

TERAGO INC.
Condensed Consolidated Financial Statements
Three and nine months ended September 30, 2018 and 2017
(Unaudited)

Contents

Condensed Consolidated Financial Statements

Statements of Financial Position	2
Statements of Comprehensive Loss	3
Statements of Cash Flows	4
Statements of Changes in Equity	5
Notes to Financial Statements	6-17

TERAGO INC.
Condensed Consolidated Statements of Financial Position
(In thousands)
(unaudited)

	<i>Note</i>	September 30 2018	December 31 2017*
Assets			
Cash and cash equivalents	6(a)	\$ 9,488	\$ 6,986
Accounts receivable	6(b)	3,851	3,389
Prepaid expenses and other assets		1,503	2,516
Current portion of contract costs		541	-
Current portion of other long-term assets	10(a)	39	27
Total current assets		15,422	12,918
Network assets, property and equipment	7	37,103	38,822
Intangible assets	8	14,936	16,699
Goodwill	8	19,419	19,419
Contract costs	3(a)(iii)	529	-
Other long-term assets	10(a)	41	-
Total non-current assets		72,028	74,940
Total Assets		\$ 87,450	\$ 87,858
Liabilities			
Accounts payable and accrued liabilities		\$ 6,428	\$ 8,519
Current portion of deferred revenue		-	282
Current portion of contract liabilities	3(a)(iv)	171	-
Current portion of long-term debt	9	4,000	4,000
Current portion of other long-term liabilities	10(b)	174	56
Total current liabilities		10,773	12,857
Decommissioning and restoration obligations		298	277
Deferred revenue		-	205
Contract liabilities	3(a)(v)	94	-
Long-term debt	9	29,250	32,183
Other long-term liabilities	10(b)	582	419
Total non-current liabilities		30,224	33,084
Total Liabilities		40,997	45,941
Shareholders' Equity			
Share capital		93,110	86,653
Contributed surplus		25,666	25,701
Deficit		(72,323)	(70,437)
Total Shareholders' Equity		\$ 46,453	\$ 41,917
Total Liabilities and Shareholders' Equity		\$ 87,450	\$ 87,858

*The Company has initially applied IFRS 15 using the cumulative effect method. Under this method, the comparative information is not restated.

On behalf of the Board:

(signed) "Matthew Gerber"

Director

(signed) "Gary Sherlock"

Director

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

TERAGO INC.
Condensed Consolidated Statements of Comprehensive Loss
(In thousands, except per share amounts)
(unaudited)

		Three months ended September 30		Nine months ended September 30	
	Note	2018	2017*	2018	2017*
Revenue	5	\$ 14,004	13,680	\$ 41,427	41,849
Expenses					
Cost of services		3,488	3,511	10,509	10,559
Salaries and related costs		4,659	4,665	13,596	14,593
Other operating expenses		2,772	2,673	9,640	7,991
Depreciation of network assets, property and equipment	7	2,331	2,807	7,152	8,525
Amortization of intangible assets	8	497	757	1,875	2,307
		<u>13,747</u>	<u>14,413</u>	<u>42,772</u>	<u>43,975</u>
Income (Loss) from operations		257	(733)	(1,345)	(2,126)
Foreign exchange gain		12	18	18	35
Finance costs		(343)	(350)	(1,549)	(1,175)
Finance income		27	18	28	33
Loss before income taxes		<u>\$ (47)</u>	<u>(1,047)</u>	<u>\$ (2,848)</u>	<u>(3,233)</u>
Income taxes					
Income tax expense		-	-	-	-
Net loss and comprehensive loss		<u>\$ (47)</u>	<u>(1,047)</u>	<u>\$ (2,848)</u>	<u>(3,233)</u>
Deficit, beginning of period**		<u>\$ (72,276)</u>	<u>(65,329)</u>	<u>\$ (69,475)</u>	<u>(63,143)</u>
Deficit, end of period		<u>\$ (72,323)</u>	<u>(66,376)</u>	<u>\$ (72,323)</u>	<u>(66,376)</u>
Basic loss per share	12	\$ (0.00)	(0.07)	\$ (0.19)	(0.23)
Diluted loss per share	12	\$ (0.00)	(0.07)	\$ (0.19)	(0.23)
Basic weighted average number of shares outstanding		15,736	14,334	14,910	14,292
Diluted weighted average number of shares outstanding		15,736	14,334	14,910	14,292

*The Company has initially applied IFRS 15 using the cumulative effect method. Under this method, the comparative information is not restated.

**Adjusted for the adoption of IFRS 15 on January 1, 2018

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

TERAGO INC.
Condensed Consolidated Statements of Cash Flows
(In thousands)
(unaudited)

		Three months ended September 30		Nine months ended September 30	
	Note	2018	2017*	2018	2017*
Operating Activities					
Net loss for the period		\$ (47)	(1,047)	\$ (2,848)	(3,233)
Adjustments to reconcile net loss to net cash provided by operating activities:					
Severance, acquisition, and other costs		90	371	689	1,090
Depreciation of network assets, property and equipment	7	2,331	2,807	7,152	8,525
Amortization of intangible assets	8	497	757	1,875	2,307
Stock-based compensation expense	11(d)	250	8	684	45
Finance costs		343	350	1,549	1,175
Finance income		(27)	(18)	(28)	(33)
Loss on adjustments and disposal of network assets	7	104	(1)	360	94
Impairment of assets and related charges	7	64	-	431	-
Severance, acquisition, and other costs paid		(105)	(868)	(606)	(2,586)
Stock-based compensation paid		-	-	-	(644)
Changes in non-cash working capital items:					
Accounts receivable		(386)	(486)	(541)	167
Prepaid expenses		494	319	1,013	368
Accounts payable and accrued liabilities		(222)	685	(1,146)	(1,293)
Deferred revenue		-	8	-	(79)
Contract liabilities		(47)	-	(159)	-
Contract costs		(68)	-	(171)	-
Cash from Operating Activities		3,271	2,885	8,254	5,903
Investing Activities					
Purchase of network assets, property and equipment	7	(1,451)	(1,667)	(6,224)	(4,911)
Purchase of intangible assets	8	-	(3)	(112)	(76)
Change in non-cash working capital related to network assets, property and equipment and intangible assets		(13)	(659)	(1,209)	(2,106)
Cash used in Investing Activities		(1,464)	(2,329)	(7,545)	(7,093)
Financing Activities					
Proceeds from exercise of stock options		-	-	-	196
Proceeds from equity offering	14	-	-	6,906	-
Equity offering costs incurred	14	(19)	-	(858)	-
Interest paid, net of received		(485)	(410)	(1,255)	(1,208)
Repayment of long-term debt		(1,000)	(1,049)	(3,000)	(3,394)
Financing costs incurred		-	-	-	(312)
Cash from (used in) Financing Activities		(1,504)	(1,459)	1,793	(4,718)
Net change in cash and cash equivalents, during the period		303	(903)	2,502	(5,908)
Cash and cash equivalents, beginning of period		9,185	8,029	6,986	13,034
Cash and cash equivalents, end of period		\$ 9,488	7,126	\$ 9,488	7,126

*The Company has initially applied IFRS 15 using the cumulative effect method. Under this method, the comparative information is not restated.

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

TERAGO INC.
Consolidated Statements of Changes in Equity
(In thousands)
(unaudited)

	Share Capital		Contributed			
	Number	Amount	Surplus	Deficit	Total	
Balance, January 1, 2018	14,365	\$ 86,653	\$ 25,701	\$ (70,437)	\$	41,917
Adjustments on initial application of IFRS 15*	-	-	-	962		962
Adjusted Balance at January 1, 2018	14,365	86,653	25,701	(69,475)		42,879
Issuance of shares upon exercise of options	41	115	(114)	-		1
Stock-based compensation	-	-	79	-		79
Issuance of shares for directors' fees	45	294	-	-		294
Issuance of shares for equity offering - net of issuance costs (Note 14)	1,303	6,048	-	-		6,048
Net loss and comprehensive loss	-	-	-	(2,848)		(2,848)
Balance, September 30, 2018	15,754	\$ 93,110	\$ 25,666	\$ (72,323)	\$	46,453

	Share Capital		Contributed			
	Number	Amount	Surplus	Deficit	Total	
Balance, January 1, 2017**	14,250	\$ 86,171	\$ 25,620	\$ (63,143)	\$	48,648
Issuance of shares upon exercise of options	49	196	-	-		196
Stock-based compensation	-	-	35	-		35
Issuance of shares for directors' fees	34	147	-	-		147
Net loss and comprehensive loss	-	-	-	(2,186)		(2,186)
Balance, September 30, 2017**	14,333	86,514	25,655	(65,329)		46,840

*See Note 3(a)(vi).

**The Company has initially applied IFRS 15 using the cumulative effect method. Under this method, the comparative information is not restated.

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

TERAGO INC.
Notes to the Consolidated Financial Statements
(In thousands, except for per share amounts)
(unaudited)

1. Reporting Entity

TeraGo Inc. (the "Company") provides businesses across Canada with connectivity services, colocation services and enterprise infrastructure cloud services. The Company's head office is located in Canada at Suite 800 – 55 Commerce Valley Drive West, Thornhill, Ontario. The Company was incorporated under the Canada Business Corporations Act on December 21, 2000 and owns and operates a carrier-grade, fixed wireless, fibre-based, IP communications network, as well as cloud and colocation facilities in Canada targeting enterprise customers that require cloud, colocation, and connectivity services. The Company's common shares are listed on the Toronto Stock Exchange (TSX) under the symbol TGO.

2. Basis of Preparation and Presentation

(a) Basis of preparation

These unaudited condensed interim consolidated financial statements ("interim financial statements") were prepared using the same accounting policies and methods as those used in the Company's consolidated financial statements for the year ended December 31, 2017 (the "2017 Consolidated Financial Statements") except as described in Note 3. These interim financial statements are in compliance with International Accounting Standard 34, Interim Financial Reporting ("IAS 34"). Accordingly, certain information and footnote disclosure normally included in annual financial statements prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"), have been omitted or condensed.

The preparation of financial statements in accordance with IAS 34 requires the use of certain critical accounting estimates. It also requires management to exercise judgment in applying the Company's accounting policies. The areas involving a higher degree of judgment or complexity, or areas where assumptions and estimates are significant to the financial statements have been set out in Note 2 of the Company's 2017 Consolidated Financial Statements. These interim financial statements should be read in conjunction with the Company's 2017 Consolidated Financial Statements.

The Company's operating results are subject to seasonal fluctuations that may materially impact quarter-to-quarter operating results and, thus, one quarter's operating results are not necessarily indicative of a subsequent quarter's operating results.

The policies applied in these interim financial statements are based on IFRS issued and outstanding as at September 30, 2018. The Board of Directors authorized the interim financial statements for issue on November 7, 2018.

These interim financial statements include the accounts of TeraGo Inc. and its wholly owned subsidiary, TeraGo Networks Inc.

The notes presented in these interim financial statements include only significant changes and transactions that have occurred since the last fiscal year end.

(b) Functional and Presentation Currency

These consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency.

3. Accounting Pronouncements Adopted in 2018

a) IFRS 15 Revenue from Contracts with Customers

Effective January 1, 2018, the Company adopted IFRS 15 Revenue from Contracts with Customers. IFRS 15 supersedes the existing standards and interpretations including IAS 18, Revenue and IFRIC 13, Customer Loyalty Programmes. IFRS 15 introduces a single model for recognizing revenue from contracts with customers with the exception of certain contracts under other IFRSs. The standard requires revenue to be recognized in a manner that depicts the transfer of promised goods or services to a customer and at an amount that reflects the expected consideration receivable in exchange for transferring those goods or services. This is achieved by applying the following five steps:

TERAGO INC.
Notes to the Consolidated Financial Statements
(In thousands, except for per share amounts)
(unaudited)

1. Identify the contract with a customer;
2. Identify the performance obligations in the contract;
3. Determine the transaction price;
4. Allocate the transaction price to the performance obligations in the contract; and
5. Recognize revenue when (or as) the entity satisfies a performance obligation.

IFRS 15 also provides guidance relating to the treatment of contract acquisition and contract fulfillment costs.

The Company adopted IFRS 15 using the cumulative effect method, i.e. by recognizing the cumulative effect of initially applying IFRS 15 as an adjustment to the opening balance of retained earnings at January 1, 2018. Therefore, comparative information has not been restated and continues to be reported under IAS 18.

The Company has implemented several processes and policies to ensure the consistent, timely, and appropriate allocation of revenue between performance obligations in contracts with customers.

The adoption of IFRS 15 did not affect the Company's cash flows from operating, investing, or financing activities. Furthermore, the impact on timing of revenue recognition was not material as the treatment of revenue for services rendered over time, which is the method under which Company satisfies the majority of its performance obligations, is consistent under IFRS 15 and IAS 18. The details of the significant changes and quantitative impact of the changes are outlined below.

i) Sale of Bundled Services

The Company offers certain customers bundled connectivity, colocation, and cloud services. Revenue from these arrangements were previously classified based on the nature of the contract. Under IFRS 15, total consideration in contracts with customers are allocated to distinct performance obligations based on their stand-alone selling prices. The Company determined the stand-alone selling price to be the list price at which the Company sells connectivity, and colocation and cloud services. As a result of the allocation of performance obligations under IFRS 15, certain amounts that would have been classified as cloud and colocation revenue are now presented as connectivity revenue.

ii) Service Credits

The Company has obligations for credits under its contracts with customers when certain criteria are met. Credits are recognized net of revenue recognized and presented in total revenue on the statement of comprehensive income.

iii) Contract Costs

IFRS 15 requires certain contract acquisition costs to be recognized as an asset on the statement of financial position and amortized into income over time. The Company typically incurs internal or external sales commissions to obtain contracts with customers. Prior to the adoption of IFRS 15, the Company expensed all commission costs as incurred. The Company now capitalizes these commission fees as costs of obtaining a contract when they are incremental and expected to be recovered. These costs are amortized consistently with the pattern of revenue for the related contracts and are recorded in salaries and related costs on the statement of comprehensive loss.

Contract costs are presented separately as an asset on the consolidated statement of financial position. The Company has opted not to use practical expedients under the cumulative effect method and as a result, the current portion of contract costs are presented in current assets. The current portion represent amounts expected to be amortized in the next 12 months. The Company had to make significant judgments and estimates when estimating certain contract costs incurred in prior years that continue to be incremental and recoverable in the current period.

The following table summarizes the key movement in contract costs during the three and nine months ended September 30, 2018:

TERAGO INC.
Notes to the Consolidated Financial Statements
(In thousands, except for per share amounts)
(unaudited)

	Three months ended September 30	Nine months ended September 30
	2018	2018
Opening Balance	\$ 1,002	\$ 899
Incremental commissions capitalized	239	648
Amortization	(171)	(477)
Balance end of period	1,070	1,070
Less: current	(541)	(541)
	\$ 529	\$ 529

iv) Contract Assets

Contract assets arise primarily as a result of services offered and provided in advance of payments received from a customer. From time to time, the Company will offer promotions which will give rise to contract assets. These arrangements are recorded in other long-term assets on the balance sheet with current and long-term amounts presented separately on the statement of financial position. The current portion represents the performance obligation to be satisfied and recognized as revenue in the next twelve months.

v) Contract Liabilities

Contract liabilities arise primarily as a result of payment received in advance of providing services to a customer. The Company had previously presented these arrangements as deferred revenue. These payments are now presented as contract liabilities with current and long-term amounts presented separately on the statement of financial position. The current portion represents the performance obligation to be satisfied and recognized as revenue in the next twelve months.

vi) Impacts on Consolidated Financial Statements

Impact on Consolidated Statement of Financial Position

	As at September 30 2018			As at January 1 2018		
	As Reported	Adj.	Balances without adoption of IFRS 15	Balance after adoption of IFRS 15	Adj.	Balances without adoption of IFRS 15
Assets						
Cash and cash equivalents	9,488	-	9,488	6,986	-	6,986
Accounts receivable	3,851	79	3,930	3,389	-	3,389
Prepaid expenses and other assets	1,503	-	1,503	2,516	-	2,516
Other long-term assets	80	(80)	-	27	-	27
Network assets, property and equipment	37,103	-	37,103	38,822	-	38,822
Intangible assets	14,936	-	14,936	16,699	-	16,699
Goodwill	19,419	-	19,419	19,419	-	19,419
Contract costs	1,070	(1,070)	-	899	(899)	-
Total Assets	87,450	(1,071)	86,379	88,757	(899)	87,858
Liabilities						
Accounts payable and accrued liabilities	6,428	-	6,428	8,519	-	8,519
Deferred revenue	-	339	339	-	487	487
Contract liabilities	265	(265)	-	424	(424)	-
Long-term debt	33,250	-	33,250	36,183	-	36,183
Other long-term liabilities	756	-	756	475	-	475
Decommissioning and restoration obligations	298	-	298	277	-	277
Total Liabilities	40,997	74	41,071	45,878	63	45,941

TERAGO INC.
Notes to the Consolidated Financial Statements
(In thousands, except for per share amounts)
(unaudited)

Shareholders' Equity

Share capital	93,110	-	93,110	86,653	-	86,653
Contributed surplus	25,666	-	25,666	25,701	-	25,701
Deficit	(72,323)	(1,145)	(73,468)	(69,475)	(962)	(70,437)
Total Shareholders' Equity	87,450	(1,071)	86,379	88,757	(899)	87,858

Impact on Consolidated Statement of Comprehensive Income

	Three months ended September 30 2018			Nine months ended September 30 2018		
	As Reported	Adj.	Balances without adoption of IFRS 15	As Reported	Adj.	Balances without adoption of IFRS 15
Revenue	14,004	(23)	13,981	41,427	(11)	41,416
Cost of services	(3,488)	-	(3,488)	(10,509)	-	(10,509)
Salaries and related costs	(3,765)	(68)	(3,833)	(13,596)	(171)	(13,767)
Other operating expenses	(3,666)	-	(3,666)	(9,640)	-	(9,640)
Depreciation of network assets, property and equipment	(2,331)	-	(2,331)	(7,152)	-	(7,152)
Amortization of intangible assets	(497)	-	(497)	(1,875)	-	(1,875)
Foreign exchange gain	12	-	12	18	-	18
Finance costs	(343)	-	(343)	(1,549)	-	(1,549)
Finance income	27	-	27	28	-	28
Income tax expense	-	-	-	-	-	-
Net loss and comprehensive loss	(47)	(91)	(138)	(2,848)	(182)	(3,030)

Impact on Consolidated Statement of Cash Flows

	Three months ended September 30 2018			Nine months ended September 30 2018		
	As Reported	Adj.	Balances without adoption of IFRS 15	As Reported	Adj.	Balances without adoption of IFRS 15
Operating Activities						
Net loss for the year	(47)	(91)	(138)	(2,848)	(182)	(3,030)
Adjustments to reconcile net loss to net cash provided by (used in) operating activities	3,547	-	3,547	12,106	-	12,106
Changes in non-cash working capital items:						
Accounts receivable	(387)	-	(387)	(541)	-	(541)
Prepaid expenses	494	-	494	1,013	-	1,013
Accounts payable and accrued liabilities	(121)	-	(121)	(1,146)	-	(1,146)
Deferred revenue	-	(24)	(24)	-	(148)	(148)
Contract liabilities	(47)	47	-	(159)	159	-
Contract costs	(68)	68	-	(171)	171	-
Cash from Operating Activities	3,371	-	3,371	8,254	-	8,254
Cash used in Investing Activities	(1,464)	-	(1,464)	(7,545)	-	(7,545)
Cash from (used in) Financing Activities	(1,604)	-	(1,604)	1,793	-	1,793
Net change in cash and cash equivalents, during the period	303	-	303	2,502	-	2,502
Cash and cash equivalents, beginning of period	9,185	-	9,185	6,986	-	6,986
Cash and cash equivalents, end of period	9,488	-	9,488	9,488	-	9,488

TERAGO INC.
Notes to the Consolidated Financial Statements
(In thousands, except for per share amounts)
(unaudited)

vii) Use of estimates

The Company used estimates in the following areas:

- Determining the enforceable term of contracts required estimating average contract terms based on available historical data
- Significant judgments in determining whether the promises to deliver certain services are considered distinct and represent separate performance obligations
- Evaluating whether costs incurred to obtain a contract were incremental and expected to be recoverable

b) IFRS 9 Financial Instruments

Effective January 1, 2018, the Company adopted IFRS 9 Financial Instruments. IFRS 9 sets out requirements for recognising and measuring financial assets, financial liabilities and some contracts to buy or sell non-financial items. This standard replaces IAS 39 Financial Instruments: Recognition and Measurement.

The adoption of this standard did not have a material effect on our consolidated financial statements.

i) Impairment of financial assets

IFRS 9 replaces the 'incurred loss' model in IAS 39 with an 'expected credit loss' (ECL) model. The new impairment model applies to financial assets measured at amortised cost, contract assets and debt investments at FVOCI, but not to investments in equity instruments. Under IFRS 9, credit losses are recognised earlier than under IAS 39.

The Company's financial assets measured at amortized cost consist of assets discussed in Note 13.

Under IFRS 9, loss allowances are measured on either of the following bases:

- *12-month ECLs*: these are ECLs that result from possible default events within the 12 months after the reporting date; and
- *lifetime ECLs*: these are ECLs that result from all possible default events over the expected life of a financial instrument.

The Company measures loss allowances for trade receivables and any contract assets at an amount equal to lifetime ECLs. When determining whether the credit risk of a financial asset has increased significantly since initial recognition and when estimating ECLs, the Company considers reasonable and supportable information that is relevant and available without undue cost or effort. This includes both quantitative and qualitative information and analysis, based on the Company's historical experience and informed credit assessment and including forward-looking information.

At each reporting date, the Company assesses whether financial assets carried at amortized cost are credit-impaired.

ii) Measurement of loss allowances

For trade receivables, the Company uses historic actual credit losses as the basis for estimating ECLs and uniformly applies this estimate to its gross balance net of balances already fully impaired at each reporting date. The Company believes this amount to best estimate the expected credit losses.

iii) Presentation of loss allowances

Loss allowances on financial assets measured at amortized cost are deducted from the gross carrying amount of the asset and the related impairment loss is recorded separately on the statement of comprehensive income.

4. Upcoming accounting pronouncements not yet adopted

The IASB has issued new standards and amendments to existing standards. These changes are not yet adopted as at September 30, 2018 and could have an impact on future periods.

TERAGO INC.
Notes to the Consolidated Financial Statements
(In thousands, except for per share amounts)
(unaudited)

IFRS 16 Leases

On January 13, 2016, the IASB issued the final publication of the IFRS 16 standard, which will supersede the current IAS 17, Leases standard. Under IFRS 16, a lease will exist when a customer controls the right to use an identified asset as demonstrated by the customer having exclusive use of the asset for a period of time. IFRS 16 introduces a single accounting model for lessees and all leases will require an asset and liability to be recognized on the statement of financial position at inception.

The standard is effective for annual periods beginning on or after January 1, 2019 with early adoption permitted, but only if the entity is also applying IFRS 15. The Company has a dedicated team to assess the impact of IFRS 16 and the team has started gathering the information necessary to evaluate the impact of the standard. The team is expected to quantify the impact of the standard upon completion of their assessment.

5. Revenue

The Company's operations and main sources of revenue are those described in the 2017 Consolidated Financial Statements. The Company's revenue is primarily derived from contracts with customers.

The effect of initially applying IFRS 15 on the Company's interim financial statements is disclosed in Note 3(a).

Satisfaction of performance obligations

The Company measures the timing of satisfaction of its performance obligations from contracts with customers consistently across all the Company's performance obligations: as services are provided (typically on a monthly basis).

Disaggregation of revenue

In the following table and in accordance with IFRS 15, the Company's disaggregates revenue into two primary categories that depict the nature of its revenue streams.

	Three months ended September 30		Nine months ended September 30	
	2018	2017*	2018	2017*
Cloud and Colocation Revenue	\$ 5,190	4,705	\$ 14,815	14,234
Connectivity Revenue	8,814	8,975	26,612	27,615
	<u>\$ 14,004</u>	<u>13,680</u>	<u>\$ 41,427</u>	<u>41,849</u>

*The Company has initially applied IFRS 15 using the cumulative effect method. Under this method, the comparative information is not restated.

6. Current Assets

Details of selected current asset balances are as follows:

(a) Cash and cash equivalents

The Company's cash and cash equivalents are comprised of bank balances at major Canadian financial institutions.

(b) Accounts receivable

The Company's accounts receivable is comprised of the following:

TERAGO INC.
Notes to the Consolidated Financial Statements
(In thousands, except for per share amounts)
(unaudited)

	September 30	December 31
	2018	2017
Trade receivables	\$ 3,701	\$ 3,137
Loss allowances (Note 13(b))	(49)	(21)
Other	199	273
	\$ 3,851	\$ 3,389

7. Network Assets, Property and Equipment

Cost	Network Assets	Cloud & Datacentre Infrastructure	Computer Equipment	Office Furniture and Equipment	Leasehold Improvements	Vehicles	Total
Balance, January 1, 2018	\$ 117,170	\$ 14,578	\$ 2,770	\$ 2,357	\$ 2,330	\$ 49	\$ 139,254
Additions / reclassifications	5,079	343	4	1	797	-	6,224
Disposals / Adjustments	(1,773)	(370)	361	-	(1)	-	(1,783)
Impairment	(1,019)	-	-	-	-	-	(1,019)
Balance, September 30, 2018	\$ 119,457	\$ 14,551	\$ 3,135	\$ 2,358	\$ 3,126	\$ 49	\$ 142,676
Accumulated Depreciation							
Balance, January 1, 2018	\$ 90,454	\$ 3,902	\$ 2,542	\$ 2,222	\$ 1,263	\$ 49	\$ 100,432
Depreciation for the period	5,452	658	686	37	319	-	7,152
Disposals / Adjustments	(1,421)	462	(465)	-	1	-	(1,423)
Impairment	(588)	-	-	-	-	-	(588)
Balance, September 30, 2018	\$ 93,897	\$ 5,022	\$ 2,763	\$ 2,259	\$ 1,583	\$ 49	\$ 105,573
Net Book Value, September 30, 2018	\$ 25,560	\$ 9,529	\$ 372	\$ 99	\$ 1,543	\$ -	\$ 37,103

During the three and nine months ended September 30, 2018 the Company wrote off assets with net book value \$104 (Cost of \$331 less accumulated depreciation of \$227) and \$360 (Cost of \$1,783 less accumulated depreciation of \$1,423) respectively, to reflect inventory adjustments and disposals (2017 – (\$1) and \$94, respectively). The corresponding loss on disposal was included in other operating expenses.

Impairment

As result of the loss of certain customers and customer locations in primarily connectivity offerings during the three months and nine months ended September 30, 2018, the Company determined that certain network assets were not recoverable. The assets were subsequently written down to their recoverable amount and an impairment charge of \$64 (Cost of \$153 less accumulated depreciation of \$89) and \$431 (Cost of \$1,019 less accumulated depreciation of \$588) respectively, was recorded in other operating expenses on the statement of comprehensive loss (2017 - \$nil and \$nil, respectively).

TERAGO INC.
Notes to the Consolidated Financial Statements
(In thousands, except for per share amounts)
(unaudited)

8. Intangible Assets and Goodwill

Cost	Radio spectrum licenses	Computer Software	Customer relationships	Other	Total Intangibles	Goodwill	Total Intangibles and Goodwill
Balance, January 1, 2018	\$ 7,041	\$ 9,803	\$ 17,690	\$ 4,831	\$ 39,365	\$ 19,419	\$ 58,784
Additions	-	112	-	-	112	-	112
Balance, September 30, 2018	\$ 7,041	\$ 9,915	\$ 17,690	\$ 4,831	\$ 39,477	\$ 19,419	\$ 58,896
Accumulated Depreciation							
Balance, January 1, 2018	\$ 2,371	\$ 8,584	\$ 9,177	\$ 2,534	\$ 22,666	\$ -	\$ 22,666
Amortization for the period	-	494	1,124	257	1,875	-	1,875
Balance September 30, 2018	\$ 2,371	\$ 9,078	\$ 10,301	\$ 2,791	\$ 24,541	\$ -	\$ 24,541
Net Book Value, September 30, 2018	\$ 4,670	\$ 837	\$ 7,389	\$ 2,040	\$ 14,936	\$ 19,419	\$ 34,355

On September 18, 2018, TeraGo entered into a share purchase agreement to acquire all of the issued and outstanding shares of Mobilexchange Spectrum Inc. and its parent holding company Mobilexchange Spectrum Holdings Inc. (collectively, "MSI") for aggregate cash consideration of \$5,700. The acquisition is being funded through the net proceeds of TeraGo's bought deal equity offering which previously closed on June 18, 2018. On November 1, 2018, TeraGo received a letter from ISD setting out its approval for the deemed transfer of the six 24 GHz spectrum licences currently held by MSI, pursuant to an application that was filed in connection with the acquisition. Closing of the acquisition is expected to occur in November, 2018, subject to customary closing conditions and as a result, has not yet been reflected in the Company's financial statements.

9. Long-term Debt

	September 30 2018	December 31 2017
Term debt facility	\$ 33,586	\$ 36,611
less: financing fees	(336)	(428)
	33,250	36,183
less: current portion	(4,000)	(4,000)
	\$ 29,250	\$ 32,183

Term Debt Facility

In June 2014, the Company entered into an agreement with a syndicate led by the National Bank of Canada ("NBC") to provide a \$50,000 credit facility that is principally secured by a general security agreement over the Company's assets.

In March 2015, the Company entered into an amended agreement with the syndicate led by NBC that increased the credit facility by \$35,000 (\$30,000 increase to the term debt facility and \$5,000 increase to the revolving facility) and extended the term from June 6, 2017 to September 30, 2018. Other terms were substantially consistent with the existing credit facilities.

In June 2017, the Company entered into a second amended agreement with the syndicate led by NBC that reduced the term debt facility from \$50,000 to \$40,000 (as a result of principal previously repaid), reduced the quarterly principal installment from \$1,250 to \$1,000 and extended the term from September 30, 2018 to June 14, 2021. Other terms were substantially consistent with the existing credit facilities.

The total \$75,000 facility that matures June 14, 2021 is made up of the following:

- \$10,000 revolving facility which bears interest at prime plus a margin percent. As of September 30, 2018, \$nil amount is outstanding (2017 - \$nil). Letters of credit issued under the facility totaled \$655 as of September 30, 2018 (2017 - \$655).
- \$40,000 term facility which bears interest at prime or Banker's Acceptance (at the Company's option) plus a margin percent and is repayable in quarterly principal installments of \$1,000. This facility was fully drawn upon signing the

TERAGO INC.
Notes to the Consolidated Financial Statements
(In thousands, except for per share amounts)
(unaudited)

second amended agreement.

On September 30, 2018, \$33,800 of the term facility principal balance outstanding was in a Banker's Acceptance and the remaining \$200 was at a floating rate. During 2018, the Company entered into two amended interest rate swap contracts that mature June 29, 2021. The interest rate swap contracts have not been designated as a hedge and will be marked-to-market each quarter. The fair value of the interest rate swap contracts at September 30, 2018 was a liability of \$12 (December 31, 2017 – asset of \$27) and is recorded in other long-term assets/liabilities (Note 10), with a corresponding charge (recovery) for the change in fair value recorded in finance costs. The effective interest rate on the Company's long-term debt at September 30, 2018 was 5.34% which represents the Company's interest on its Banker's Acceptance net of its interest swap contracts.

As at September 30, 2018, the Company prepaid interest in the amount of \$414 which represents the net settlement of the Banker's Acceptance and is recorded as a reduction in the carrying value of the debt.

- \$25,000 available for funding acquisitions and will bear interest at prime plus a margin percent and is repayable in quarterly principal installments of 2.5% of the aggregate amount outstanding. As of September 30, 2018, this facility remains undrawn.

Financing fees incurred as part of the Company's debt origination and modifications have been recorded as a reduction in the carrying amount of the debt and deferred and amortized using the effective interest method over the remaining term of the facility.

The NBC facility is subject to certain financial and non-financial covenants which the Company is in compliance with at September 30, 2018. Under this facility, the Company is subject to a cash flow sweep that could accelerate a certain amount of principal repayment based on a calculation outlined by the credit agreement not later than 120 days after the end of each fiscal year.

10. Other Long-Term Assets/Liabilities

(a) Other long-term assets

	September 30	December 31
	2018	2017
Interest rate swap contract (Note 9)	\$ -	\$ 27
Contract Asset	80	-
	80	27
less: current portion	(39)	(27)
	\$ 41	\$ -

(b) Other long-term liabilities

	September 30	December 31
	2018	2017
Performance based share units (Note 11(c))	\$ 63	\$ 43
Restricted share units (Note 11(b))	463	171
Interest rate swap contract (Note 9)	12	-
Lease inducement liability	218	261
	756	475
less: current portion	(174)	(56)
	\$ 582	\$ 419

TERAGO INC.
Notes to the Consolidated Financial Statements
(In thousands, except for per share amounts)
(unaudited)

11. Stock-Based Compensation

(a) Stock Options

For the three and nine months ended September 30, 2018, the Company recorded stock-based compensation related to stock options of \$22 and \$79, respectively. For the three and nine months ended September 30, 2017, the Company recorded stock-based compensation related to stock options of \$16 and \$51, respectively.

A summary of the status of the Company's stock option plan as at September 30, 2018 is presented below.

	2018	
	Number of Options	Weighted Average Exercise Price
Outstanding - January 1, 2018	588	\$5.58
Exercised	(517)	\$5.74
Forfeited / Expired	(1)	\$6.25
Outstanding - September 30, 2018	70	\$4.40
Exercisable	13	\$4.40

(b) Restricted Share Units (RSUs)

For the three and nine months ended September 30, 2018, the Company granted nil and 151 RSUs, respectively, to certain key executives. For the three and nine months ended September 30, 2017, the Company granted 28 and 180 RSUs, respectively, to certain key executives.

For the three and nine months ended September 30, 2018, the Company recorded compensation expense of \$110 and \$291, respectively, related to the RSUs granted and paid \$nil and \$nil, respectively, to the holders of RSUs that vested in the period. For the three and nine months ended September 30, 2017, the Company recorded compensation expense (recovery) of \$34 and (\$2), respectively, related to the RSUs granted and paid \$nil and \$587, respectively, to the holders of RSUs that vested in the period. As of September 30, 2018, a liability of \$463 (December 31, 2017 - \$171) related to the RSUs outstanding is included in other long-term liabilities (Note 10(b)).

The following table is a summary of the number of outstanding RSU as at:

	September 30 2018
Opening Balance, January 1, 2018	149
Granted	151
Forfeited	(18)
Vested and paid	-
Ending Balance, September 30, 2018	282

(c) Performance Based Share Units (PSUs)

For the three and nine months ended September 30, 2018, the Company recorded stock-based compensation expense (recovery) of \$7 and \$20, respectively, related to the PSUs outstanding and paid \$nil and \$nil, respectively, to the holders of the PSUs that vested in the period. For the three and nine months ended September 30, 2017, the Company recorded stock-based compensation expense (recovery) of (\$115) and (\$224), respectively, related to the PSUs outstanding and paid \$nil and \$57, respectively, to the holders of the PSUs that vested in the period. As at September 30, 2018, a liability of \$63 (December 31, 2017 - \$43) related to the PSUs granted is included in the other long-term liabilities (Note 10(b)).

The following table is a summary of the number of outstanding PSUs as at:

TERAGO INC.
Notes to the Consolidated Financial Statements
(In thousands, except for per share amounts)
(unaudited)

	September 30
	2018
Opening Balance, January 1, 2018	19
Granted	-
Vested and paid	-
Forfeited / Expired	-
Ending Balance, September 30, 2018	19

(d) Stock-Based Compensation Summary

The following table is a summary of the stock-based compensation expense (recovery):

	Three months ended		September 30		Nine months ended		September 30	
	2018		2017		2018		2017	
Restricted share units	\$	110		34	\$	291		(2)
Performance-based share units		7		(115)		20		(224)
Stock options		22		16		79		51
Directors' fees paid in shares		111		73		294		220
	\$	<u>250</u>		<u>8</u>	\$	<u>684</u>		<u>45</u>

12. Loss Per Share

The following table sets forth the calculation of basic and diluted loss per share.

	Three months ended		September 30		Nine months ended		September 30	
	2018		2017		2018		2017	
Numerator for basic and diluted loss per share:								
Net loss for the period	\$	(47)		(1,047)	\$	(2,848)		(3,233)
Denominator for basic and diluted loss per share:								
Basic weighted average number of shares outstanding		15,736		14,334		14,910		14,292
Effect of stock options, RSUs and PSUs		-		-		-		-
Diluted weighted average number of shares outstanding		<u>15,736</u>		<u>14,334</u>		<u>14,910</u>		<u>14,292</u>
Loss per share:								
Basic	\$	(0.00)		(0.07)	\$	(0.19)		(0.23)
Diluted	\$	(0.00)		(0.07)	\$	(0.19)		(0.23)

Due to the loss for the three and nine months ended September 30, 2018, the impact of all the options, RSUs, and PSUs totaling 380 and 414, respectively (2017 – 813 and 891), were excluded in the calculation of diluted loss per share because they were antidilutive.

TERAGO INC.
Notes to the Consolidated Financial Statements
(In thousands, except for per share amounts)
(unaudited)

13. Fair value of financial instruments

The following table outlines the carrying amounts and fair value of its financial assets and financial liabilities including their level in the fair value hierarchy. Cash and cash equivalents, accounts receivable, accounts payable, and accrued liabilities are not shown below as the carrying value of these financial instruments approximates their fair value due to their short-term maturities.

a) Classification and fair values

	Carrying Amount		Fair Value (Level 2)	
	September 30 2018	December 31 2017	September 30 2018	December 31 2017
Financial Assets				
Interest rate swap contract	\$ -	\$ 27	\$ -	\$ 27
Financial Liabilities				
Interest rate swap contract	\$ 12	\$ -	\$ 12	\$ -
Long-term debt	33,250	36,183	33,250	36,183

b) Credit risk

During the nine months ended September 30, 2018, the movement in the credit loss allowance in respect of trade receivables was as follows:

	September 30 2018
Opening Balance, January 1, 2018	21
Amounts written off	(21)
Remeasurement of loss allowance	49
Ending Balance, September 30, 2018	49

14. Equity Offering

On June 18, 2018, the Company completed an equity offering to issue and sell 1,303 common shares for gross proceeds of \$6,906 (the "Offering"). Proceeds net of commissions, legal, accounting and listing fees was \$6,067. The Offering was carried out pursuant to an underwriting agreement dated June 4, 2018 with a syndicate of underwriters led by TD Securities Inc., and included Cormark Securities Inc. and Desjardins Securities Inc.