falco for the Approval will take place on November 29, 2018.

Pursuant to the Agreement, the Stream Agreement is subject to a ROFR in favor of Glencore Canada. Pursuant to the ROFR, Glencore Canada shall have a period of 60 days following the receipt of a notice accompanied by a copy of the Stream Agreement to notify Falco that it wishes to purchase the silver stream in accordance with the terms described in the Stream Agreement.

As of September 30, 2018, the Company has incurred \$500,000 of transaction costs on the Stream Agreement, which is accounted for as an other non-current asset on the balance sheet.

8. Convertible debenture

On June 29, 2018, the Company closed a financing transaction (the "Convertible Debenture") with Osisko for \$7,000,000. Under the terms of the Convertible Debenture, Osisko purchased a secured debenture (the "Debenture") having a principal amount of \$7,000,000 (the "Principal").

Upon receipt of the Approval, the Debenture will be convertible (the "Conversion") into units of the Company (the "Converted Units"). There will be no interest payable at any time on the outstanding Principal of the Debenture unless Falco fails to obtain the Approval, in which case interest shall accrue retroactively from the closing date of the Convertible Debenture at a rate per annum that is equal to 7%, compounded quarterly. Accrued interest shall be payable upon repayment of the Principal when due, as per the terms of the Debenture. The maturity date of the Debenture shall be the earlier of (i) the date of the meeting of the Falco shareholders to be held to obtain the Approval and (ii) December 31, 2018.

On the date upon which the Company obtains the Approval, the Debenture shall be converted into 12,104,444 Converted Units of Falco. Each Converted Unit shall consist of one common share of the Company ("Common Share") and one-half of one common share purchase warrant ("Warrant"). Each whole Warrant shall entitle the holder to purchase one Common Share, subject to customary anti-dilution clauses, at a price of \$0.75 for a period of thirty-six months from the date the Converted Units are issued.

As the Company has the unconditional right to avoid delivering cash or another financial asset to settle the Debenture, it has been recorded in equity, net of \$125,000 in transaction costs in the statement of financial position as at September 30, 2018.

9. Secured loan

On September 10, 2018, Falco closed a secured senior loan agreement with Osisko (the "Secured Loan"). Under the terms of the Secured Loan, Osisko provided the Company with a loan for \$10,000,000 (the "Principal Amount"). The Secured Loan will be used for the advancement of the Horne 5 Project and for general corporate purposes. The Secured Loan has a maturity date of December 31, 2018 and interest shall be payable on the Principal Amount at a rate per annum that is equal to 7%, compounded quarterly. Accrued interest shall be payable upon repayment of the Principal Amount. The Principal Amount shall be repaid on the earliest of the closing date of the Stream Agreement (Note 7) or December 31, 2018. The Principal Amount, has been recorded as a short-term liability, net of \$44,600 in transaction costs, in the statement of financial position as at September 30, 2018.

Falco Resources Ltd.

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(Unaudited)

(Expressed in Canadian Dollars)

10. Deferred premium on flow-through shares

	September 30, 2018	June 30, 2018
	\$	\$
Balance – beginning of period	489,851	2,284,567
Deferred premium on flow-through shares issued	-	1,599,441
Recognition of deferred premium on flow-through shares	(489,851)	(3,394,157)
Balance – end of period	-	489,851

On December 21, 2017, the Company issued 7,203,730 flow-through shares for gross proceeds of \$8,500,401 and recognized a deferred premium on flow-through shares of \$1,728,895, net of \$129,454 of share issue costs. As at September 30, 2018, the Company has completed its commitment to spending the gross proceeds on exploration activities.

11. Warrants

The following table details the changes in the Company's warrants:

	Number of Warrants	Weighted Average Exercise Price
		\$
Balance – June 30, 2017	28,281,717	1.55
Issued	350,000	1.15
Expired	(12,091,675)	1.45
Balance – June 30, 2018	16,540,042	1.61
Expired	(5,046,542)	1.45
Balance – September 30, 2018	11,493,500	1.68

The warrants outstanding at September 30, 2018, are as follows:

Exercise Price (\$)	Number of Warrants	Expiry Date	Weighted Average Remaining Contractual Life (Years)
1.15	350,000	October 4, 2022	4.01
1.70	11,143,500	December 7, 2018	0.19
	11,493,500		

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For the three-month periods ended September 30, 2018 and 2017

(Unaudited)

(Expressed in Canadian Dollars)

12. Share-based compensation

Share options

The following table summarizes information about the movement of the share options:

	Number of options	Weighted Average Exercise Price (\$)
Balance – June 30, 2017	9,151,736	0.49
Granted	3,206,000	0.95
Exercised	(1,959,365)	0.41
Expired	(50,000)	0.45
Balance – June 30, 2018	10,348,371	0.65
Exercised	(38,113)	0.25
Balance – September 30, 2018	10,310,258	0.65
Options exercisable – September 30, 2018	5,689,036	0.44

Share option compensation for the three-month period ended September 30, 2018 amounted to \$418,931 (\$248,834 for the three-month period ended September 30, 2017) of which \$42,049 (\$ nil for the three-month period ended September 30, 2017) was capitalized to construction in progress and \$10,904 (\$15,283 for the three-month period ended September 30, 2017) were capitalized to exploration and evaluation assets.

Restricted, deferred and performance share units

The Company has a share unit plan (the "LTI Plan") for the benefit of the Company's employees and consultants. The LTI Plan provides for the issuance of common shares from treasury, in the form of Restricted Share Units ("RSUs"), Deferred Shares Units and Performance Share Units which can be settled in cash or whole common shares, at the discretion of the Company. The maximum number of shares reserved for issuance should not exceed 2,500,000 shares.

No RSUs are outstanding as at September 30, 2018 (nil as at June 30, 2018). Share-based compensation expense for RSUs for the three-month periods ended September 30, 2018 amounted to \$ nil (\$4,476 for the three-month period ended September 30, 2017).

13. Net loss per share

The calculation of basic and diluted loss per share for the three-month period ended September 30, 2018 was based on the net loss attributable to shareholders of \$1,407,533 (\$1,280,190 for the three-month period ended September 30, 2017) and the weighted average number of common shares outstanding for the three-month period ended September 30, 2018 of 189,187,691 (179,743,170 common shares for the three-month period ended September 30, 2017). As a result of the net loss for the three-month periods ended September 30, 2018 and 2017, all potentially dilutive common shares (Notes 8, 11 and 12) are deemed to be antidilutive and thus diluted net loss per share is equal to the basic net loss per share for these periods.

Falco Resources Ltd.

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For the three-month periods ended September 30, 2018 and 2017

(Unaudited)

(Expressed in Canadian Dollars)

14. Key management and related party transactions

Key management includes directors (executive and non-executive) and certain officers of the Company. The compensation paid or payable to key management for employee services is presented below for the three-month periods ended September 30, 2018 and 2017:

	2018	2017
	\$	\$
Salaries and short-term employee benefits ⁽¹⁾	398,192	496,898
Share-based compensation	343,884	221,440
	<u>742,076</u>	<u>718,338</u>

⁽¹⁾ Including consulting fees.

Related party transactions and balances, not otherwise disclosed, are summarized below:

During the three-month period ended September 30, 2018, an amount of \$397,817 (\$714,467 for the three-month period ended September 30, 2017) was invoiced by Osisko for professional services and rental of offices. An amount of \$1,754,407 is included in accounts payable and accrued liabilities as at September 30, 2018 (\$1,356,590 as at June 30, 2018).

On May 30, 2016, the Company entered into the Loan with Osisko (Note 9). As at September 30, 2018, interest payable on this loan amounted to \$1,493,147 (\$1,493,147 as at June 30, 2018) and was included in accounts payable and accrued liabilities on the balance sheet. Interest expense on the Loan for the three-month period ended September 30, 2018 was \$ nil (\$189,603 for the three-month period ended September 30, 2017).

On September 10, 2018, the Company entered into the Secured Loan with Osisko (Note 9). As at September 30, 2018, interest expense and interest payable on the Secured Loan amounted to \$40,274 and was included in accounts payable and accrued liabilities on the balance sheet.

15. Fair value of financial instruments

The Company has no financial assets and no financial liabilities at fair value in the balance sheets as at September 30, 2018 and June 30, 2018.

Financial instruments that are not measured at fair value on the balance sheets are represented by cash, restricted cash, accounts payable and accrued liabilities, the contingently payable liability and the Secured Loan. The fair values of these instruments approximate their respective carrying values due to their short-term nature.

Falco Resources Ltd.

Notes to the Condensed Interim Financial Statements

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(Unaudited)

(Expressed in Canadian Dollars)

16. Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet the obligations associated with its financial liabilities. The Company manages the liquidity risk by continuously monitoring actual and projected cash flows, taking into account the requirements related to its investment commitments and mining properties and matching the maturity profile of financial assets and liabilities. The Board reviews and approves any material transaction out of the ordinary course of business, including proposals on mergers, acquisitions or other major investments or divestitures. As at September 30, 2018, cash is comprised of bank balances. As described in Note 1, the Company estimates that with its liquidity position as at September 30, 2018, it does not have enough funds available to meet its financial liabilities for the next year.

The following table summarizes the Company's contractual commitments, including interest as at September 30, 2018:

	Less than one year	Between one and three years	More than three years
	\$	\$	\$
Accounts payable and accrued liabilities	18,926,429	-	-
Contingently payable liability	11,493,147	-	-
Secured Loan	10,160,000	-	-

The following table summarizes the Company's contractual commitments, including interest as at June 30, 2018:

	Less than one year	Between one and three years	More than three years
	\$	\$	\$
Accounts payable and accrued liabilities	24,271,120	-	-
Contingently payable liability	11,493,147	-	-

17. Supplemental disclosure – Statements of cash flows

	Three-months ended September 30, 2018	Three-months ended September 30, 2017
	\$	\$
Property and equipment acquisitions included in accounts payable and accrued liabilities and long-term payable on the purchase of property		
Beginning of period	17,360,519	3,309,234
End of period	11,464,827	5,841,465
Exploration and evaluation asset expenditures included in accounts payable and accrued liabilities		
Beginning of period	3,652,179	1,748,818
End of period	2,667,256	3,581,068
Share issue costs included in accounts payable and accrued liabilities		
Beginning of period	28,734	158,523
End of period	-	-
Depreciation capitalized	9,432	11,422
Interest income received	25,773	153,455
Refundable tax credits received	800,000	-
Other non-current assets included in accounts payable and accrued liabilities	500,000	-