



**VICTORY NICKEL INC.**

**CONSOLIDATED FINANCIAL STATEMENTS**

**FOR THE YEARS ENDED  
DECEMBER 31, 2017 AND 2016**

**DATED APRIL 16, 2018**

## **MANAGEMENT'S RESPONSIBILITY FOR CONSOLIDATED FINANCIAL STATEMENTS**

All of the information in the accompanying consolidated financial statements of Victory Nickel Inc. is the responsibility of management. The consolidated financial statements have been prepared by management in accordance with Canadian generally accepted accounting principles for public companies, being international financial reporting standards. Where necessary, management has made judgements and estimates in preparing the consolidated financial statements and such statements have been prepared within acceptable limits of materiality.

Management maintains appropriate systems of internal control to give reasonable assurance that its assets are safeguarded, and the financial records are properly maintained.

The Board of Directors is responsible for ensuring that management fulfils its responsibilities for financial reporting and internal control and exercises this responsibility principally through the Audit Committee. The Audit Committee, which is comprised of Directors, none of whom are employees or officers of the Company, meets with management and the external auditors to review the independent auditor's report and the consolidated financial statements to satisfy itself that management is properly discharging its responsibilities to the Directors, who approve the consolidated financial statements.

A firm of independent Chartered Professional Accountants, appointed by the shareholders, audits the consolidated financial statements in accordance with Canadian generally accepted auditing standards and provides an independent professional opinion thereon. The external auditors have free and full access to the Audit Committee with respect to their findings regarding the fairness of financial reporting and the adequacy of internal controls.

René R. Galipeau  
Vice-Chairman and CEO  
April 16, 2018

Margaret Lai  
Chief Financial Officer  
April 16, 2018

**INDEPENDENT AUDITOR'S REPORT  
TO THE SHAREHOLDERS OF VICTORY NICKEL INC.**

We have audited the accompanying consolidated financial statements of Victory Nickel Inc. which comprise the consolidated balance sheets as at December 31, 2017 and December 31, 2016 and the consolidated statements of operations, comprehensive loss, shareholders' equity and cash flows for the years ended December 31, 2017 and December 31, 2016 and a summary of significant accounting policies and other explanatory information.

**Management's Responsibility for the Consolidated Financial Statements**

Management is responsible for the preparation and fair presentation of these consolidated financial statements in accordance with International Financial Reporting Standards and for such internal control as management determines is necessary to enable the preparation of consolidated financial statements that are free from material misstatement, whether due to fraud or error.

**Auditor's Responsibility**

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on the auditor's judgement, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements.

We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.

**Opinion**

In our opinion, the consolidated financial statements present fairly, in all material respects, the financial position of Victory Nickel Inc. as at December 31, 2017 and December 31, 2016 and its financial performance and its cash flows for the years ended December 31, 2017 and December 31, 2016 in accordance with International Financial Reporting Standards.

**Emphasis of Matter**

Without qualifying our opinion, we draw attention to Note 1 in the consolidated financial statements which indicates that at year-end certain loans and borrowing were in default and significant liquidity issues the Company is facing. In addition, none of the Company's mining projects have commenced commercial production and, accordingly, the Company is dependent upon debt or equity financings, and the optioning and/or sale of resource or resource-related assets and/or the ability to generate sufficient cash flow from its other operating activities for its funding. These conditions, along with other matters as set forth in Note 1, indicate the existence of a material uncertainty that cast significant doubt about the Company's ability to continue as a going concern.

*Flabbi & Associates LLP*

Chartered Professional Accountants, Licensed Public Accountants  
Toronto, Ontario  
April 16, 2018

## Consolidated Balance Sheets

(in thousands of United States dollars)

| As at December 31,                                | Notes | 2017             | 2016             |
|---|-------|------------------|------------------|
| <b>ASSETS</b>                                     |       |                  |                  |
| <b>Current assets</b>                             |       |                  |                  |
| Cash and cash equivalents                         |       | \$ 125           | \$ 197           |
| Receivables and prepaids                          | 6     | 88               | 78               |
| Marketable securities                             | 7     | 255              | 158              |
| Inventory   | 8     | 1,851            | 2,223            |
| <b>Total current assets</b>                       |       | <b>2,319</b>     | <b>2,656</b>     |
| <b>Non-current assets</b>                         |       |                  |                  |
| Property, plant and equipment                     | 10    | 3,057            | 3,567            |
| Mine property and development project             | 11    | 34,996           | 34,974           |
| Exploration and evaluation projects               | 12    | 8,718            | 8,718            |
| <b>Total non-current assets</b>                   |       | <b>46,771</b>    | <b>47,259</b>    |
| <b>Total Assets</b>                               |       | <b>\$ 49,090</b> | <b>\$ 49,915</b> |
| <b>LIABILITIES AND SHAREHOLDERS' EQUITY</b>       |       |                  |                  |
| <b>Current liabilities</b>                        |       |                  |                  |
| Trade and other payables                          | 13    | \$ 2,225         | \$ 2,141         |
| Loans and borrowings                              | 14    | 6,500            | 6,073            |
| <b>Total current liabilities</b>                  |       | <b>8,725</b>     | <b>8,214</b>     |
| <b>Non-current liabilities</b>                    |       |                  |                  |
| Loans and borrowings                              | 14    | 7,286            | 5,871            |
| Participating Interest                            | 15    | 529              | 933              |
| Lease obligations                                 | 16    | -                | 5                |
| Deferred tax liability                            | 17    | 911              | 3,809            |
| <b>Total non-current liabilities</b>              |       | <b>8,726</b>     | <b>10,618</b>    |
| <b>Total Liabilities</b>                          |       | <b>17,451</b>    | <b>18,832</b>    |
| <b>Shareholders' equity</b>                       |       |                  |                  |
| Share capital                                     | 18    | 53,323           | 53,241           |
| Contributed surplus                               |       | 6,140            | 5,696            |
| Accumulated other comprehensive loss              |       | (3,777)          | (3,855)          |
| Deficit   |       | (24,047)         | (23,999)         |
| <b>Total shareholders' equity</b>                 |       | <b>31,639</b>    | <b>31,083</b>    |
| <b>Total Liabilities and Shareholders' Equity</b> |       | <b>\$ 49,090</b> | <b>\$ 49,915</b> |

### NATURE OF OPERATIONS AND GOING CONCERN (Note 1)

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

Approved by the Board of Directors

(signed)  
**Cynthia P. Thomas**  
 Director

(signed)  
**René R. Galipeau**  
 Director

## Consolidated Statements of Operations

(in thousands of United States dollars, except per share amounts)

| Years ended December 31,                       | Notes | 2017           | 2016              |
|--|-------|----------------|-------------------|
| Sales  |       | \$ 879         | \$ 100            |
| Cost of goods sold                             | 8     | (690)          | (644)             |
| <b>Gross margin</b>                            |       | <b>189</b>     | <b>(544)</b>      |
| <b>Operating expenses</b>                      |       |                |                   |
| General and administrative                     |       | (591)          | (851)             |
| Share based payments                           | 20    | (444)          | -                 |
| Amortization of property, plant and equipment  | 10    | (590)          | (611)             |
| Writedown of Exploration & Evaluation projects | 12    | -              | (4,700)           |
| <b>Operating loss</b>                          |       | <b>(1,436)</b> | <b>(6,706)</b>    |
| Finance income                                 | 21    | 488            | 3,783             |
| Finance costs                                  | 21    | (1,998)        | (1,891)           |
| <b>Net finance (costs) income</b>              |       | <b>(1,510)</b> | <b>1,892</b>      |
| <b>Loss before income taxes</b>                |       | <b>(2,946)</b> | <b>(4,814)</b>    |
| Income tax recovery (expense)                  | 22    | 2,898          | (3,813)           |
| <b>Net loss for the period</b>                 |       | <b>\$ (48)</b> | <b>\$ (8,627)</b> |
| <b>Loss per share</b>                          | 19    |                |                   |
| Basic and diluted loss per share               |       | \$ (0.00)      | \$ (0.10)         |

## Consolidated Statements of Comprehensive Loss

(in thousands of United States dollars)

| Years ended December 31,                                | 2017           | 2016              |
|---|----------------|-------------------|
| <b>Net loss for the period</b>                          | <b>\$ (48)</b> | <b>\$ (8,627)</b> |
| <b>Other comprehensive income (loss) ("OCI")</b>        |                |                   |
| Net change in fair value of financial assets            | 7              | 143               |
| Income tax loss   | -              | 4                 |
| Foreign exchange loss                                   | (65)           | (76)              |
| <b>Other comprehensive income for the period</b>        | <b>78</b>      | <b>275</b>        |
| <b>Total Comprehensive Income (Loss) for the period</b> | <b>\$ 30</b>   | <b>\$ (8,352)</b> |

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

## Consolidated Statements of Shareholders' Equity

| (in thousands of United States dollars)                      |              | Share<br>Capital | Contributed<br>Surplus | Accumulated<br>Other<br>Comprehensive<br>(Loss) Income | Deficit     | Total Equity |
|--|--------------|------------------|------------------------|--|-------------|--------------|
| <b>Balances as at January 1, 2016</b>                        | <i>Notes</i> | \$ 52,570        | \$ 5,696               | \$ (4,130)   | \$ (15,372) | \$ 38,764    |
| <b>Total comprehensive loss for the period</b>               |              |                  |                        |  |             |              |
| Net loss for the period                                      |              |                  |                        |  | (8,627)     | (8,627)      |
| <b>Other comprehensive income (loss)</b>                     |              |                  |                        |  |             |              |
| Net change in fair value of financial assets                 |              |                  |                        | 347  |             | 347          |
| Income tax loss  |              |                  |                        | 4  |             | 4            |
| Foreign exchange on change in functional currency            |              |                  |                        | (76)   |             | (76)         |
| <b>Total other comprehensive income</b>                      |              |                  |                        | 275  |             | 275          |
| <b>Total comprehensive loss for the period</b>               |              |                  |                        |  |             | (8,352)      |
| <b>Transactions with owners, recorded directly in equity</b> |              |                  |                        |  |             |              |
| <b>Contributions in the period</b>                           |              |                  |                        |  |             |              |
| Issuance of shares on settlement of debt                     | 18           | 671              |                        |  |             | 671          |
| <b>Total contributions by owners</b>                         |              | 671              |                        |  |             | 671          |
| <b>Total transactions with owners</b>                        |              | 671              |                        |  |             | 671          |
| <b>Balances as at December 31, 2016</b>                      |              | \$ 53,241        | \$ 5,696               | \$ (3,855)   | \$ (23,999) | \$ 31,083    |
| <b>Total comprehensive loss for the period</b>               |              |                  |                        |  |             |              |
| Net Loss for the period                                      |              |                  |                        |  | (48)        | (48)         |
| <b>Other comprehensive income (loss)</b>                     |              |                  |                        |  |             |              |
| Net change in fair value of financial assets                 | 7            |                  |                        | 143  |             | 143          |
| Foreign exchange on change in functional currency            |              |                  |                        | (65)   |             | (65)         |
| <b>Total other comprehensive income</b>                      |              |                  |                        | 78   |             | 78           |
| <b>Total comprehensive income for the period</b>             |              |                  |                        |  |             | 30           |
| <b>Transactions with owners, recorded directly in equity</b> |              |                  |                        |  |             |              |
| <b>Contributions in the period</b>                           |              |                  |                        |  |             |              |
| Issuance of common shares for loan fee                       | 18           | 82               |                        |  |             | 82           |
| Options granted and vesting                                  | 20           |                  | 444                    |  |             | 444          |
| <b>Total contributions</b>                                   |              | 82               | 444                    |  |             | 526          |
| <b>Total transactions with owners</b>                        |              | 82               | 444                    |  |             | 526          |
| <b>Balances as at December 31, 2017</b>                      |              | \$ 53,323        | \$ 6,140               | \$ (3,777)   | \$ (24,047) | \$ 31,639    |

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

## Consolidated Statements of Cash Flows

(in thousands of United States dollars)

| Years ended December 31,                                     | Notes | 2017          | 2016          |
|--|-------|---------------|---------------|
| <b>Cash flows from operating activities</b>                  |       |               |               |
| Net loss for the period                                      |       | \$ (48)       | \$ (8,627)    |
| Adjustments for:   |       |               |               |
| Share based payments   | 20    | 444           | -             |
| Amortization of property, plant and equipment                | 10    | 590           | 611           |
| (Write-up impairment) provision for inventory                | 8     | (307)         | 517           |
| Writedown of exploration and evaluation project              | 12    | -             | 4,700         |
| Net finance costs (income)                                   | 21    | 1,444         | (1,498)       |
| Income tax (recovery) loss                                   | 22    | (2,898)       | 3,813         |
| Net change in working capital:                               |       |               |               |
| Change in receivables and prepaids                           | 6     | (10)          | 228           |
| Change in inventory  | 8     | 679           | 134           |
| Change in trade and other payables                           | 13    | 289           | (189)         |
| <b>Net cash provided (used) by operating activities</b>      |       | <b>183</b>    | <b>(311)</b>  |
| <b>Cash flows from investing activities</b>                  |       |               |               |
| Expenditures on mine property and development project        | 11    | (22)          | (22)          |
| Expenditures on exploration and evaluation projects          | 12    | -             | (9)           |
| Proceeds on sale of partnership                              |       | -             | 283           |
| Purchase of property, plant and equipment                    | 10    | (77)          | -             |
| Proceeds on sale of marketable securities                    | 7     | 46            | 404           |
| <b>Net cash (used) provided by from investing activities</b> |       | <b>(53)</b>   | <b>656</b>    |
| <b>Cash flows from financing activities</b>                  |       |               |               |
| Payments of interest   | 14    | (22)          | (38)          |
| Receipt of other current loan                                | 14    | 65            | -             |
| Issuance of current promissory note                          | 6     | (55)          | -             |
| Payments under leases  | 16    | (125)         | (146)         |
| Deposits of restricted cash received                         |       | -             | 36            |
| <b>Net cash used by financing activities</b>                 |       | <b>(137)</b>  | <b>(148)</b>  |
| <b>Net decrease in cash and cash equivalents</b>             |       | <b>(7)</b>    | <b>197</b>    |
| Foreign exchange effect on cash and cash equivalents         |       | (65)          | (85)          |
| <b>Cash and cash equivalents, beginning of the period</b>    |       | <b>197</b>    | <b>85</b>     |
| <b>Cash and cash equivalents, end of the period</b>          |       | <b>\$ 125</b> | <b>\$ 197</b> |

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

# Notes to the Consolidated Financial Statements

*(all tabular amounts in thousands of United States dollars, except common share and per share information)*

## 1. NATURE OF OPERATIONS AND GOING CONCERN

### Nature of Operations

Victory Nickel Inc. (“Victory Nickel” or the “Company”) is a company domiciled in Canada. The address of the Company’s registered office is 80 Richmond St. West, Suite 1802, Toronto, Ontario, M5H 2A4. The consolidated financial statements as at and for the years ended December 31, 2017 and 2016 comprise of the Company and its subsidiaries Victory Silica Ltd. (“Victory Silica”) and BG Solutions Ltd. (“BG”) together referred to as “Victory Nickel” and individually as “Victory Nickel entities”. Victory Nickel was primarily engaged in the acquisition, exploration and development of nickel properties and associated products in Canada until the second quarter of 2014 when the Company became a producer and supplier of premium frac sand from its frac sand plant (the “7P Plant”), located near the town of Seven Persons, approximately 18 kilometres southwest of Medicine Hat, Alberta. The 7P Plant comprises a fully-operational wet plant with a nominal capacity of approximately 120,000 tons per annum (“tpa”) and a dry plant with a nominal capacity of 500,000 tpa. Frac sand is specialized sand that is used as a proppant to enhance recovery from oil and gas wells. The Company was formed on February 1, 2007 pursuant to a plan of arrangement.

On February 22, 2016 the Company commenced trading its common shares on the Canadian Securities Exchange (“CSE”) under the symbol NI. Previously, the Company was listed on the Toronto Stock Exchange (“TSX”) under the symbol NI.

All dollar amounts are quoted in United States dollars (“US\$” or “US dollars”), except for those denoted as Canadian dollars (“CAD\$”) or Australian dollars (“AU\$”).

### Going Concern

These 2017 audited consolidated financial statements have been prepared using Generally Accepted Accounting Principles (“GAAP”) 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. As at December 31, 2017, the Company had a working capital deficiency of \$6,406,000, calculated as current assets less current liabilities, an increase from a working capital deficiency of \$5,558,000 as at December 31, 2016. At December 31, 2017, the debts of \$6,500,000 were the largest factor in the Company’s working capital deficiency, as the Company was in default on all unsecured debt and related interest.

The Company’s main assets are its nickel projects. Minago, the most advanced of its projects is permitted and ready for development. However, development costs are in excess of \$500,000,000 and given the current price of nickel, it is unlikely that financing for this project will be available in the near future. If the Company is unable to finance and develop these projects, the potential recovery via sale of these projects may be below the current carrying amounts. Given the defaults on various loans discussed below, there is an increased risk that the Company’s creditors could force the Company to liquidate its core assets under less than favourable terms.

On April 14, 2015, the Company announced that operations at the 7P Plant were temporarily suspended until the demand for frac sand improved; this temporary suspension was due to the dramatic decrease in energy pricing that began in 2014. Since March 2015, sales have been significantly below rates achieved during 2014 and continue well below the level required to generate positive cash flow. The 7P Plant was restarted in March 2017 and continues to operate on an as-needed basis in order to fulfil customer needs. In October 2017, the Company announced that it had completed the refurbishment of its frac sand wash plant at the 7P Plant. The wash plant is now operational, enhancing the ability to produce and sell frac sand. 2017 has shown some improvement in the slowdown in drilling activity due to the severe drop in the price of oil, but sales have yet to recover to levels that would generate positive cash flow.

The near-term outlook in the frac sand market remains unclear. The US dollar continues to impact demand for high-quality Wisconsin frac sand in Canada, as the price for domestic frac sand has dropped and service companies appear satisfied with using lower-quality domestic frac sand, because of the price differential caused mainly by the exchange rate. As the Company’s inventory is Wisconsin frac sand, this will continue to stress the Company’s liquidity until such time as the market demand recovers and operations can resume on a consistent basis.

Cash flows from frac sand sales in 2017 were sufficient to cover operating costs but not sufficient to pay financing costs and the Company was not able to make the majority of its interest payments due during 2017 and 2016.



## Notes to the Consolidated Financial Statements

*(all tabular amounts in thousands of United States dollars, except common share and per share information)*

In March 2016, the Company announced that it had completed the restructuring of the SPA Amended Loan (as defined and outlined in Note 14), which included terms of a debt restructuring package (the "Debt Restructuring Agreement") for the holders of the promissory convertible notes (the "Promissory Convertible Notes") and the Company's trade creditors. The SPA Amended Loan was increased to \$5,500,000 and the maturity date extended to January 31, 2018 (the "Senior Secured Debt"). On December 31, 2017, the Senior Secured Debt was increased by the amount of the unpaid interest to \$7,050,000 and the maturity date was extended to July 31, 2019.

Pursuant to the terms of the Senior Secured Debt, the Company is prevented from making payments under outstanding unsecured debt until the Senior Secured Debt is repaid. Only a portion of the interest due under the Senior Secured Debt during 2017 and 2016 was paid. The lender of the Senior Secured Debt (the "Secured Lender") provided a forbearance agreement for the balance of the accrued interest and made short term advances to cover non-discretionary costs. An advance on December 28, 2017 is included on other current loans, while advances in 2016 were paid during 2016. Barring a significant improvement in the sales of frac sand, the Company is unlikely to be able to repay the Senior Secured Debt in full when it matures in July 2019. The Company's ability to make the required interest payments in 2018 is also in doubt and dependent upon frac sand sales. To date, the Company's Secured Lender has communicated its commitment to ensuring the protection of the Company's core assets, including the advances noted above and the forbearance agreement. Should the support of the Secured Lender change, the going concern assumption would be in doubt.

All of the Promissory Convertible Note holders participated in the Debt Restructuring Agreement, except for one holder of a \$3,000,000 Promissory Convertible Note (the "Outstanding Note"). In March 2016, the Company announced that it had received notice that the holder of the Outstanding Note had filed a statement of claim concerning non-payment of principal and interest. The Company has reviewed the statement of claim with legal counsel to assess its impact on the Company and has concluded that there is no significant impact on the status of the Company's debt. The Outstanding Note matured in July 2016 and the Company has been unable to repay the amounts owing and interest payments due, which has resulted in the Company defaulting on the note.

On March 7, 2016, March 31, 2016 and June 7, 2016, the Company announced that it had completed private placements with certain of its unsecured lenders, trade creditors and management in settlement of the Promissory Convertible Notes and debt owed, as per the terms of the Debt Restructuring Agreement, as described in Note 14. The Company has not paid interest payments due on its New Promissory Convertible Notes as described in Note 14, which has resulted in the Company defaulting on its New Promissory Convertible Notes.

In March 2016, the Company entered into a general partnership agreement (the "Partnership") for the purpose of carrying on a trading and investment business. The Partnership entered into various forward foreign exchange contracts and in June 2016, the Company sold its interest in the Partnership for net proceeds of CAD\$358,000. The net proceeds were used to fund working capital requirements.

In October 2016, the Company sold a portion of its marketable securities for net proceeds of AU\$515,000. To the extent required, the Company will continue to sell non-core assets to fund its working capital requirements.

The ability of the Company to continue as a going concern is heavily dependent on the continued support of its lenders and the frac sand market improving, both in demand and in price, and the Company's ability to resume full operations at its 7P Plant. In addition to the liquidity and solvency uncertainties described above, the ability to resume full operations at the 7P Plant will require additional financing. In order to resume purchasing and shipping supplies of frac sand and full operations at the 7P Plant, the Company will require additional working capital. As noted, the Company's Secured Lender has been supportive to date. However, there are no assurances that the Company will be able to obtain the working capital to resume operations at the level sufficient to generate cash flows to repay its outstanding obligations.

The Company has cut non-essential costs in an effort to reduce operating losses and has deferred payments wherever possible. During 2017 and 2016, the Company, with the agreement of its Secured Lender, sold non-core assets, including marketable securities and its interest in the Partnership, to provide operating funds. However, without an injection of capital and/or until the demand for frac sand returns to pre-2015 levels, the Company will not be able to meet its outstanding obligations or any new obligations as they become due. The defaults on the Company's existing obligations add to the challenge of obtaining additional capital.

# Notes to the Consolidated Financial Statements

*(all tabular amounts in thousands of United States dollars, except common share and per share information)*

There can be no assurance that the Company will be able to restructure its debt further and/or recapitalize, and there is no certainty as to what further steps, if any, the secured and unsecured lenders may take. To date, the Secured Lender has been supportive and has provided limited working capital needed to protect the Company's core assets, and management and the board of directors have reduced and/or deferred salaries and director fees until business recovers, but there is no certainty that this will continue. Management salary reductions and/or deferrals put the Company at risk of being unable to retain key personnel.

In addition to the above liquidity issues, the Company is subject to the risks and challenges experienced by other companies at a comparable stage. These risks include, but are not limited to, continuing losses, dependence on key individuals and the ability to secure adequate financing or to complete corporate transactions to meet the minimum capital required to successfully fund its projects and operating expenses.

None of the Company's mining projects have commenced commercial production and, accordingly, the Company is dependent upon debt or equity financings, the optioning and/or sale of resource or resource-related assets or interests, exploration results which have the potential for the discovery of economically-recoverable reserves and resources, and/or the ability to generate sufficient cash flow from its other operating activities for its funding. Development of the Company's current nickel mining projects to the production stage will require significant financing. Given the current economic climate, including the low nickel price, and the Company's existing liquidity challenges, the ability to raise sufficient funds will be difficult.

Should the Company not be able to overcome the risks described in this section, the carrying value of the Company's assets would be subject to material adjustment and, in addition, other adjustments may be necessary to these consolidated financial statements should such adverse events impair the Company's ability to continue as a going concern as contemplated under GAAP. There is no certainty that the Company will be able to generate sufficient cash to fund its activities including debt servicing, project expenditures and corporate costs. These conditions indicate the existence of a material uncertainty that may cast significant doubt about the Company's ability to continue as a going concern. Failure to continue as a going concern would require that the Company's assets and liabilities be restated on a liquidation basis, which would differ significantly from the going concern basis.

## **2. BASIS OF PREPARATION**

### **(a) Statement of Compliance**

The consolidated financial statements have been prepared using accounting policies consistent with International Financial Reporting Standards ("IFRS") and its interpretations adopted by the International Accounting Standards Board ("IASB"). The accounting policies, methods of computation and presentation applied in these consolidated financial statements are consistent with those of the previous fiscal year.

The management of the Company prepares the consolidated financial statements, which are then reviewed by the Audit Committee and the Board of Directors. The consolidated financial statements were authorized for issue by the Board of Directors on April 16, 2018 and are made available to shareholders and others through filing on SEDAR shortly thereafter.

### **(b) Basis of Measurement**

The consolidated financial statements have been prepared on the historic cost basis except for derivative financial instruments, such as warrants and the Participating Interest (as described in Note 15), which are measured at fair value with changes through operations and financial assets, such as marketable securities, which are measured at fair value with changes through other comprehensive income or loss ("OCI").

### **(c) Functional and Presentation Currency**

Under IFRS, an entity's functional currency should reflect the underlying transactions, events and conditions relevant to the entity. Revenues and significant expenses of the Company's operating entity are driven by prices in US Dollars, which influence managements' primary operating, capital and financing decisions.

These financial statements are presented in US dollars, which is the Company's functional currency. All financial information is expressed in US dollars unless otherwise stated; tabular amounts are stated in thousands of dollars.

### **(d) Comparative Figures**

Comparative figures have been reclassified to conform with presentation used in the current year.

# Notes to the Consolidated Financial Statements

(all tabular amounts in thousands of United States dollars, except common share and per share information)

## **(e) Use of Estimates and Judgements**

The preparation of financial statements in conformity with IFRS requires management to make estimates, judgements and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Actual results may differ from these estimates.

It is reasonably possible that, on the basis of existing knowledge, outcomes in the next financial year that are different from the assumptions used could require a material adjustment to the carrying amount of the asset or liability affected.

The accompanying consolidated financial statements include all adjustments that are, in the opinion of management, necessary for fair presentation.

### **Significant estimates and assumptions**

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected.

Information regarding significant areas of estimation uncertainty made in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements is included in the following notes:

- Note 8 – valuation of inventory;
- Note 11 – measurement of the recoverable amount of mine property and development project;
- Note 12 – measurement of the recoverable amount of exploration and evaluation projects;
- Note 14 – measurement and valuation of the embedded derivatives in promissory convertible notes;
- Note 14 – measurement and the valuation of the fair value of debt issued in the restructuring;
- Note 14 – measurement and valuation of the current portion of the Senior Secured Debt under the cash sweep terms;
- Note 15 – measurement and valuation of the Participating Interest; and
- Note 20 – measurement of share-based payments.

### **Significant judgements**

Judgements are reviewed on an ongoing basis. Changes resulting from the effects of amended judgements are recognized in the period in which the circumstance giving rise to the change occurs and in any future periods presented. Information regarding significant areas of critical judgements made in applying accounting policies that have the most significant effect on the amounts recognized in the consolidated financial statements is included in the following notes:

- Note 1 – going concern assessment;
- Note 2 – determination of the functional currency for the Company and its subsidiaries;
- Note 8 – impairment of inventory;
- Note 11 – classification of expenditures as mine property and development project or operating expenses;
- Note 12 – classification of expenditures as exploration and evaluation projects or operating expenses;
- Note 11 – impairment of mine property and development project;
- Note 12 – impairment of exploration and evaluation projects; and
- Note 17 – recoverability of deferred tax assets.

## **3. SIGNIFICANT ACCOUNTING POLICIES**

The accounting policies of the Company are set out in detail below. Such policies have been applied consistently by all Victory Nickel entities and to all periods presented in these consolidated financial statements.

### **(a) Basis of Consolidation**

#### **Subsidiary**

A subsidiary is an entity controlled by Victory Nickel. Control exists when Victory Nickel has the power to govern the financial and operating policies of an entity so as to obtain benefits from its activities. In assessing control, potential voting rights that currently are exercisable are taken into account. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases. The accounting policies of subsidiaries align with the policies adopted by Victory Nickel. Significant Company entities are listed in Note 25.

# Notes to the Consolidated Financial Statements

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## **Transactions eliminated on consolidation**

Intercompany balances and transactions, and any unrealized income and expenses arising from intercompany transactions, are eliminated in preparing the consolidated financial statements. Unrealized gains arising from transactions with equity-accounted investees are eliminated against the investment to the extent of Victory Nickel's interest in the investee. Unrealized losses are eliminated in the same way as unrealized gains, but only to the extent that there is no evidence of impairment.

## **(b) Foreign Currency**

### **Foreign currency transactions**

Transactions in foreign currencies are translated to the respective functional currency of Victory Nickel at exchange rates at the dates of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are retranslated to the functional currency at the exchange rate at that date. The foreign currency gain or loss on monetary items is the difference between amortized cost in the functional currency at the beginning of the period, adjusted for effective interest and payments during the period, and the amortized cost in foreign currency translated at the exchange rate at the end of the period. Non-monetary assets and liabilities denominated in foreign currencies that are measured at fair value are retranslated to the functional currency at the exchange rate at the date that the fair value was determined. Foreign currency differences arising on retranslation are recognized through operations, except for differences arising on the retranslation of marketable securities, which are recognized directly in OCI. Non-monetary items that are measured in terms of historic cost in a foreign currency are translated using the exchange rate at the date of the transaction.

## **(c) Financial Instruments**

### **IFRS 9 Financial Instruments**

IFRS 9 Financial Instruments ("IFRS 9"), which impacts the classification and measurement of financial assets, has been adopted by the Company.

### **(i) Non-derivative financial instruments**

Non-derivative financial instruments comprise investments in equity securities, receivables, cash and cash equivalents, restricted deposits, trade and other payables, loans and borrowings.

Non-derivative financial instruments, with the exception of financial assets at fair value through OCI, are recognized initially at fair value plus, for instruments not at fair value through operations, any directly attributable transaction costs. Subsequent to initial recognition, non-derivative financial instruments are measured as described below.

Cash and cash equivalents comprise cash balances and call deposits. Restricted deposits are funds on deposit with a Canadian chartered bank to support letters of credit, if any, being used to facilitate business activity with certain vendors.

Loans, receivables and borrowings are financial assets and liabilities with fixed or determinable payments that are not quoted in an active market. Such assets and liabilities are recognized initially at fair value plus any directly attributable transaction costs. Subsequent to initial recognition, loans, receivables and borrowings are measured at amortized cost using the effective interest method, less any impairment losses. Accounting for finance income and expenses is discussed in Note 3(n).

### *Financial assets at fair value through OCI*

Victory Nickel's investments in equity securities are measured at fair value and changes therein, as well as foreign currency differences on those investments, are recognized directly in OCI.

### *Financial instruments at amortized cost*

Other non-derivative financial instruments are measured at amortized cost using the effective interest method, less any impairment losses.

### **(ii) Derivative financial instruments**

Victory Nickel may periodically hold warrants as part of its portfolio of marketable securities, which are financial assets at fair value through operations. Convertible promissory notes contain embedded derivatives which are separated from the financial instrument measured at amortized cost.

Derivatives are recognized initially at fair value; attributable transaction costs are recognized through operations when incurred. Subsequent to initial recognition, derivatives are measured at fair value and changes therein are

## Notes to the Consolidated Financial Statements

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recognized immediately through operations. The Participating Interest is a derivative that requires adjustment to the fair value at each reporting period (refer to Note 15).

### (d) Inventory

Finished products and raw materials inventories are valued at the lower of cost and net realizable value. Cost comprises all costs of purchase, costs of processing and other costs incurred in bringing inventories to their present location and condition. Net realizable value for finished products and raw materials is generally considered to be the selling price of the finished product in the ordinary course of business less the estimated costs of completion and estimated costs to make the sale. Inventory is reviewed to ensure the carrying value does not exceed net realizable value. A write-down is recognized when carrying cost exceeds net realizable value. The write-down may be reversed if the circumstances which caused it no longer to exist.

### (e) Property, Plant and Equipment

#### (i) Recognition and measurement

Items of property, plant and equipment are measured at cost less accumulated depreciation and accumulated impairment losses. Cost includes any expenditure that is directly attributable to the acquisition of the asset.

When parts of an item of property, plant and equipment have different useful lives, they are accounted for as separate items (major components) of property and equipment. Gains and losses on disposal of an item of property and equipment are determined by comparing the proceeds from disposal with the carrying amount of property and equipment and are recognized net within *Loss on Sale of Asset* in the consolidated statement of operations.

#### (ii) Depreciation

Depreciation is calculated as a function of the depreciable amount, which is the cost of an asset less its residual value. Depreciation is recognized through operations over the estimated useful lives of each part of an item of property and equipment. Land is not depreciated. Depreciation commences when an asset is placed into service. Operations at the 7P Plant began in 2014, at which time amortization of plant equipment commenced.

The depreciation rates and methods for the current and comparative periods are as follows:

| Item                            | Method            | 2017       | 2016       |
|---------------------------------|-------------------|------------|------------|
| Building                        | Declining-balance | 5%         | 5%         |
| Plant and Equipment at 7P Plant | Straight-line     | 10% to 20% | 10% to 20% |
| Other Equipment and Furniture   | Declining-balance | 20%        | 20%        |
| Vehicles and Mobile Equipment   | Declining-balance | 30%        | 30%        |

Depreciation methods, useful lives and residual values are reviewed at each financial year end and adjusted if appropriate.

### (f) Exploration and Evaluation Projects

#### (i) Exploration and Evaluation expenditures

Exploration and Evaluation ("E&E") expenditures relate to costs incurred on the exploration for and evaluation of potential mineral reserves and includes costs related to the following: acquisition of exploration rights, conducting geological studies, exploratory drilling and sampling, and evaluating the technical feasibility and commercial viability of extracting a mineral resource.

E&E expenditures, including costs of acquiring licenses, are capitalized as E&E assets on an "area of interest basis" which generally is defined as a project. The Company considers a project to be an individual geological area whereby the presence of a mineral deposit is considered favourable or has been proven to exist and, in most cases, comprises a single mine or deposit.

E&E assets are recognized if the rights to the project are current and either:

- the expenditures are expected to be recouped through successful development and exploitation of the project, or alternatively by its sale; or
- activities on the project have not, at the reporting date, reached a stage which permits a reasonable assessment of the existence or otherwise of economically recoverable reserves and active and significant operations in, or in relation to, the project are continuing.

## Notes to the Consolidated Financial Statements

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E&E expenditures are initially capitalized as intangible E&E assets. Such E&E expenditures may include costs of licence acquisition, technical services and studies, geophysical surveys, exploration drilling and testing, materials and fuels used, rentals and payments made to contractors and consultants. To the extent that a tangible asset is consumed in developing an intangible E&E asset, the amount reflecting that consumption is recorded as part of the cost of the intangible asset.

Once the technical feasibility and commercial viability of the extraction of mineral reserves in a project are demonstrable, permitted and development is approved by the Board, E&E assets attributable to that project are first tested for impairment and then reclassified to *Mine property and development projects* on the consolidated balance sheet.

### **(ii) Pre-E&E expenditures**

Pre-E&E expenditures are incurred on activities that precede exploration for an evaluation of mineral resources, being all expenditures incurred prior to securing the legal rights to explore an area. Pre-E&E expenditures are expensed immediately as *Pre-exploration write-offs* through the consolidated statement of operations.

### **(iii) Impairment**

E&E assets are assessed for impairment when facts and circumstances suggest that the carrying amount of an E&E asset may exceed its recoverable amount and any impairment loss is recognized as *Writedown of Exploration and Evaluation projects* through the consolidated statement of operations. The following facts and circumstances, among other things, indicate that E&E assets must be tested for impairment:

- the term of exploration license for the project has expired during the reporting period or will expire in the near future, and is not expected to be renewed;
- substantive expenditure on further exploration for and evaluation of mineral resources in the project area is neither budgeted nor planned;
- exploration for and evaluation of mineral resources in the project area have not led to the discovery of commercially viable quantities of mineral resources and the Company plans to discontinue activities in the specific area; or
- sufficient data exists to indicate that while development activity is likely to proceed, the carrying amount of the E&E asset is unlikely to be recovered in full through such activity.

E&E assets are tested for impairment on an individual project (area of interest) basis. As noted above, a project would also be tested for impairment before being transferred to *Mine property and development projects* on the consolidated balance sheet.

### **(g) Mine Property and Development Project**

#### **(i) Pre-production development expenditures**

The Company considers a project to be in the development phase when an identified mineral reserve is being prepared for production as approved by the Board, for example when there is construction of access to the mineral reserves upon determination that there is economic viability of the project under a successful feasibility study and is permitted for development. As such, project development activities are related to the construction of an asset to be used in production or preparation for extraction of a specific mineral resource.

The costs of mining properties, which include the costs of acquiring and developing mining properties and mineral rights, are capitalized in the same manner as property and equipment under *Mine property and development project* ("MP&D") assets on the consolidated balance sheet in the period in which they are incurred or transferred from E&E assets upon determination of economic viability. At that point, all further pre-production primary development expenditure other than land, buildings, plant and equipment, etc. is capitalized as part of the cost of the project until the project is capable of commercial production. This includes costs incurred in preparing the site for mining operations, including pre-stripping costs.

Presently, the Company's sole project classified as an *MP&D* asset on the consolidated balance sheet is the Minago project; it continues to be in the pre-production phase and costs continue to be capitalized without depreciation.

#### **(ii) Impairment**

If a property were to be abandoned, there is little likelihood of a mineral right being exploited, or the value of the exploitable mineral right has diminished below cost, the cumulative capitalized cost relating to the property is written off to its recoverable amount through operations.

## Notes to the Consolidated Financial Statements

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### **(h) Borrowing Costs**

The Company's policy is to capitalize project-related borrowing costs related to qualifying assets as incurred. A qualifying asset is an asset that necessarily takes a substantial period of time to get ready for its intended use or sale. The Company presently does not have any project-related borrowings on qualifying assets.

### **(i) Government Grants**

Government grants that compensate Victory Nickel for expenses incurred are recognized through operations on a systematic basis in the same periods in which the expenses are recognized. Grants that compensate Victory Nickel for the cost of an asset are recognized through operations on a systematic basis over the useful life of the asset. For assets which are not being amortized, such as E&E assets or MP&D assets, the government grant is deducted from the related asset.

### **(j) Investment Tax Credits**

Investment tax credits may be claimed by the Company on qualifying expenditures. The Company accounts for these when such qualifying expenditures have been made by reducing the deferred tax liability and recording an income tax recovery through the consolidated statement of operations.

### **(k) Impairment**

#### ***(i) Financial assets***

A financial asset is assessed at each reporting date to determine whether there is any objective evidence that it is impaired. A financial asset is considered to be impaired if objective evidence indicates that one or more events have had a negative effect on the estimated future cash flows of that asset.

An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between its carrying amount and the present value of the estimated future cash flows discounted at the original effective interest rate. Individually significant financial assets are tested for impairment on an individual basis. The remaining financial assets are assessed collectively in groups that share similar credit risk characteristics.

An impairment loss is reversed if the reversal can be related objectively to an event occurring after the impairment loss was recognized. For financial assets measured at amortized cost, the reversal is recognized through operations.

#### ***(ii) Non-financial assets***

The carrying amounts of Victory Nickel's non-financial assets, other than deferred tax assets, are reviewed at each reporting date to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. For goodwill and intangible assets that have indefinite lives or that are not yet available for use, the recoverable amount is estimated each year at the same time.

The recoverable amount of an asset or cash-generating unit ("CGU") (see definition below) is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset. For the purpose of impairment testing, assets are grouped together into the smallest group of assets that generates, or has the potential to generate, cash inflows from continuing use that are largely independent of the cash inflows of other assets or groups of assets. Generally, a CGU is analogous to an individual project. The goodwill acquired in a business combination, for the purpose of impairment testing, is allocated to CGUs that are expected to benefit from the synergies of the combination.

An impairment loss is recognized if the carrying amount of an asset or a CGU exceeds its estimated recoverable amount. Impairment losses are recognized through operations. Impairment losses recognized in respect of CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the units and then to reduce the carrying amounts of the other assets in the unit (group of units) on a pro rata basis.

Impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortization, if no impairment loss had been recognized.

# Notes to the Consolidated Financial Statements

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## **(l) Employee Benefits**

### ***(i) Termination benefits***

Termination benefits are recognized as an expense when Victory Nickel is demonstrably committed, without realistic possibility of withdrawal, to a formal detailed plan to either terminate employment before the normal retirement date, or to provide termination benefits as a result of an offer made to encourage voluntary redundancy. Termination benefits for voluntary redundancies are recognized as an expense if Victory Nickel has made an offer of voluntary redundancy, it is probable that the offer will be accepted and the number of acceptances can be reliably estimated.

### ***(ii) Short-term benefits***

Short-term employee benefit obligations are measured on an undiscounted basis and are expensed as the related service is provided. A liability is recognized for the amount expected to be paid under short-term cash bonus plans if Victory Nickel has a present legal or constructive obligation to pay this amount as a result of past service provided by the employee and the obligation can be reliably estimated.

### ***(iii) Share-based payment transactions***

The grant-date fair value of options granted to employees, directors and consultants is recognized as an employee expense, with a corresponding increase in equity, over the period that the individuals become unconditionally entitled to the options. The amount recognized as an expense is adjusted to reflect the actual number of share options for which the related service and non-market vesting conditions are met.

Share-based payment arrangements in which the Company receives properties, goods or services as consideration for its own equity instruments are accounted for as equity-settled share-based payment transactions, regardless of how the equity instruments are obtained by Victory Nickel.

## **(m) Provisions**

A provision is recognized if, as a result of a past event, the Company has a present legal or constructive obligation that can be reliably estimated and it is probable that an outflow of economic benefits will be required to settle the obligation. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The unwinding of the discount is recognized as a finance cost.

In accordance with the Company's environmental policy and applicable legal requirements, a provision for site restoration or decommissioning in respect of land restoration, and the related expense, is recognized when the land is contaminated and there is a legal obligation to restore the site. The Company presently has no decommissioning liabilities.

## **(n) Finance Income and Finance Costs**

Finance income comprises interest income on funds invested (including financial assets at fair value through operations), gains on the disposal of financial assets at fair value through operations, amortization of flow-through premiums and changes in the fair value of financial assets (warrants) at fair value through operations. Interest income is recognized as it accrues through operations, using the effective interest method. Gains on the disposal of financial assets are recognized on the settlement date.

Finance costs comprise interest expense on borrowings, unwinding of the discount on provisions, changes in the fair value of financial assets and liabilities at fair value through operations and losses recognized on financial assets that are recognized through operations. All borrowing costs are recognized through operations using the effective interest method, except for those amounts capitalized as part of the cost of qualifying assets.

Foreign currency gains and losses are reported on a net basis.

## **(o) Income Taxes**

Income tax expense comprises current and deferred tax. Income tax expense is recognized through operations except to the extent that it relates to items recognized either in OCI or directly in equity, in which case it is recognized in OCI or in equity respectively.

Current tax is the expected tax payable on the taxable income for the period, using tax rates enacted or substantively enacted at the reporting date and any adjustment to tax payable in respect of previous years.

Deferred tax is recognized using the balance sheet method, providing for temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation



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purposes. Deferred tax is not recognized for the following temporary differences: the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss, and differences relating to investments in subsidiaries and jointly-controlled entities to the extent that it is probable that they will not reverse in the foreseeable future. In addition, deferred tax is not recognized for taxable temporary differences arising on the initial recognition of goodwill. Deferred tax is measured at the tax rates that are expected to be applied to temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets, and they relate to income taxes levied by the same tax authority on the same taxable entity, or on different tax entities, but they intend to settle current tax liabilities and assets on a net basis or their tax assets and liabilities will be realized simultaneously.

A deferred tax asset is recognized to the extent that it is probable that future taxable profits will be available against which the temporary difference can be utilized. Deferred tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

In 2009, pursuant to the receipt of a positive feasibility study for the Minago project, Victory Nickel determined that it was probable that it would be able to realize the benefit associated with its losses and costs prior to their expiry. Accordingly, the Company recognized the deferred tax assets (to the extent of the deferred tax liability) at that time. Victory Nickel continues to believe it is probable that the benefit of its losses and other costs will be realized prior to their expiry. The Company has not recognized any deferred tax assets relating to Victory Silica.

### **(p) Share Capital**

#### **(i) Common shares**

Common shares are classified as equity. Incremental costs directly attributable to the issue of common shares and share options are recognized as a deduction from equity, net of any tax effects.

The Company has financed a portion of its E&E activities through the issue of flow-through shares. Under the terms of these share issues, the tax attributes of the related expenditures are renounced to subscribers. Common shares issued on a flow-through basis typically include a flow-through premium because of the tax benefits associated therewith. Flow-through shares may also be issued with a warrant feature. At the time of issue, the Company estimates the proportion of proceeds attributable to the flow-through premium, the common share and the warrant with reference to closing market prices and such techniques as the Black-Scholes option-pricing model. The flow-through premium is estimated as the excess of the subscription price over the market value of the share and is recorded as a liability in *Trade and other payables* on the consolidated balance sheet. The proceeds attributable to the warrants is also treated as equity and recorded in *Contributed surplus* on the consolidated balance sheet until exercise, when the associated proportion is transferred to share capital along with the cash proceeds received on exercise.

The effect of renunciation of the tax benefits to holders of such shares is recognized pro rata with the associated expenditures being incurred by the Company. This could occur either before or after the formal renunciation of expenditures to the tax authorities have been made. When the eligible expenditures are incurred, the tax value of the renunciation is recorded as a deferred tax liability and charged against operations as a deferred tax provision.

Furthermore, as eligible expenditures are incurred, the Company recognizes a pro rata amount of the flow-through premium through *Finance income* in the consolidated statement of operations with a decrement to the liability in *Trade and other payables* on the consolidated balance sheet.

#### **(ii) Share-based payment arrangements**

##### **Stock Option Plan**

The Company has a stock option plan (the "Stock Option Plan") which is described in Note 20. Awards to non-employees are measured at the fair value of the goods or services received. Awards made to employees are measured at the grant date. All stock-based awards made to employees and non-employees are recognized at the date of grant using a fair-value-based method to calculate the share-based payment. The share-based payment is charged to operations over the vesting period of the options or service period, whichever is shorter. Stock options vest either immediately or over a 12-month period.

##### **Share Incentive Plan**

The Company has a share incentive plan (the "Share Incentive Plan"), which includes both a share purchase plan (the "Share Purchase Plan") and a share bonus plan (the "Share Bonus Plan"). The Share Incentive Plan is

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administered by the directors of the Company. The Share Incentive Plan provides that eligible persons thereunder include directors, senior officers and employees of the Company and its designated affiliates and consultants who are primarily responsible for the management and profitable growth of the business.

The Share Incentive Plan is described in Note 18. The Company uses the fair value method of accounting for, and to recognize as compensation expense, its share-based payments for employees. Common shares issued under the Share Incentive Plan are valued based on the quoted market price on the date of the award. This amount is expensed over the vesting period.

## **(q) Revenue Recognition**

Revenues from frac sand sales are recognized when legal title passes to the customer, which may occur at the Company's production facility, rail origin or at the destination terminal or transload facility. At that point, delivery has occurred, evidence of a contractual arrangement exists and collectability is reasonably assured.

## **(r) Earnings (Loss) per Share**

The Company presents basic and diluted earnings (loss) per share ("EPS") data for its common shares. Basic EPS is calculated by dividing the results of operations attributable to ordinary shareholders of the Company by the weighted average number of common shares outstanding during the period. Diluted EPS is determined by adjusting the results of operations attributable to common shareholders and the weighted average number of common shares outstanding for the effects of all dilutive potential common shares, which comprise warrants and share options.

## **(s) New Standards and Interpretations Not Yet Adopted**

The Company has not yet adopted the following new accounting pronouncements which are effective for fiscal periods of the Company beginning on or after January 1, 2018:

### ***IFRS 15, Revenue from Contracts with Customers***

IFRS 15 deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. Under IFRS 15, revenue is recognized when a customer obtains control of a good or service. The standard replaces IAS 18 "Revenue" and IAS 11 "Construction Contracts" and related interpretations. The standard is effective for annual periods beginning on or after January 1, 2018 and earlier application is permitted.

The Company has not identified any differences between the new standard and its current revenue recognition policy.

### ***IFRS 16, Leases***

In 2016, the IASB issued its new leasing standard. IFRS 16 eliminates the classification of leases as either operating leases or finance leases as previously required by IAS 17. Instead, it introduces a single lease accounting model that requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value, and to depreciate the lease assets separately from interest on the lease liabilities on the income statement. IFRS 16 will be effective for the Company's fiscal year beginning January 1, 2019, with earlier adoption permitted if the entity also adopts IFRS 15.

The Company has evaluated the impact of adopting this standard and does not believe it will have a material effect on its financial statements.

## **4. FINANCIAL RISK MANAGEMENT AND CAPITAL MANAGEMENT DISCLOSURES**

### **Overview**

The Company has exposure to the following risks from its use of financial instruments:

- credit risk;
- liquidity risk;
- market risk; and
- operational risk.

This note presents information about the Company's exposure to each of the above risks, the Company's objectives, policies and processes for measuring and managing risk, and the Company's management of capital.

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Further quantitative disclosures are included throughout these consolidated financial statements.

### **Risk Management Framework**

The Board of Directors has overall responsibility for the establishment and oversight of the Company's risk management framework. The Board fulfils its responsibility through the Audit Committee which is responsible for overseeing the Company's risk management policies.

The Company's risk management policies are established to identify and analyze the risks faced by the Company, to set appropriate risk limits and controls, and to monitor risks and adherence to limits. Risk management practices are reviewed regularly to reflect changes in market conditions and the Company's activities including entry into new operations, such as the frac sand business. The Company has an established code of conduct which sets out the control environment within which framework all directors' and employees' roles and obligations are outlined. The Company's risk and control framework is facilitated by the small-sized and hands-on executive team.

### **Credit Risk**

Credit risk is the risk of an unexpected financial loss to the Company if a customer or third-party to a financial instrument fails to meet its contractual obligations and arises principally from the Company's cash and cash equivalents, restricted deposits if any, receivables and marketable securities.

### **Cash and cash equivalents and restricted deposits**

The Company's cash and cash equivalents and restricted deposits, if any, are held through large Canadian financial institutions. The Company has a corporate policy of investing its available cash in Canadian government instruments and certificates of deposit or other direct obligations of major Canadian banks.

### **Receivables**

The Company has increased its exposure to credit risk upon commencement of sales of frac sand. The Company's other receivables consist of amounts due from federal and provincial governments. Amounts due from other parties are settled on a regular basis.

When necessary, the Company establishes an allowance for impairment that represents its estimate of incurred losses in respect of receivables. The main component of this allowance is a specific loss component that relates to individually significant exposures.

Further, when the Company engages in corporate transactions, it seeks to manage its exposure by ensuring that appropriate recourse is included in such agreements upon the counterparty's failure to meet contractual obligations.

### **Marketable securities**

The Company limits its exposure to credit risk by investing only in securities which are listed on public stock exchanges. Such strategic investments are approved by the Board of Directors of the Company. Management actively monitors changes in the markets and management does not expect any counterparty to fail to meet its obligations. The Company's investments are generally in the junior natural resources sector and these companies are subject to similar areas of risk as the Company itself.

### **Guarantees**

The Company's policy is to provide financial guarantees only to wholly-owned subsidiaries or under business arrangements where the benefit of the guarantee will enure to the Company. As at December 31, 2017 and 2016, the Company had no third-party guarantees outstanding.

### **Liquidity Risk**

Liquidity risk is the risk that the Company will encounter difficulty in meeting the obligations associated with its financial liabilities that are settled by delivering cash or another financial asset. The Company's approach to managing liquidity is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due without incurring unacceptable losses or risking undue damage to the Company's reputation.

The Company's objective is to maintain sufficient capital in order to meet short-term business requirements, after taking into account cash flows from operations and the Company's holdings of cash and cash equivalents and marketable securities. This is accomplished by budgets and forecasts which are updated on a periodic basis to understand future cash needs and sources. When possible, spending plans are adjusted accordingly to provide for liquidity.

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The Company manages its liquidity risk through the mechanisms described above and as part of Capital Disclosures below. The Company has historically relied on issuances of common shares to develop projects and to finance day-to-day operations and may do so again in the future.

As described in Note 1, the Company is experiencing liquidity issues and has refinanced a portion of its trade payables and loans, as outlined in Note 14.

### **Market Risk**

Market risk is the risk that changes in market prices, such as foreign exchange rates, interest rates, commodity prices and equity prices, will affect the Company's income, the value of its E&E and MP&D properties or the value of its holdings of financial instruments. The objective of market risk management is to manage and control market risk exposures within acceptable parameters, while optimizing the return. The frac sand market is relatively new to the Company and is subject to market forces affecting oil and natural gas pricing and related demand for frac sand.

### **Currency risk**

The Company is exposed to currency risk on purchases and other payables that are denominated in a currency other than the functional currency of the Company; the US dollar. The primary currency in which these transactions are denominated is the Canadian dollar. The Company does not actively hedge its foreign currency exposure.

### **Interest rate risk**

Interest rate risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market interest rates. The Company's cash equivalents earn interest at variable short-term rates. The Company's debt bears interest at fixed rates (Note 14). Accordingly, the estimated effect of a 50bps change in interest rate would not have a material effect on the Company's results of operations. None of the Company's other financial instruments are interest-bearing. Consequently, the Company is not presently exposed to any significant interest rate risk which could be caused by a sudden change in market interest rates.

### **Other market price risk**

The Company's marketable securities and strategic investments are subject to equity price risk. The values of these investments will fluctuate as a result of changes in market prices, the price of metals or other factors affecting the value of the investments.

Commodity price risk is the potential adverse impact on earnings and economic value due to commodity price movements and volatilities. The value of the Company's mineral resource properties is related to the price of, and outlook for, base and precious metals. Historically, such prices have fluctuated and are affected by numerous factors outside of the Company's control, including, but not limited to: industrial and retail demand, central bank lending, forward sales by producers and speculators, levels of worldwide production, short-term changes in supply and demand because of speculative hedging activities and other factors such as significant mine closures.

The Company does not have any hedging or other commodity-based risks respecting its operations. The value of the Company's strategic investments is also related to the price of, and outlook for, base and precious metals and other minerals. The future prices of frac sand sales are also subject to similar risks.

### **Operational Risk**

Operational risk is the risk of direct or indirect loss arising from a wide variety of causes associated with the Company's processes, personnel, technology and infrastructure, and from external factors other than credit, market and liquidity risks such as those arising from legal and regulatory requirements and generally accepted standards of corporate behaviour. Operational risks arise from all of the Company's operations. The Company typically has two main sand suppliers and, in order to partly mitigate supply risk, has optioned the Bear Coulee property (defined below).

The Company's objective is to manage operational risk so as to balance the avoidance of financial losses and damage to the Company's reputation with overall cost effectiveness and to avoid control procedures that restrict initiative and creativity.

The primary responsibility for the development and implementation of controls to address operational risk is assigned to senior management. The Company has a small but hands-on and experienced executive team which facilitates communication across the Company. This expertise is supplemented, when necessary, by the use of

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experienced consultants in legal, compliance and industry-related specialties. The Company also has standards for the management of operational risk in the following areas:

- requirements for appropriate segregation of duties, including the independent authorization of transactions;
- requirements for the reconciliation and monitoring of transactions;
- compliance with regulatory and other legal requirements, including the Occupational Health and Safety Act and related regulations and codes, and the Railway Safety Act and requirements of the Canadian Transportation Agency;
- documentation of controls and procedures, including quality control and plant maintenance;
- development of contingency plans;
- ethical and business standards; and
- risk mitigation, including insurance when this is effective and available.

Compliance with Company standards is supported by a code of conduct which is provided to salaried employees, officers and directors. The Company requires sign-off of compliance with the code of conduct.

## Capital Management Disclosures

The Company's objective when managing capital is to safeguard its accumulated capital in order to provide an adequate return to shareholders by maintaining a sufficient level of funds to support continued project development and corporate activities. Capital is defined by the Company as the aggregate of its shareholders' equity as well as any long-term debt, equipment-based and/or project-based financing.

| <b>As at December 31,</b>                | <b>2017</b> |               | <b>2016</b> |               |
|--|-------------|---------------|-------------|---------------|
| Shareholders' equity                     | \$          | <b>31,639</b> | \$          | 31,083        |
| Loans and borrowings - long-term portion |             | <b>7,286</b>  |             | 5,871         |
| Participating Interest                   |             | <b>529</b>    |             | 933           |
| Lease obligations - long-term portion    |             | -             |             | 5             |
|  | \$          | <b>39,454</b> | \$          | <b>37,892</b> |

The Company manages its capital structure and makes adjustments to it based on the level of funds available to the Company to manage its operations. In order to maintain or adjust the capital structure, the Company expects that it will be able to obtain equity, long-term debt, equipment-based, working capital and/or project-based financing sufficient to maintain and expand its operations. There are no assurances that these initiatives will be successful. In order to achieve these objectives, the Company invests its unexpended cash in highly-liquid, rated financial instruments.

Neither the Company, nor its subsidiaries, are subject to externally-imposed capital requirements. There were no changes in the Company's approach to capital management during the year.

## 5. DETERMINATION OF FAIR VALUES

A number of the Company's accounting policies and disclosures require the determination of fair value for both financial and non-financial assets and liabilities. Fair values have been determined for measurement and/or disclosure purposes based on the methods described below. When applicable, further information about the assumptions made in determining fair values is disclosed in the notes specific to that asset or liability.

### **Fair value hierarchy**

The different levels of valuation are defined as follows:

- Level 1: Quoted prices (unadjusted) in active markets for identical assets or liabilities;
- Level 2: Inputs other than quoted prices included within Level 1 that are observable for the asset or liability, either directly (i.e. as prices) or indirectly (i.e. derived from prices); and
- Level 3: Inputs for the asset or liability are not based on observable market data (unobservable inputs).

### **(a) Participating Interest**

The fair value of the Participating Interest is based on the estimates of expected future cash flows, as the expectations of payments of the Participating Interest change.

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### (b) Marketable Securities

The fair value of financial assets at fair value through operations or OCI is determined by reference to their quoted closing bid price at the reporting date.

### (c) Receivables

The fair value of receivables is estimated as the present value of future cash flows, discounted at the market rate of interest at the reporting date. This fair value is determined for disclosure purposes only.

### (d) Warrants and/or embedded derivatives

The fair values of warrants and/or embedded derivatives included in either financial assets or liabilities at fair value through operations or in equity are based upon the Black-Scholes option-pricing model. Measurement inputs include: share price on measurement date, exercise price of the instrument, expected volatility (based on weighted average historic volatility adjusted for changes expected due to publicly-available information), weighted average expected life of the instruments (based on historic experience and general option-holder behaviour), expected dividends and the risk-free interest rate (based on government bonds).

### (e) Non-derivative Financial Liabilities

Fair value, which is determined for disclosure purposes, is calculated based on the present value of future principal and interest cash flows, discounted at the market rate of interest at the reporting date.

### (f) Share-based Payment Transactions

The fair value of share options is measured using the Black-Scholes option-pricing model. The measurement inputs are described above under Note 5(e). Any service and non-market performance conditions attached to the transactions are not taken into account in determining fair value.

## 6. RECEIVABLES AND PREPAIDS

| As at December 31,                    |    | 2017 |    | 2016 |
|---------------------------------------|----|------|----|------|
| Trade accounts receivable             | \$ | 19   | \$ | 41   |
| Less: Allowance for doubtful accounts |    | -    |    | (23) |
|                                       |    | 19   |    | 18   |
| Other receivables                     |    | 14   |    | 51   |
| Promissory note                       |    | 55   |    |      |
| Prepaid expenses and deposits         |    | -    |    | 9    |
|                                       | \$ | 88   | \$ | 78   |

During 2017, the Company loaned \$55,000 to a company in the Frac Sand business. The Company has committed to provide up to \$200,000 in funding under certain terms of this note. The note has interest bearing at 15%, is secured and matures June 22, 2018. Any proceeds received from repayment of this loan must be used to repay the other current loan (in Note 14).

The aging of trade accounts receivable is as follows:

| As at December 31,        |    | 2017 |    | 2016 |
|---------------------------|----|------|----|------|
| Trade accounts receivable |    |      |    |      |
| Current                   | \$ | 19   | \$ | 16   |
| Past due 0-30 days        |    | -    |    | 2    |
| Past due 90 days          |    | -    |    | 23   |
|                           | \$ | 19   | \$ | 41   |

The Company maintains an allowance for doubtful accounts that represents its estimate of the uncollectible amounts based on specific losses estimated on individual exposures. As at December 31, 2016, the Company determined that it had exposure to losses due to the quality of one of its customers, in which the Company has not been able to collect the balance outstanding with this customer. During 2017, the balance outstanding of \$23,000 was written off.

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As at December 31, 2017, one of the Company's customers accounted for 100% of the trade accounts receivable balance (2016 – two customers for 100%).

### 7. MARKETABLE SECURITIES

The Company records its investment in shares at available market prices with any difference in fair value compared with acquisition cost being recorded as gain or loss on financial assets at fair value through OCI. The Company's financial assets at fair value through OCI are listed on public stock exchanges, including the TSX and TSX Venture Exchange. During 2017, the Company sold a portion of its holdings in marketable securities for proceeds of \$46,000. As at December 31, 2017, one junior mining company comprised 99% (2016 – 99%) of the balance of the Company's investment in shares.

In April 2015, the Company received 40,000,000 shares of Corazon Mining Limited ("Corazon") valued at \$192,000 as part of the option agreement of Lynn Lake as described in Note 12. During 2016, the Company sold all of its holdings in Corazon for net proceeds of AU\$515,000 and a small portion of its holdings in other marketable securities for net proceeds of CAD\$9,000.

### 8. INVENTORY

| As at December 31,               | 2017     | 2016     |
|----------------------------------|----------|----------|
| Raw material                     |          |          |
| At transload facility            | \$ -     | \$ 188   |
| Stored at 7P Plant               | 1,503    | 568      |
|                                  | 1,503    | 756      |
| Finished goods & other inventory | 348      | 1,467    |
|                                  | \$ 1,851 | \$ 2,223 |

The Company determined that a recovery of previously impaired inventory of \$495,000 (2016 – impairment write-down of \$517,000) to net realizable value was required during the year and was included in cost of goods sold. During 2017, ownership of 8,000 tons of sand stored in Wisconsin was transferred to the storage facilities, resulting in a reduction in the Company's inventory value of \$188,000.

### 9. FINANCIAL INSTRUMENTS

#### Credit Risk

##### Exposure to credit risk

The carrying amount of financial assets represents the maximum credit exposure. All amounts are held in Canada. The maximum exposure to credit risk at the reporting date was:

| As at December 31,                         | Notes | 2017   | 2016   |
|--|-------|--------|--------|
| <b>Carrying amount</b>                     |       |        |        |
| Cash and cash equivalents                  |       | \$ 125 | \$ 197 |
| Receivables                                | 6     | 88     | 78     |
| Financial assets at fair value through OCI | 7     | 255    | 158    |
|  |       | \$ 468 | \$ 433 |

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### Liquidity Risk

The following table shows the contractual maturities of financial liabilities as at the reporting date.

|                                | <u>Non-derivative financial liabilities</u> |                     |                                  |                          |  | Total     |
|--------------------------------|---|---------------------|----------------------------------|--------------------------|--|-----------|
|                                | Trade and other<br>payables <sup>(1)</sup>  | Short-term<br>loans | Leases<br>payable <sup>(1)</sup> | Long-term<br>liabilities |  |           |
| <b>As at December 31, 2017</b> |   |                     |                                  |                          |  |           |
| Carrying amount                | \$ 2,220                                    | \$ 6,500            | \$ 5                             | \$ 7,286                 |  | \$ 16,011 |
| Contractual cash flows         | 2,220                                       | 6,882               | 5                                | 7,368                    |  | 16,475    |
| 6 months or less               | 2,220                                       | 6,882               | 5                                | -                        |  | 9,107     |
| 6 - 12 months                  | -   | -                   | -                                | -                        |  | -         |
| 1 - 2 years                    | -   | -                   | -                                | 7,368                    |  | 7,368     |
| <b>As at December 31, 2016</b> |   |                     |                                  |                          |  |           |
| Carrying amount                | \$ 2,141                                    | \$ 6,073            | \$ 130                           | \$ 5,871                 |  | \$ 14,215 |
| Contractual cash flows         | 2,141                                       | 6,607               | 135                              | 6,023                    |  | 14,906    |
| 6 months or less               | 2,141                                       | 6,607               | 75                               | -                        |  | 8,823     |
| 6 - 12 months                  | -   | -                   | 55                               | -                        |  | 55        |
| 1 - 2 years                    | -   | -                   | 5                                | 6,023                    |  | 6,028     |

(1) Current leases payable are disclosed within *Trade and other payables* (Note 13) on the consolidated balance sheet.

As described in Notes 13 and 14, significant amounts in trade payables and the entire balance of short-term loans cannot be repaid until the Secured Lender is repaid. Thus, although the contractual cash flows of these balances are all six months or less, they are not expected to be repaid until after the maturity date of the Secured Lender.

### Currency Risk

#### *Exposure to currency risk*

#### **As at December 31, 2017**

(in thousands of US dollars)

|                           | US\$               | CAD\$             |
|---------------------------|--------------------|-------------------|
| Cash and cash equivalents | \$ 110             | \$ 15             |
| Receivables and prepaids  | 78                 | 10                |
| Marketable securities     | -                  | 255               |
| Trade and other payables  | (1,094)            | (1,131)           |
| Loans and borrowings      | (12,939)           | (847)             |
| Participating Interest    | -                  | (529)             |
|                           | <b>\$ (13,845)</b> | <b>\$ (2,227)</b> |

#### **As at December 31, 2016**

(in thousands of US dollars)

|                           | US\$               | CAD\$             |
|---------------------------|--------------------|-------------------|
| Cash and cash equivalents | \$ 12              | \$ 185            |
| Receivables and prepaids  | 21                 | 57                |
| Marketable securities     | -                  | 158               |
| Trade and other payables  | (1,121)            | (1,020)           |
| Loans and borrowings      | (11,278)           | (666)             |
| Participating Interest    | -                  | (933)             |
|                           | <b>\$ (12,366)</b> | <b>\$ (2,219)</b> |

### **Sensitivity analysis**

A 10% weakening of the United States dollar would have an approximate effect on the Company's equity of \$223,000 on balances denominated in CAD\$ as at December 31, 2017 (2016 - \$222,000). The analysis assumes that all other variables, in particular interest rates, remain constant.



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### Fair Value

#### Fair values versus carrying amounts

The fair values of the Company's financial assets and liabilities equal their carrying amounts shown in the consolidated balance sheets. The Company has not made any reclassifications between assets recorded at cost or amortized cost and fair value.

The table below analyses financial instruments carried at fair value by valuation method:

|  | Level 1 | Level 3  | Total    |
|--|---------|----------|----------|
| <b>As at December 31, 2017</b>             |         |          |          |
| Financial assets at fair value through OCI | \$ 255  | \$ -     | \$ 255   |
| Financial liabilities at fair value        | \$ -    | \$ (529) | \$ (529) |
|  | \$ 255  | \$ (529) | \$ (274) |

|  | Level 1 | Level 3    | Total      |
|--|---------|------------|------------|
| <b>As at December 31, 2016</b>             |         |            |            |
| Financial assets at fair value through OCI | \$ 158  | \$ -       | \$ 158     |
| Financial liabilities at fair value        | \$ -    | \$ (1,009) | \$ (1,009) |
|  | \$ 158  | \$ (1,009) | \$ (851)   |

There have been no transfers between Level 1, Level 2 and Level 3 during the current and prior reporting periods. All of the shares owned by the Company are valued using Level 1 methodologies.

### 10. PROPERTY, PLANT AND EQUIPMENT

|   | Land and Building | 7P Plant        | Vehicles and Mobile Equipment | Equipment and Furniture | Total           |
|---|-------------------|-----------------|-------------------------------|-------------------------|-----------------|
| <b>Balances as at January 1, 2016</b>   |                   |                 |                               |                         |                 |
| Cost                                    | 83                | 4,804           | 708                           | 220                     | 5,815           |
| Accumulated Amortization                | (12)              | (900)           | (327)                         | (35)                    | (1,274)         |
| Effect of Foreign Exchange              | (8)               | (157)           | (47)                          | (160)                   | (372)           |
| <b>Carrying Amount</b>                  | <b>\$ 63</b>      | <b>\$ 3,747</b> | <b>\$ 334</b>                 | <b>\$ 25</b>            | <b>\$ 4,169</b> |
| Amortization                            | (1)               | (515)           | (91)                          | (4)                     | (611)           |
| <b>Balances as at December 31, 2016</b> |                   |                 |                               |                         |                 |
| Cost                                    | 83                | 4,804           | 708                           | 220                     | 5,815           |
| Accumulated Amortization                | (13)              | (1,415)         | (418)                         | (39)                    | (1,885)         |
| Effect of Foreign Exchange              | (8)               | (145)           | (41)                          | (169)                   | (363)           |
| <b>Carrying Amount</b>                  | <b>\$ 62</b>      | <b>\$ 3,244</b> | <b>\$ 249</b>                 | <b>\$ 12</b>            | <b>\$ 3,567</b> |
| Additions                               | -                 | 77              | -                             | -                       | 77              |
| Disposals - cost                        | -                 | -               | (23)                          | -                       | (23)            |
| Disposals - accumulated amortization    | -                 | -               | 15                            | -                       | 15              |
| Amortization                            | (1)               | (521)           | (65)                          | (3)                     | (590)           |
| <b>Balances as at December 31, 2017</b> |                   |                 |                               |                         |                 |
| Cost                                    | 83                | 4,881           | 685                           | 220                     | 5,869           |
| Accumulated Amortization                | (14)              | (1,936)         | (468)                         | (42)                    | (2,460)         |
| Effect of Foreign Exchange              | (7)               | (133)           | (41)                          | (171)                   | (352)           |
| <b>Carrying Amount</b>                  | <b>\$ 62</b>      | <b>\$ 2,812</b> | <b>\$ 176</b>                 | <b>\$ 7</b>             | <b>\$ 3,057</b> |

During 2017, the Company completed the refurbishment of its frac sand wash plant at the 7P Plant. The wash plant is now operational, providing the ability to immediately wash and sell frac sand. As at December 31, 2017 Vehicles and Mobile Equipment includes \$46,000 (2016 - \$617,000) of equipment remaining to be acquired at the end of its term under finance leases (Note 16).

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### 11. MINE PROPERTY AND DEVELOPMENT PROJECT

|        | January 1,<br>2017 | Current<br>Expenditures | December 31,<br>2017 |
|--------|--------------------|-------------------------|----------------------|
| Minago | \$ 34,974          | \$ 22                   | \$ 34,996            |
|        | \$ 34,974          | \$ 22                   | \$ 34,996            |

|        | January 1,<br>2016 | Current<br>Expenditures | December 31,<br>2016 |
|--------|--------------------|-------------------------|----------------------|
| Minago | \$ 34,952          | \$ 22                   | \$ 34,974            |
|        | \$ 34,952          | \$ 22                   | \$ 34,974            |

#### Minago

The 100%-owned Minago project covers approximately 19,799 ha, through a combination of mining claims, mineral leases and a mineral exploration licence, on Manitoba's Thompson Nickel Belt. The property encompasses the Nose Deposit, which contains the entire current nickel mineral resource, and the North Limb, a zone of nickel mineralization with a known strike length of 1.5 kilometres located to the north of the Nose Deposit.

From 2006 to date, considerable work has been performed, including diamond drilling, metallurgical testing and engineering studies and all the studies required to complete the Environmental Impact Study that was filed in May 2010. As a result, in August 2011, the Company received its Environmental Act Licence ("EAL"). In April 2014, the Company announced the filing of an amendment to the EAL to relocate the permitted Minago tailings facilities, such that it will not interfere with potential nickel resources and also reduce operating costs. Consultations with First Nations by the Government of Manitoba continue. On completion, the government is expected to issue the amendment to the existing EAL which continues to be valid. The results of the Minago Feasibility Study ("FS") were announced in December 2009 and improvements thereto announced in June 2010 and July 2011.

Five mineral claims totalling 691 ha located at the north end of the Company's existing Minago property package are subject to a maximum 2% net smelter return royalty ("NSR") with a 50% back-in right; these claims represent approximately 2.4% of the total Minago project and are not contained in the FS pit footprint.

The Minago project is not in production. Accordingly, the Minago project is not being depreciated.

As at December 31, 2017, the Company tested the Minago project for impairment. The economic model in the FS was used as a base. The business model used in the FS and the intention of management is to develop and produce the nickel and frac sand co-product simultaneously. Under IFRS, for the purposes of assessing the impairment of Minago, frac sand is treated as a raw material for sale into the market and is not processed to a finished product. This required elimination from the FS economic model of the following: processing plant capital, processing operating costs, transportation costs and the finished goods margin. This does not reflect how management intends to develop Minago, nor, in management's opinion, does it reflect how any other organization would develop the project.

In addition, adjustments were made for prices derived from the forecasted average of \$8 per pound for nickel and an exchange rate of US\$0.775:CAD\$1.00. The forecasted average price and exchange rate were obtained from third-party reports. A discount rate of 11% was used in the analysis. These factors resulted in a recoverable amount in excess of the book value of Minago. Accordingly, no impairment exists on the Minago project.

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The impairment model is sensitive to several of the model key input variables. The following table indicates the estimated impact on the recoverable amount:

| Change in Model Key Input      | Change in Recoverable Amount of Minago |
|--------------------------------|--|
| Effect of:                     |  |
| Increase discount rate by 1%   | (24%)                                  |
| Increase exchange rate by 0.05 | (23%)                                  |
| Increase nickel prices by 1%   | 4%                                     |
| Increase operating costs by 5% | (9%)                                   |

## 12. EXPLORATION AND EVALUATION PROJECTS

Cumulative costs relating to the acquisition of mineral properties and E&E expenditures have been incurred on the following projects:

|            | January 1,<br>2017 | Current<br>Expenditures | Writedowns | December 31,<br>2017 |
|------------|--------------------|-------------------------|------------|----------------------|
| Lac Rocher | \$ 1,922           | \$ -                    | \$ -       | \$ 1,922             |
| Mel        | 6,796              | -                       | -          | 6,796                |
|            | \$ 8,718           | \$ -                    | \$ -       | \$ 8,718             |

|            | January 1,<br>2016 | Current<br>Expenditures | Writedowns | December 31,<br>2016 |
|------------|--------------------|-------------------------|------------|----------------------|
| Lac Rocher | \$ 6,617           | \$ 5                    | \$ (4,700) | \$ 1,922             |
| Mel        | 6,792              | 4                       | -          | 6,796                |
|            | \$ 13,409          | \$ 9                    | \$ (4,700) | \$ 8,718             |

### Lac Rocher

The Lac Rocher project, which is 100%-owned, is located 140 kilometres northeast of Matagami in northwestern Québec. The project is subject to a royalty of CAD\$0.50 per ton on any ores mined and milled from the property and a 2% NSR described below.

The Lac Rocher property is subject to a discovery incentive plan (the "DIP") to reward certain individuals involved in the discovery of Lac Rocher with a 2% NSR for mines that were discovered on certain properties prior to the expiry of the DIP. The NSR is payable only on revenues earned after recovery of all development costs for any mine on the property. The terms of the DIP provide the Company with a right of first refusal on any proposed disposition of the NSR. In addition, the DIP contains put/call provisions under which the Company may be required to purchase, or may exercise an option to purchase, the NSR at the value of its discounted cash flows, as defined therein. The Lac Rocher property is the only property subject to the DIP. As the Lac Rocher property is not yet in production, no royalties are currently payable.

### Mel

The Company purchased a 100% interest in the Mel properties located near Thomson, Manitoba from Vale. Vale is entitled to a 10% royalty on "distributable earnings" defined as net revenue less operating expenses, before federal and provincial income taxes, after provincial mining taxes and less aggregate pre-production capital but before depreciation.

Vale has a contractual obligation to mill ore mined from the Mel deposit at its cash cost plus 5% provided that the product meets Vale specifications and that Vale has sufficient mill capacity.

### Lynn Lake

The Company owns a 100% right, title and interest in the Lynn Lake nickel property ("Lynn Lake"), covering approximately 600 ha in northern Manitoba. In November 2014, the Company announced that it had optioned the

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Lynn Lake property to Corazon. Under the terms of the option agreement, subject to any required regulatory approvals, Corazon can acquire a 100% interest in Lynn Lake by issuing to Victory Nickel, 40,000,000 Corazon shares upon closing and incurring AU\$3,500,000 in exploration expenditures or payments (in cash or Corazon shares at Corazon's option) to Victory Nickel before November 2019. In addition, Victory Nickel will retain a 1.5% net smelter royalty on production from Lynn Lake and receive a payment of AU\$1,000,000 (in cash or Corazon shares at Corazon's option) within 30 days of ore processing activities. In April 2015, the Company received 40,000,000 shares of Corazon valued at \$192,000 as part of the option agreement. These shares were sold in 2016.

### Bear Coulee

In October 2014, the Company entered into an option to acquire a 100% interest in a frac sand land package totalling over 300 acres in Trempeleau County Wisconsin, USA (the "Bear Coulee Property"). The option agreement provides for a cash payment on signing of the agreement, a second cash payment on delivery of permits and a third cash payment on exercise of the option. The option is valid for six months from receipt of permits with two equivalent extensions available under certain circumstances. Prior to production, the Company will be required to pay \$40,000 per annum as advance royalties on the initial 20,000 tons of sand production. Once the Bear Coulee Property is in production, the Company will be required to pay a royalty of \$2.00 per ton of frac sand sold that is mined from the property.

In February 2015, the Company announced that a resource estimate of approximately 11 million tons of sand has been completed on the Bear Coulee Property and was incorporated into a National Instrument 43-101 technical report.

### 13. TRADE AND OTHER PAYABLES

| As at December 31,                    | 2017            | 2016            |
|---------------------------------------|-----------------|-----------------|
| Accounts payable                      |                 |                 |
| Mine property and development project | \$ 15           | \$ 11           |
| Exploration and evaluation projects   | 3               | 3               |
| Frac Sand segment                     | 1,818           | 1,765           |
| Other payables                        | 52              | 10              |
| Accrued liabilities                   |                 |                 |
| Other accrued liabilities             | 332             | 227             |
| Lease obligations - current portion   | 5               | 125             |
|                                       | <u>\$ 2,225</u> | <u>\$ 2,141</u> |

During 2016, the Company completed the restructuring of a portion of its trade payables, under the terms of the Debt Restructuring Agreement, in settlement of aggregate amounts of \$106,000 and CAD\$533,000 in trade payables and CAD\$267,000 of indebtedness to directors and management.

As part of the SPA Amended Loan (described in Note 14) with the Secured Lender, the Company agreed to not make any payments to settle past unsecured debt or balances outstanding with trade creditors who did not agree to the Debt Restructuring Agreement, prior to the repayment of the Senior Secured Debt, without the Secured Lender's approval. The balances with trade creditors, who did not agree to the Debt Restructuring Agreement, amount to \$975,000 and CAD\$777,000, and remain outstanding as at December 31, 2017.

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### 14. LOANS AND BORROWINGS

| As at December 31,                   | Notes | 2017      | 2016      |
|--------------------------------------|-------|-----------|-----------|
| Current loans and borrowings         |       |           |           |
| Outstanding Note                     | (b)   | \$ 3,000  | \$ 3,000  |
| New Promissory Convertible Notes     | (b)   | 1,629     | 1,298     |
| Accrued interest                     |       | 1,806     | 1,775     |
| Other current loan                   |       | 65        | -         |
| Total current loans and borrowings   |       | 6,500     | 6,073     |
| Long-term loans and borrowings       |       |           |           |
| Senior Secured Debt                  | (a)   | \$ 6,968  | \$ 5,468  |
| New Promissory Convertible Notes     | (b)   | -         | 123       |
| Debt owed to management & directors  | (b)   | 318       | 280       |
| Total long-term loans and borrowings |       | 7,286     | 5,871     |
|                                      |       | \$ 13,786 | \$ 11,944 |

During 2017, the Company made interest payments of \$22,000 (2016 - \$38,000) and a further \$1,550,000 was capitalized when the Senior Secured Debt was extended. The Company also incurred interest expense of \$1,617,000 (2016 - \$1,422,000), amortized loan fees of \$25,000 (2016 - \$21,000) and amortized embedded derivatives of \$260,000 (2016 - \$340,000).

#### (a) Senior Secured Debt

| As at December 31,  | 2017            | 2016            |
|---|-----------------|-----------------|
| Carrying balance at beginning of the year                         | \$ 5,468        | \$ 5,150        |
| Conversion from accrued interest                                  | 1,550           | 350             |
| Change in fair value of warrants with a cashless exercise feature | (6)             | 6               |
| Change in unamortized fair value of warrants                      | 15              | (15)            |
| Unamortized loan fees   | (59)            | (23)            |
| <b>Senior Secured Debt</b>  | <b>\$ 6,968</b> | <b>\$ 5,468</b> |

In May 2014 the Company announced that it had executed the SPA Loan ("SPA Loan"), to issue and sell to the purchaser senior secured 14.8% notes in the aggregate principal amount of \$4,000,000. In June 2015, the Company announced it had entered into an amending agreement (the "SPA Amended Loan") with respect to the SPA Loan. The SPA Loan was amended to permit the issuance of additional notes by the Company for a sum of \$1,150,000. The aggregate principal amount of \$5,150,000 under the SPA Amended Loan was due July 30, 2015. In July 2015, the Company announced that it was not able to make the quarterly interest payments due, including the principal amount.

In March 2016, the Company announced that it had restructured the SPA Amended Loan per the terms of the Debt Restructuring Agreement. The SPA Amended Loan was increased to \$5,500,000 and the maturity date was extended to January 31, 2018. The amount under the Senior Secured Debt was used to repay the principal of \$5,150,000 and \$350,000 of accrued interest. The Secured Lender received a fee in common shares equal to 4% of outstanding common shares of the Company prior to the restructuring of the SPA Amended Loan. Accordingly, 2,305,404 common shares were issued.

On December 31, 2017, the Senior Secured Debt was increased to \$7,050,000, to repay \$1,550,000 of accrued interest, and the maturity date was extended to July 31, 2019. The Secured Lender received a fee of 2,500,000 common shares. Under the terms of the amendment, if the Senior Secured Debt is outstanding on December 31, 2018, an additional fee of 2,500,000 common shares will be issued by the Company to the Secured Lender.

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The interest rate on the Senior Secured Debt remained unchanged at 14.8% with interest payable in arrears. The Senior Secured Debt is due in full on the date of maturity, subject to a cash sweep of 75% of free cash flow ("Free Cash Flow") payable within 45 days following the end of each fiscal quarter and 90 days from each fiscal year end. Free Cash Flow will be calculated based on the Company's quarterly unaudited and annually audited consolidated statement of cash flows, as net cash from operating and investing activities, plus interest and lease payments from financing activities. Allowable investing activities must be approved in advance by the Secured Lender.

In addition, the Company has agreed to not make any payments to settle past unsecured debt prior to the repayment of the Senior Secured Debt, without the Secured Lender's approval.

### Warrants issued to the Secured Lender

Under the terms of the SPA Loan, the Company issued 2,000,000 common share purchase warrants. The number of common share purchase warrants is subject to an increase from 500,000 to 1,000,000 warrants for each \$1,000,000 note issued under the SPA Loan, if any of the notes are prepaid and the closing price of the Company's share price is CAD\$2.00 or lower on the trading day preceding the date of such prepayment (the "Original Warrants"). Given that there are costs associated with the prepayment right, the Company has valued the prepayment right at \$nil.

Pursuant to the terms under SPA Amended Loan, the Company issued an additional 575,000 common share purchase warrants on the same terms as the Original Warrants (together with the Original Warrants, the "Amended Warrants").

Under the terms of the Senior Secured Debt, the Amended Warrants were modified to reduce the exercise price to CAD\$0.25 from CAD\$1.00 and to extend the expiry date to January 31, 2018. Additionally, as partial consideration for entering into the Senior Secured Debt, the Company issued an additional 175,000 common share purchase warrants on the same terms as the Amended Warrants (together with the Amended Warrants, the "Warrants").

The Warrants are subject to a cashless exercise provision and are considered a component of debt rather than equity; the fair value at inception of the Senior Secured Debt was calculated at \$26,000 and was revalued at December 31, 2017 to \$nil (2016 - \$6,000), with the change in fair value of \$6,000 (2016 - \$20,000) being recorded in finance income (Note 21).

The value of the Warrants has been calculated using the Black-Scholes option-pricing model using the following parameters:

| <b>As at December 31,</b>       | <b>2017</b>       | <b>2016</b> |
|---------------------------------|-------------------|-------------|
| Fair value                      | <b>CAD\$0.00</b>  | CAD\$0.002  |
| Share price at valuation date   | <b>CAD\$0.045</b> | CAD\$0.02   |
| <b>Assumptions</b>              |                   |             |
| Exercise price                  | <b>CAD\$0.25</b>  | CAD\$0.25   |
| Expected volatility             | <b>151%</b>       | 167%        |
| Expected remaining term (years) | <b>0.08</b>       | 1.08        |
| Risk-free interest rate         | <b>1.66%</b>      | 0.73%       |

Subsequent to December 31, 2017, the Warrants expired unexercised on January 31, 2018.

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### (b) Promissory Convertible Notes

| As at December 31,   | 2017        | 2016          |
|--|-------------|---------------|
| Total Principal Outstanding at beginning of the year                         | \$ 4,421    | \$ 5,942      |
| Less: restructuring of Promissory Convertible Notes                          | -           | (1,475)       |
| Add: restructuring of debt owed to trade creditors, directors and management | -           | 512           |
| Change in present value discount on debt                                     | 148         | (473)         |
| Change in fair value of conversion options                                   | (70)        | 70            |
| Change in unamortized embedded derivatives                                   | 97          | (155)         |
| Effect of foreign exchange   | 33          | -             |
| Carrying balance at the end of the year                                      | 4,629       | 4,421         |
| Less: Outstanding Note   | (3,000)     | (3,000)       |
| Less: current portion of New Promissory Convertible Notes                    | (1,629)     | (1,298)       |
| <b>New Promissory Convertible Notes - Long term portion</b>                  | <b>\$ -</b> | <b>\$ 123</b> |

During 2013 and 2014, the Company entered into several unsecured Promissory Convertible Notes and incurred interest payable quarterly at 14.8%. All Promissory Convertible Notes had a two-year term.

During 2016, the Company announced that it had restructured a portion of its debt through private placements of common shares and unsecured promissory convertible notes (the "New Promissory Convertible Notes") in settlement of current indebtedness to certain of its unsecured lenders and trade creditors (collectively the "Unsecured Debt Restructuring"). Completion of the Unsecured Debt Restructuring represented 50% of the value owed to the Promissory Convertible Note holders and trade creditors. The Unsecured Debt Restructuring included issuing a total of 27,698,443 common shares of the Company and New Promissory Convertible Notes for a total of \$1,481,000 and CAD\$933,000.

The market prices of the Company's common shares on the dates of issuance during 2016 were lower than the calculated cost per common share upon conversion to the New Promissory Convertible Notes and settlement of outstanding interest, resulting in an increase in share capital of \$637,000 and a non-cash gain on settlement of debt of \$2,545,000.

The Company has not made any interest payments due on its New Promissory Convertible Notes, which has resulted in the Company defaulting on the New Promissory Convertible Notes.

#### Promissory Convertible Note Holders

During 2016, unsecured debt of \$2,750,000 and CAD\$265,000 held by the Promissory Convertible Note holders was repaid under the following terms:

- 1) 50% of the value of the Promissory Convertible Notes issued during 2013 and 2014, with an interest rate of 14.8% per annum, was converted to 8,876,350 of common shares of the Company.
- 2) Outstanding interest on the Promissory Convertible Notes was settled with the issuance of 4,732,028 common shares of the Company.
- 3) The remaining 50% of the value of the Promissory Convertible Notes were replaced with the New Promissory Convertible Notes for a total of \$1,375,000 and CAD\$133,000, having the following terms:
  - A maturity date of July 31, 2018;
  - An interest rate of 7% per annum, payable annually or at any time in cash or in common shares valued at market, at the option of the Company;
  - Convertible at CAD\$0.25 per share, at the option of the holder; and
  - Holders of the New Promissory Convertible Notes will also receive one common share purchase warrant for every four common shares acquired upon conversion of the New Promissory Convertible Notes, with an exercise price of CAD\$0.50 per share, exercisable for a five year period from the date of conversion.

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### Outstanding Note

All of the Promissory Convertible Note holders participated in the Debt Restructuring Agreement, except for one holder of the Outstanding Note of \$3,000,000. In March 2016, the Company announced that it had received notice that the holder of the Outstanding Note had filed a statement of claim concerning non-payment of principal and interest. The Company has reviewed the statement of claim with legal counsel to assess its impact on the Company and has concluded that there is no significant impact on the status of the Company's debt. Pursuant to the terms of the Senior Secured Debt, the Company is prevented from making payments under outstanding unsecured debt until the Senior Secured Debt is repaid. As a result, the Company has not paid interest accrued on the Outstanding Note. The Outstanding Note matured in July 2016 and the Company has been unable to repay the amounts owing and interest payments due. This has resulted in the Company defaulting on the Outstanding Note.

### Debt Owed to Trade Creditors, Directors and Management

During 2016, restructuring of debt owed to certain trade creditors, directors and management of \$211,000 and CAD\$1,600,000 was repaid under the following terms:

- 1) 50% of debt owed to trade creditors, directors and management, was converted to 18,822,093 of common shares of the Company.
- 2) The remaining 50% of the debt owed to trade creditors was paid with the New Promissory Convertible Notes for a total of \$106,000 and CAD\$533,000, having the same terms as outlined above in the section *Promissory Convertible Note Holders*.
- 3) The remaining 50% of debt owed to directors and management amounting to CAD\$267,000 was deferred for payment by January 31, 2018.

As at December 31, 2017, current directors and management agreed to defer payment of all outstanding debt and director fees until July 2019. As a result, the long-term debt of \$318,000 owed to directors and management is comprised of a portion of the restructured debt owed to current directors and management amounting to CAD\$224,000, and director fees incurred by current directors during 2016 and 2017 totalling CAD\$175,000.

### Conversion Options of the New Promissory Convertible Notes

The options to convert the New Promissory Convertible Notes to common shares of the Company have been calculated using the Black-Scholes option-pricing model with the following parameters:

| <b>As at December 31,</b>       | <b>2017</b>         | <b>2016</b>         |
|---------------------------------|---------------------|---------------------|
| Fair values                     | <b>CAD\$0.00</b>    | CAD\$0.00 to \$0.01 |
| Share price at valuation date   | <b>CAD\$0.045</b>   | CAD\$0.02           |
| <b>Assumptions</b>              |                     |                     |
| Exercise price                  | <b>CAD\$0.25</b>    | CAD\$0.25           |
| Expected volatilities           | <b>152% to 157%</b> | 158% to 163%        |
| Expected remaining term (years) | <b>0.58</b>         | 1.58                |
| Risk-free interest rate         | <b>1.66%</b>        | 0.73%               |

Due to the unlikelihood of the conversion options being exercised at a fair value of \$nil at December 31, 2017, the common share purchase warrants, that the holders of the New Promissory Convertible Notes would receive upon conversion of the notes to common shares of the Company, are also valued at \$nil.

## 15. PARTICIPATING INTEREST

| <b>As at December 31,</b>     | <b>2017</b>   | <b>2016</b> |
|-------------------------------|---------------|-------------|
| Opening balance               | <b>\$ 933</b> | \$ 1,702    |
| Change in fair value          | <b>(404)</b>  | (769)       |
| <b>Participating Interest</b> | <b>\$ 529</b> | \$ 933      |



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Pursuant to a participating interest loan (the "Participating Interest") with Nuinsco Resources Limited ("Nuinsco" or the "Lender"), the Lender has the right to convert the outstanding balance into a limited participating interest (the "Conversion"), whereby the Lender is entitled to receive a share of cash flows earned from the sale of frac sand from the 7P Plant. The Lender's participation was capped at CAD\$10,000,000, with a minimum of CAD\$7,500,000, and was subject to adjustment under certain circumstances.

The Participating Interest is classified as a financial liability carried at amortized cost. The estimated future cash flows discounted at 15% were determined using a probability-weighted estimation of future expected cash flow scenarios from the three-phased frac sand business based on current expectations of business results, capital costs and pre-operating expenditures. An assessment is made regarding the applicable ceiling for the cash flows which is dependent upon the phase attained by the Company when payments under the Participating Interest are anticipated. These cash flows were on the basis of completion of phase two; the Company expects to enter phase two before paying out the expected cash flows, despite announcing during February 2015, a deferral of phase two. The Company also included probability weightings of 50%, 25% and 25% as risk factors applied to varying levels of expected cash flows – being zero, 50% and 100% of the applicable ceiling maximum of CAD\$7,667,000.

As described earlier, the percentage participation in net cash flows is 52.16% and the applicable ceiling for phase two is CAD\$7,667,000 (phase one - CAD\$10,222,000). As a result of the continued slowdown in demand for frac sand, the continued suspension of operations at the 7P Plant and the losses incurred during the last few years, the estimated fair value of the Participating Interest was valued at \$529,000 at December 31, 2017 (2016 - \$933,000). This is a Level 3 methodology and is subject to the highest level of uncertainty. The Company will continue to review and revise its estimates of expected future cash flows, as the expectations of payments of the Participating Interest change. Changes in that estimate will be recorded through operations with appropriate adjustment for actual cash flows paid.

### 16. LEASE OBLIGATIONS

| <b>As at December 31,</b>                                      | <b>2017</b> |     | 2016   |
|--|-------------|-----|--------|
| Vehicles and Mobile Equipment:                                 |             |     |        |
| Total present value of minimum lease payments                  | \$          | 5   | \$ 516 |
| Principal payments   |             | (5) | (386)  |
| <b>Total present value of minimum lease payments remaining</b> |             | -   | 130    |
| Lease obligations - current portion                            |             | -   | (125)  |
| <b>Lease obligations - long-term</b>                           | \$          | -   | \$ 5   |

The Company has one remaining finance lease obligation for equipment in use at the 7P Plant. At the end of the lease obligation, ownership is transferred to the Company after an election is made 90 days prior to the end of the lease term at the purchase option price of CAD\$10.00.

The future minimum lease payments (also reflected in the liquidity risk section in Note 9) are as follows:

| <b>As at December 31,</b>                        | <b>2017</b> |   | 2016   |
|--|-------------|---|--------|
| Less than 1 year                                 | \$          | 5 | \$ 130 |
| Between 1 and 5 years                            |             | - | 5      |
| <b>Total minimum lease payments payable</b>      |             | 5 | 135    |
| Future finance charges on minimum lease payments |             | - | 5      |
| <b>Present value of minimum lease payments</b>   | \$          | 5 | \$ 130 |

### 17. DEFERRED TAX LIABILITY

During 2016, the sale of the Partnership generated income for tax purposes significantly in excess of its accounting income and created a significant deferred tax liability, which allowed the Company to utilize a majority of its non-capital tax losses carried forward from prior years. In 2017, the Company confirmed that its election to use US

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dollars as its functional currency for income taxes had been received and processed. As a result, the Company recorded a tax recovery mainly due to foreign exchange, to adjust the rate used to convert its various tax pools from Canadian dollars to US dollars. Refer to Note 22.

Deferred income tax assets and liabilities were recognized for temporary differences between the carrying value of the balance sheet items and their corresponding tax values. The differences as presented below:

| As at December 31,                                  | 2017            | 2016              |
|---|-----------------|-------------------|
| Temporary Differences                               |                 |                   |
| Property, plant and equipment, net                  | \$ 348          | \$ 113            |
| Exploration, evaluation & development projects, net | (4,787)         | (5,752)           |
| Non-capital losses carried forward                  | 3,753           | 2,057             |
| Capital losses carried forward                      | 1,838           | 1,823             |
| Other   | 104             | 65                |
| Deferred tax liability                              | \$ 1,256        | \$ (1,694)        |
| Add Back: Unrecognized deferred tax asset           | (2,167)         | (2,115)           |
| <b>Deferred tax liability, net</b>                  | <b>\$ (911)</b> | <b>\$ (3,809)</b> |

Deferred income tax assets are recognized to the extent of the deferred tax liabilities, since the Company currently believes that it is probable that the benefit associated with these losses and costs will be realized prior to their expiry. It also includes the effect of enacted rate changes.

Non-capital losses, on which a deferred tax asset was recognized, expire in 2027 to 2037. As at December 31, 2017, the Company had capital losses of \$13,618,000 available to be carried forward indefinitely (December 31, 2016 - \$13,505,000).

### 18. CAPITAL AND OTHER COMPONENTS OF EQUITY

#### Share Capital

The Company is authorized to issue an unlimited number of common shares with no par value. The issued and outstanding common shares for the following periods are as follows:

|  | Number of<br>Shares | Share<br>Capital |
|--|---------------------|------------------|
| Balance as at January 1, 2017          | 92,370,968          | \$ 53,241        |
| Issue of common shares for loan fee    | 2,500,000           | 82               |
| <b>Balance as at December 31, 2017</b> | <b>94,870,968</b>   | <b>\$ 53,323</b> |

On December 31, 2017, the Company issued common shares as a loan fee to the Secured Lender, as part of the amended terms of the Senior Secured Debt as outlined in Note 14.

|   | Number of<br>Shares | Share<br>Capital |
|---|---------------------|------------------|
| Balance as at January 1, 2016                         | 57,635,093          | \$ 52,570        |
| Issue of Common shares for loan fee                   | 2,305,404           | 34               |
| Issue of common shares - Unsecured Debt Restructuring | 32,430,471          | 637              |
| Balance as at December 31, 2016                       | 92,370,968          | \$ 53,241        |

During 2016, the Company issued common shares as part of the Unsecured Debt Restructuring and Senior Secured Debt, as outlined in Note 14.

#### Share Incentive Plan

The Company has a Share Incentive Plan which includes a Share Purchase Plan and a Share Bonus Plan. The purpose of the Share Incentive Plan is to encourage ownership of common shares by directors, senior officers and employees of the Company and its designated affiliates and consultants who are primarily responsible for the

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management and profitable growth of its business, to advance the interests of the Company by providing additional incentive for superior performance by such persons and to enable the Company and its designated affiliates to attract and retain valued directors, officers, employees and consultants.

### **Share Purchase Plan**

Under the Share Purchase Plan, eligible directors, senior officers and employees of the Company and its designated affiliates and consultants can contribute up to 10% of their annual basic salary before deductions to purchase common shares. The Company matches each participant's contribution. The purchase price per common share is the volume-weighted average of the trading prices of the common shares on the CSE for the calendar quarter in respect of which the common shares are issued. Common shares acquired are held in safekeeping and delivered to employees as soon as practicable following March 31, June 30, September 30 and December 31 in each calendar year. No common shares have yet been issued pursuant to the Share Purchase Plan. The maximum number of common shares issuable under the Share Purchase Plan is the lesser of: (i) that number of common shares that can be purchased with a dollar amount equal to 20% of the gross annual salary of the Participants (as defined in the Share Incentive Plan); and (ii) 1% of the aggregate number of issued and outstanding common shares (calculated on a non-diluted basis) from time to time.

### **Share Bonus Plan**

The Share Bonus Plan permits common shares to be issued as a discretionary bonus to eligible directors, senior officers and employees of the Company and its designated affiliates, and consultants from time to time. At the Company's Annual and Special Meeting of Shareholders held on June 26, 2012, shareholders approved an increase in the maximum number of common shares issuable under the Share Bonus Plan to 1,000,000. No shares were issued under the plan during 2017 or 2016.

### **Accumulated Other Comprehensive Income or (Loss) ("AOCI")**

AOCI is comprised of the following separate components of equity:

#### ***Net change of financial assets at fair value through OCI***

This comprises the cumulative net change in the fair value of financial assets at fair value through OCI.

#### ***Income tax on other comprehensive income***

This comprises the amount of income tax determined to be required on the cumulative net change in the fair value of financial assets at fair value through OCI.

#### ***Foreign exchange on change in functional currency***

This comprises the effects of the translation of the financial statements of the Company's subsidiaries, presented in CAD\$ and translated to US\$ (the Company's functional currency). Refer to Note 2.

## **19. EARNINGS (LOSS) PER SHARE**

The calculation of basic and diluted earnings (loss) per share for the years ended December 31, 2017 and 2016 was based on the information in the table below.

| <b>Years ended December 31,</b>  | <b>2017</b>       | <b>2016</b>       |
|--|-------------------|-------------------|
| <b>Balance as at beginning of the year</b>   | <b>92,370,968</b> | 57,635,093        |
| Effect of shares issued - Unsecured Debt Restructuring                                 | -                 | 27,361,620        |
| Effect of shares issued for loan fees  | <b>6,849</b>      | -                 |
| <b>Weighted average number of common shares at end of the year - Basic and Diluted</b> | <b>92,377,817</b> | 84,996,713        |
| Number of options excluded   | 12,625,000        | 2,235,000         |
| Number of warrants excluded  | 2,750,000         | 2,750,000         |
| Number of shares from conversion of New Promissory Notes excluded                      | 10,092,813        | 10,614,584        |
| <b>Net loss attributable to shareholders - Basic and Diluted</b>                       | <b>\$ (48)</b>    | <b>\$ (8,627)</b> |
| <b>Weighted Average Basic and Diluted Loss Per Share</b>                               | <b>\$ (0.00)</b>  | <b>\$ (0.10)</b>  |

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The effect of adjustments to the weighted average number of common shares would be anti-dilutive when the Company incurs losses. The table above provides the weighted average number of common shares on a diluted basis for periods where losses are incurred for information only.

### 20. SHARE-BASED PAYMENTS

The Company's share-based payment arrangements are described below.

#### **Share Bonus Plan**

The terms of the Share Bonus Plan are set out in Note 18.

#### **Share purchase warrants (equity-settled)**

The 2,750,000 Warrants issued on March 3, 2016, pursuant to the Senior Secured Debt, may be settled cashless and are, accordingly, classified as debt (Note 14) and expired on January 31, 2018.

#### **Stock Option Plan (equity-settled)**

The Company has a Stock Option Plan to encourage ownership of its common shares by key management personnel (directors and executive management), employees and consultants, and to provide compensation for certain services. The terms of the Stock Option Plan provide that the directors have the right to grant options to acquire common shares of the Company at not less than the closing market price of the common shares on the day preceding the grant. No compensation is recognized when options are exercised. The number of common shares reserved for issuance is not to exceed 15% of the aggregate number of common shares issued and outstanding (calculated on a non-diluted basis) from time to time.

As at December 31, 2017, the Company had 1,605,645 common shares available for the granting of future options (2016 – 11,620,645 common shares). Options are exercisable at the closing market price of the common shares at the date prior to grant. The Company does not have any cash-settled transactions. The terms and conditions relating to the grants of the Stock Option Plan are as follows:

- Options issued during the year and granted to executive management, consultants and employees have a maximum term of five years and are equity-settled. Of the options granted, 50% vest immediately, while the remaining options are exercisable after one year.
- Options issued during the year and granted to directors have a maximum term of five years and are equity-settled. All options granted vest immediately.
- All options are to be settled by physical delivery of common shares.

#### **Stock Option Plan**

The number and weighted average exercise prices of options are as follows:

| (amounts in Canadian dollars)<br>Years ended December 31, | Number of options  |           | Weighted average exercise price |         |
|---|--------------------|-----------|---------------------------------|---------|
|   | 2017               | 2016      | 2017                            | 2016    |
| <b>Outstanding as at beginning of the year</b>            | <b>2,235,000</b>   | 2,683,000 | <b>\$ 0.49</b>                  | \$ 0.58 |
| Granted   | <b>12,900,000</b>  | -         | <b>\$ 0.05</b>                  | \$ -    |
| Expired   | <b>(300,000)</b>   | (448,000) | <b>\$ 0.50</b>                  | \$ 1.05 |
| Cancelled   | <b>(1,210,000)</b> | -         | <b>\$ 0.49</b>                  | \$ -    |
| Surrendered   | <b>(1,000,000)</b> | -         | <b>\$ 0.05</b>                  | \$ -    |
| <b>Outstanding as at end of the year</b>                  | <b>12,625,000</b>  | 2,235,000 | <b>\$ 0.07</b>                  | \$ 0.49 |
| <b>Exercisable as at end of the year</b>                  | <b>9,175,000</b>   | 2,235,000 | <b>\$ 0.08</b>                  | \$ 0.49 |

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| As at December 31,                                 | Number of options outstanding |           | Weighted average remaining contractual life (years) |      |
|--|-------------------------------|-----------|---|------|
|  | 2017                          | 2016      | 2017  | 2016 |
| <b>Range of exercise prices</b> (Canadian dollars) |                               |           |   |      |
| \$0.05 to \$0.06                                   | 11,900,000                    | -         | 4.19  | -    |
| \$0.30 to \$0.50                                   | 367,000                       | 1,397,000 | 0.50  | 1.04 |
| \$0.55   | 103,000                       | 213,000   | 1.10  | 2.09 |
| \$0.70 to \$1.10                                   | 255,000                       | 625,000   | 1.55  | 2.55 |
|  | <b>12,625,000</b>             | 2,235,000 | <b>4.00</b>   | 1.60 |

During 2017, the Company recorded \$444,000 (2016 - \$nil) in share-based payments upon the vesting of options. As at December 31, 2017, an additional \$22,000 (2016 - \$nil) in share-based payments remain to be recognized up until May 2018. Options outstanding at December 31, 2017 expire between May 2018 and June 2022.

The grant-date fair values of share-based payments were measured based on the Black-Scholes option pricing model. The inputs used in the measurement of the fair values at grant dates during 2017 were as follows:

| For the year ended December 31,  | 2017                     |
|----------------------------------|--------------------------|
| Fair values                      | CAD\$0.047 to CAD\$0.057 |
| Share prices at valuation dates  | CAD\$0.05 and CAD\$0.06  |
| <b>Assumptions</b>               |                          |
| Exercise price                   | CAD\$0.05 and CAD\$0.06  |
| Expected volatilities            | 169.48% to 169.73%       |
| Expected remaining terms (years) | 5                        |
| Expected dividends               | -                        |
| Risk-free interest rates         | 0.88% to 1.10%           |

### Share purchase warrants

The number and weighted average exercise prices of warrants are as follows:

| (in Canadian dollars)                                      | Date Issued   | Life (mths) | Number of warrants |           | Weighted average exercise price |         |
|--|---------------|-------------|--------------------|-----------|---------------------------------|---------|
|  |               |             | 2017               | 2016      | 2017                            | 2016    |
| <b>As at December 31,</b>                                  |               |             |                    |           |                                 |         |
| <b>Issued and cancelled pursuant to private placements</b> |               |             |                    |           |                                 |         |
| Amended Warrants   | June 3, 2015  | 24          | 2,575,000          |           |                                 |         |
| Amended Warrants cancelled                                 | March 3, 2016 |             | (2,575,000)        |           |                                 |         |
| Warrants   | March 3, 2016 | 23          | <b>2,750,000</b>   | 2,750,000 | \$ 0.25                         | \$ 0.25 |
| <b>Outstanding as at end of the year</b>                   |               |             | <b>2,750,000</b>   | 2,750,000 | <b>\$ 0.25</b>                  | \$ 0.25 |

The life of all warrants above, are shown in number of months from issue date. The Amended Warrants and Warrants may be settled without cash and are, accordingly, classified as debt rather than as a component of contributed surplus. Refer to Note 14 for more details on the issuance of warrants related to the Senior Secured Debt. Subsequent to December 31, 2017, the Warrants expired unexercised on January 31, 2018.

## Notes to the Consolidated Financial Statements

(all tabular amounts in thousands of United States dollars, except common share and per share information)

### 21. FINANCE INCOME AND FINANCE COSTS

| Years ended December 31,   | 2017              | 2016            |
|--|-------------------|-----------------|
| Change in value of conversion options under Debt Restructuring Agreement | \$ 76             | \$ 186          |
| Gain on Debt Restructuring Agreement                                     | -                 | 2,545           |
| Change on the value of Participating Interest                            | 404               | 769             |
| Gain on sale of Partnership  | -                 | 283             |
| Other  | 8                 | -               |
| <b>Finance income</b>  | <b>488</b>        | <b>3,783</b>    |
| Interest expense on loans  |                   |                 |
| Accrued and/or cash settled  | 1,617             | 1,422           |
| Amortization of loan fees  | 25                | 21              |
| Amortization of embedded derivatives                                     | 260               | 340             |
| Net foreign exchange loss  | 65                | 43              |
| Other  | 31                | 65              |
| <b>Finance costs</b>   | <b>1,998</b>      | <b>1,891</b>    |
| <b>Net Finance (Costs) Income</b>  | <b>\$ (1,510)</b> | <b>\$ 1,892</b> |

### 22. INCOME TAXES

The combined Canadian tax rate reflects the federal and provincial tax rates for each applicable year. A reconciliation of the combined Canadian tax rate to the Company's effective rate of income tax is as follows:

| Years Ended December 31,                   | 2017              | 2016            |
|--|-------------------|-----------------|
| Loss before taxes                          | \$ (2,946)        | \$ (4,818)      |
| Combined Canadian tax rate                 | 27%               | 27%             |
| Income tax recovery at combined rate       | \$ (795)          | \$ (1,301)      |
| Non-deductible amounts                     | 179               | 117             |
| Non-taxable amounts                        | 2                 | (687)           |
| Taxable income from Partnership            | -                 | 1,699           |
| Change in deferred tax assets unrecognized | 52                | 1,292           |
| Effect of change in tax rates and other    | (2,336)           | 2,693           |
| <b>Income Tax (Recovery) Expense</b>       | <b>\$ (2,898)</b> | <b>\$ 3,813</b> |

In 2017, the Company confirmed that its election to use US dollars as its functional currency for income taxes had been received and processed. As a result, the Company recorded a tax recovery of \$2,898,000 mainly due to foreign exchange, to adjust the rate used to convert is various tax pools from Canadian dollars to US dollars. The change has been treated as a change in accounting estimate. The income tax expense of \$3,813,000 in 2016 is mainly a result of the significant taxable income generated on the sale of the Partnership. Certain components of finance income and finance costs are not taxable and their volatility has an apparent effect on the effective income tax rate.

### 23. OPERATING SEGMENT

#### Reporting Segment

The Company is engaged in the exploration, evaluation and development of properties for the mining and production of nickel and associated products; since January 1, 2014, it also has been a producer and supplier of premium frac sand from its 7P Plant. Accordingly, the Company has three reporting segments: Corporate, Exploration and Development, and Frac Sand.

The Corporate segment operates to support the Company's activities, including exploration and development

## Notes to the Consolidated Financial Statements

(all tabular amounts in thousands of United States dollars, except common share and per share information)

projects and the frac sand business.

Senior management makes decisions with respect to Exploration and Development by considering exploration and development potential and results on a project basis. The exploration and development projects are all located in Canada. Any applicable amounts relating to such projects will continue to be capitalized to the relevant project as either *Exploration and evaluation projects* or *Mine property and development project* on the consolidated balance sheets.

The Frac Sand segment is managed and operated by Victory Silica's executives and employees, although the business and operating assets are part of Victory Nickel (refer also to Note 25). The segment is located in Canada, although raw materials purchases are sourced from the United States.

The following tables provide information on the assets of the Company's segments:

| As at December 31,          | 2017             | 2016             |
|-----------------------------|------------------|------------------|
| <b>Canada</b>               |                  |                  |
| Corporate                   | \$ 2,020         | \$ 1,863         |
| Exploration and Development | 43,714           | 43,692           |
| Frac Sand                   | 4,858            | 5,803            |
| Intersegment elimination    | (1,502)          | (1,443)          |
| <b>Total Assets</b>         | <b>\$ 49,090</b> | <b>\$ 49,915</b> |

There have been no changes in the reportable segments or the treatment of segmented assets and revenues during 2017 and 2016.

| Year ended December 31, 2017                  | Corporate      | Exploration and<br>Development | Frac Sand       | Total          |
|---|----------------|--------------------------------|-----------------|----------------|
| <b>Revenues</b>                               | \$ -           | \$ -                           | \$ 879          | \$ 879         |
| Cost of goods sold                            | -              | -                              | (690)           | (690)          |
| <b>Gross margin</b>                           | -              | -                              | 189             | 189            |
| <b>Operating expenses</b>                     |                |                                |                 |                |
| General and administrative                    | (340)          | (32)                           | (219)           | (591)          |
| Share-based payments                          | (444)          | -                              | -               | (444)          |
| Amortization of property, plant and equipment | (1)            | (3)                            | (586)           | (590)          |
| <b>Operating loss</b>                         | <b>(785)</b>   | <b>(35)</b>                    | <b>(616)</b>    | <b>(1,436)</b> |
| Finance income                                | 488            | -                              | -               | 488            |
| Finance costs                                 | (1,998)        | -                              | -               | (1,998)        |
| <b>Net finance costs</b>                      | <b>(1,510)</b> | -                              | -               | <b>(1,510)</b> |
| <b>Loss before income taxes</b>               | <b>(2,295)</b> | <b>(35)</b>                    | <b>(616)</b>    | <b>(2,946)</b> |
| Income tax recovery                           | 2,898          | -                              | -               | 2,898          |
| <b>Net loss for the year</b>                  | <b>\$ 603</b>  | <b>\$ (35)</b>                 | <b>\$ (616)</b> | <b>\$ (48)</b> |

## Notes to the Consolidated Financial Statements

(all tabular amounts in thousands of United States dollars, except common share and per share information)

| Year ended December 31, 2016                    | Corporate  | Exploration and<br>Development | Frac Sand  | Total      |
|---|------------|--------------------------------|------------|------------|
| Revenues  | \$ -       | \$ -                           | \$ 100     | \$ 100     |
| Cost of goods sold                              | -          | -                              | (644)      | (644)      |
| Gross margin                                    | -          | -                              | (544)      | (544)      |
| Operating expenses                              |            |                                |            |            |
| General and administrative                      | (559)      | (25)                           | (267)      | (851)      |
| Amortization of property, plant and equipment   | (1)        | (3)                            | (607)      | (611)      |
| Writedown of exploration and evaluation project | -          | (4,700)                        | -          | (4,700)    |
| Operating loss                                  | (560)      | (4,728)                        | (1,418)    | (6,706)    |
| Finance income                                  | 3,783      | -                              | -          | 3,783      |
| Finance costs                                   | (1,891)    | -                              | -          | (1,891)    |
| Net finance income                              | 1,892      | -                              | -          | 1,892      |
| Income (loss) before income taxes               | 1,332      | (4,728)                        | (1,418)    | (4,814)    |
| Income tax expense                              | (3,813)    | -                              | -          | (3,813)    |
| Net loss for the year                           | \$ (2,481) | \$ (4,728)                     | \$ (1,418) | \$ (8,627) |

### 24. RELATED PARTIES AND MANAGEMENT AGREEMENT

#### Related Party Balances and Transactions

Short-term employee benefits provided by the Company to key management personnel include salaries, directors' fees, statutory benefit contributions, paid annual vacation and paid sick leave as well as non-monetary benefits such as medical care. In addition to short-term employee benefits, the Company may also issue options and common shares as part of the Stock Option Plan and Share Bonus Plan (Notes 20 and 18). Payables to key management personnel generally relate to director's fees, consulting fees and expense reimbursements. Balances and transactions with related parties as at and for the years ended December 31, 2017 and 2016 are shown in the following tables:

| As at December 31,                             | 2017   | 2016   |
|--|--------|--------|
| <b>Balances Outstanding</b>                    |        |        |
| Debt due to key management personnel           | \$ 318 | \$ 280 |
| Other payables due to key management personnel | 173    | 160    |
|  | \$ 491 | \$ 440 |

Key management personnel compensation is comprised of:

| Years ended December 31,     | 2017   | 2016   |
|------------------------------|--------|--------|
| Short-term employee benefits | \$ 362 | \$ 371 |
|                              | \$ 362 | \$ 371 |

### 25. COMPANY ENTITY

#### Significant Subsidiary - Victory Silica

On June 19, 2012, the Company announced the creation of Victory Silica to establish the Company as a supplier of premium frac sand, prior to commencing frac sand sales from the Minago project. Victory Silica manages the frac sand business on behalf of the Company.

| As at December 31,         | 2017  | 2016  |
|----------------------------|-------|-------|
| <b>Victory Silica Ltd.</b> |       |       |
| Current Assets             | \$ 7  | \$ 20 |
| Current Liabilities        | \$ 37 | \$ 33 |





**VICTORY NICKEL INC.**

**MANAGEMENT'S DISCUSSION AND ANALYSIS  
FOR THE YEARS ENDED  
DECEMBER 31, 2017 AND 2016**

**DATED APRIL 16, 2018**

**VICTORY NICKEL INC.**  
**MANAGEMENT'S DISCUSSION AND ANALYSIS**  
**For The Years Ended December 31, 2017 and 2016**

The following discussion of the results of operations, financial condition and cash flows of Victory Nickel Inc. ("Victory Nickel" or the "Company") prepared as of April 16, 2018 consolidates management's review of the factors that affected the Company's financial and operating performance for the years ended December 31, 2017 and 2016, and factors reasonably expected to impact on future operations and results. This discussion is intended to supplement and complement the Company's audited consolidated financial statements for the years ended December 31, 2017 and 2016 (the "2017 Audited Consolidated Financial Statements") and the notes thereto, which were prepared in accordance with International Financial Reporting Standards ("IFRS").

Certain information and discussion included in this management's discussion and analysis ("MD&A") constitutes forward-looking information. Readers are encouraged to refer to the cautionary notes contained in the section Forward-Looking Statements at the end of this MD&A.

The 2017 Audited Consolidated Financial Statements are available at [www.sedar.com](http://www.sedar.com) and at the Company's website [www.victorynickel.ca](http://www.victorynickel.ca). All amounts disclosed are in United States dollars ("US\$" or "US dollars") unless otherwise stated as Canadian dollars ("CAD\$") or Australian dollars ("AU\$"). All tabular amounts are in thousands of US dollars.

Common shares of the Company trade on the Canadian Securities Exchange ("CSE") under the symbol NI as of February 22, 2016. Prior to that date, common shares of the Company traded on the Toronto Stock Exchange ("TSX").

**COMPANY OVERVIEW**

The Company was formed on February 1, 2007 as an exploration and development mineral resource company and was primarily engaged in the acquisition, exploration, evaluation and development of nickel projects and associated products in Canada. Victory Nickel owns 100% of four advanced sulphide nickel projects: the Minago, Lynn Lake (under option with Corazon Mining Ltd. ("Corazon"), an Australian public company (ASX: CZN)) and Mel projects in Manitoba, and the Lac Rocher project in Québec. The Minago project is the Company's most advanced nickel project. A feasibility study on the Minago Project ("Minago FS") was completed and the results were announced in December 2009. The Environmental Impact Study ("EIS") was filed in May 2010 and receipt of the Environmental Act Licence ("EAL") was announced in August 2011. Subsequent improvements to the project were announced in June 2010 and July 2011. In April 2014, the Company announced the filing of an amendment to the EAL to relocate the permitted Minago tailings facilities such that it will not interfere with potential nickel resources and should also reduce operating costs. Consultations with First Nations by the government of Manitoba are ongoing. On completion, it is expected that the government of Manitoba will issue the requested amendment to the existing EAL.

The Company's decision to enter the frac sand business was initially based on the need to generate cash flow and the desire to highlight the value of frac sand, which can be sold into the oil & gas industry, as a co-product at its Minago nickel project in Manitoba. Based on the Minago FS, approximately 11 million tonnes of frac sand exist within the Minago pit footprint. The pit footprint represents only a small portion of the Minago property. The frac sand is a significant contributor to the economics of the Minago project.

During 2014, Victory Nickel became a producer and supplier of premium Wisconsin frac sand from its frac sand plant (the "7P Plant") located near Seven Persons, Alberta, approximately 18 kilometres southwest of Medicine Hat, Alberta. High-quality Northern White frac sand is sourced from Wisconsin, USA, through the Company's wholly-owned subsidiary Victory Silica Ltd. ("Victory Silica"). Northern White occurs predominantly in the US Midwest and generally exceeds American Petroleum Institute ("API") specifications for frac sand. For this reason, it is a highly-desirable and preferred frac sand. Frac sand is used as a proppant to enhance recovery from oil and gas wells. The 7P Plant comprises a wash plant with a nominal capacity of approximately 120,000 tons per annum ("tpa") and a fully-operational dry plant with a nominal capacity of 500,000 tpa. The Company established itself as a frac sand producer by acquiring concentrated sand in Wisconsin, USA, washing it prior to shipment to the 7P Plant for processing into four main categories of finished frac sand products.

Crucial to the success of its frac sand operations is the Company's ability to build a solid customer base within an economic distance of its production facilities or to acquire/build additional frac sand processing facilities to serve additional markets. The Company was able to establish itself as a preferred supplier in the areas around Medicine Hat, Alberta

through spot-market sales and short-term contracts. The Company's 7P Plant is located in close proximity to oil and gas producing plays in Alberta, BC, Saskatchewan and North Dakota, allowing customers to purchase sand FOB the 7P Plant and use their own trucks to deliver to the wellhead or, alternatively, to have the Company deliver frac sand directly to the wellhead. A small portion of finished sand is delivered by rail.

To ensure long-term supply of concentrated sand, the Company entered into an option to acquire a 100% interest in a frac sand land package totalling over 300 acres in Trempeleau County, Wisconsin, USA (the "Bear Coulee Property"). The option is valid for six months from receipt of permits with two equivalent extensions available under certain circumstances. Prior to production the Company will be required to pay \$40,000 per annum as an advance royalty on the initial 20,000 tons of sand production. Once the Bear Coulee Property is in production, the Company will be required to pay a royalty of \$2.00 per ton of frac sand sold from the property. In February 2015, the Company announced that a resource estimate of approximately 11 million tons of sand has been completed by Summit Envirosolutions Inc. on the Bear Coulee Property and was incorporated into a National Instrument 43-101 technical report.

The Company's board of directors approved the construction of a wash plant in Wisconsin or Minnesota and has considered building a second 1,000,000 tpa dry plant in or near Winnipeg, Manitoba. Market conditions necessitate the deferral of any such construction until more certainty returns to the oil and gas sector.

Due to the sudden drop in the price of oil during late 2014, drilling activity by oil and gas exploration and production ("E&P") companies decreased significantly, and sustained relatively low oil and gas prices continued to negatively affect frac sand demand through 2016 and into 2017. The drop in sales required a temporary suspension in production at the 7P Plant in April 2015. The 7P Plant operates on an as-needed basis only (see Going Concern below). In March 2017, the Company announced that due to the current increasing market demand for frac sand, it has restarted the dry plant at its 7P Plant. In October 2017, the Company announced that it had completed the refurbishment of its frac sand wash plant at 7P Plant that is now operational, enhancing the ability to produce and sell frac sand.

### **Going Concern**

The 2017 Audited Consolidated Financial Statements have been prepared using Generally Accepted Accounting Principles ("GAAP") 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. As at December 31, 2017, the Company had a working capital deficiency of \$6,406,000, calculated as current assets less current liabilities, an increase from a working capital deficiency of \$5,558,000 as at December 31, 2016. At December 31, 2017, the debts of \$6,500,000 were the largest factor in the Company's working capital deficiency. At December 31, 2017, the Company was in default on all unsecured debt and related interest, as described in Note 14 of the 2017 Audited Consolidated Financial Statements.

The Company's main assets are its nickel projects. Minago, the most advanced of its projects is permitted and ready for development. However, development costs are in excess of \$500,000,000 and given the current price of nickel, it is unlikely that financing for this project will be available in the near future. If the Company is unable to finance and develop these projects, the potential recovery via sale of these projects maybe below the current carrying amounts. Given the defaults on various loans discussed below, there is an increased risk that the Company's creditors could force the Company to liquidate its core assets under less than favourable terms.

On April 14, 2015, the Company announced that operations at the 7P Plant were temporarily suspended until the demand for frac sand improved; this temporary suspension was due to the dramatic decrease in energy pricing that began in 2014. Since March 2015, sales have been significantly below rates achieved during 2014 and continue well below the level required to generate positive cash flow. The 7P Plant was restarted in March 2017 and continues to operate on an as-needed basis in order to fulfil customer needs. 2017 has shown some improvement in the slowdown in drilling activity due to the severe drop in the price of oil, but sales have yet to recover to levels that would generate positive cash flow. In October 2017, the Company announced that it had completed the refurbishment of its frac sand wash plant at the 7P Plant. The wash plant is now operational, enhancing the ability to produce and sell frac sand. 2017 has shown some improvement in the slowdown in drilling activity due to the severe drop in the price of oil, but sales have yet to recover to levels that would generate positive cash flow.

The near-term outlook in the frac sand market remains unclear. The US dollar continues to impact demand for high-quality Wisconsin sand in Canada as the price for domestic sand has dropped and service companies appear satisfied with using lower-quality domestic sand, because of the price differential caused mainly by the exchange rate. As the Company's inventory is Wisconsin frac sand, this will continue to stress the Company's liquidity until such time as the market demand recovers and operations can resume on a consistent basis.

Cash flows from frac sand sales in 2017 were sufficient to cover operating costs but not sufficient to pay financing costs and the Company was not able to make the majority of its interest payments due during 2017 and 2016.

In March 2016, the Company announced that it had completed the restructuring of the SPA Amended Loan (as defined and outlined in Note 14 of the 2017 Audited Consolidated Financial Statements), which included terms of a debt restructuring package (the “Debt Restructuring Agreement”) for the holders of the promissory convertible notes (the “Promissory Convertible Notes”) and the Company’s trade creditors. The SPA Amended Loan was increased to \$5,500,000 and the maturity date extended to January 31, 2018 (the “Senior Secured Debt”). On December 31, 2017, the Senior Secured Debt was increased by the amount of unpaid interest to \$7,050,000 and the maturity date was extended to July 31, 2019. The Senior Secured Debt is in default, but the lender of the Senior Secured Debt (the “Secured Lender”) has provided a forbearance agreement.

Pursuant to the terms of the Senior Secured Debt, the Company is prevented from making payments under outstanding unsecured debt until the Senior Secured Debt is repaid. Only a portion of the interest due under the Senior Secured Debt was paid in 2017 and 2016. The Secured Lender provided a forbearance agreement for the balance of the accrued interest and made short term advances to cover non-discretionary costs, such as equipment lease payments. An advance on December 28, 2017 is included on other current loans, while advances in 2016 were paid during 2016. Barring a significant improvement in the sales of frac sand, the Company is unlikely to be able to repay the Senior Secured Debt in full when it matures in July 2019. The Company’s ability to make the required interest payments in 2018 is also in doubt and dependent upon frac sand sales. To date, the Company’s Secured Lender has communicated its commitment to ensuring the protection of the Company’s core assets, including the advances noted above and the forbearance agreement. Should the support of the Secured Lender change, the going concern assumption would be in doubt.

All of the Promissory Convertible Note holders participated in the Debt Restructuring Agreement, except for one holder of a \$3,000,000 Promissory Convertible Note (the “Outstanding Note”). In March 2016, the Company announced that it had received notice that the holder of the Outstanding Note had filed a statement of claim concerning non-payment of principal and interest. The Company has reviewed the statement of claim with legal counsel to assess its impact on the Company and has concluded that there is no significant impact on the status of the Company’s debt. The Outstanding Note matured in July 2016 and the Company has been unable to repay the amounts owing and interest payments due, which has resulted in the Company defaulting on the note.

On March 7, 2016, March 31, 2016 and June 7, 2016, the Company announced that it had completed private placements with certain of its unsecured lenders, trade creditors and management in settlement of the Promissory Convertible Notes and debt owed, as per the terms of the Debt Restructuring Agreement, as described in Note 14 of the 2017 Audited Consolidated Financial Statements. The Company has not paid interest payments due on its New Promissory Convertible Notes as described below, which has resulted in the Company defaulting on its New Promissory Convertible Notes.

In June 2016, the Company sold its non-core partnership interest (the “Partnership”) for net proceeds of CAD\$358,000. The net proceeds were used to fund working capital requirements. In October 2016, the Company sold a portion of its marketable securities for net proceeds of AU\$15,000. To the extent required, the Company will continue to sell non-core assets to fund its working capital requirements.

The ability of the Company to continue as a going concern is heavily dependent on the continued support of its lenders and the frac sand market improving, both in demand and in price, and the Company’s ability to resume operations at its 7P Plant. In addition to the liquidity and solvency uncertainties described above, the ability to resume full operations at the 7P Plant will require additional financing. In order to resume purchasing and shipping supplies of frac sand and full operations at the 7P Plant, the Company will require additional working capital. As noted, the Company’s Secured Lender has been supportive to date. However, there are no assurances that the Company will be able to obtain the working capital to resume operations at the level sufficient to generate cash flows to repay its outstanding obligations.

The Company has cut non-essential costs in an effort to reduce operating losses and has deferred payments wherever possible. During 2017 and 2016, the Company, with the agreement of its Secured Lender, sold non-core assets, including marketable securities and the Partnership, to provide operating funds. However, without an injection of capital and/or until the demand for frac sand returns to pre-2015 levels, the Company will not be able to meet its outstanding obligations or any new obligations as they become due. The defaults on the Company’s existing obligations add to the challenge of obtaining additional capital.

There can be no assurance that the Company will be able to restructure its debt further and/or recapitalize, and there is no certainty as to what further steps, if any, the secured and unsecured lenders may take. The date, the Secured Lender has been supportive and has provided limited working capital needed to protect the Company's core assets, and management and the board of directors have reduced and/or deferred salaries and director fees until business recovers, but there is no certainty that this will continue. Management salary reductions and/or deferrals put the company at risk of being unable to retain key personnel.

In addition to the above liquidity issues, the Company is subject to the risks and challenges experienced by other companies at a comparable stage. These risks include, but are not limited to, continuing losses, a continued prolonged slowdown in the frac sand market which would limit the Company's ability to generate cash flow from the 7P Plant, dependence on key individuals and the ability to secure adequate financing or to complete corporate transactions to meet the minimum capital required to successfully fund its projects and operating expenses.

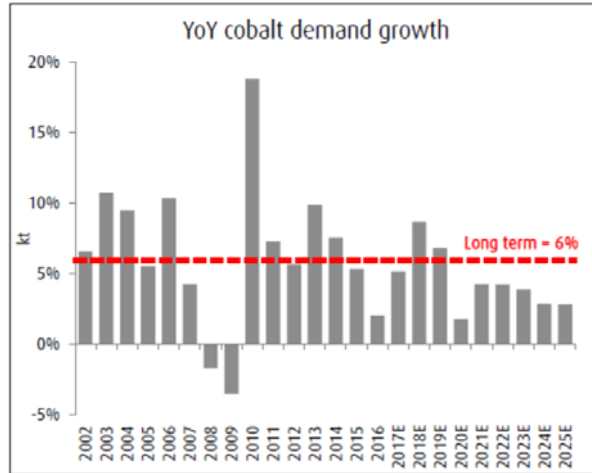
None of the Company's mining projects have commenced commercial production and, accordingly, the Company is dependent upon debt or equity financings, the optioning and/or sale of resource or resource-related assets or interests, exploration results which have the potential for the discovery of economically-recoverable reserves and resources, and/or the ability to generate sufficient cash flow from its other operating activities for its funding. Development of the Company's current nickel mining projects to the production stage will require significant financing. Given the current economic climate, including the low nickel price, and the Company's existing liquidity challenges, the ability to raise sufficient funds will be difficult.

Should the Company not be able to overcome the risks described in this section, the carrying value of the Company's assets would be subject to material adjustment and, in addition, other adjustments may be necessary to the 2017 Audited Consolidated Financial Statements should such adverse events impair the Company's ability to continue as a going concern as contemplated under GAAP. There is no certainty that the Company will be able to generate sufficient cash to fund its activities including debt servicing, project expenditures and corporate costs. These conditions indicate the existence of a material uncertainty that may cast significant doubt about the Company's ability to continue as a going concern. Failure to continue as a going concern would require that the Company's assets and liabilities be restated on a liquidation basis, which would differ significantly from the going concern basis.

## OUTLOOK

Victory Nickel is a unique minerals company. Unique in that it has one of Canada's largest undeveloped permitted sulphide nickel resources at its Minago project in Manitoba. Unique in that all of the resources at its three nickel projects are sulphide nickel giving it one of the largest sulphide nickel inventories in Canada. Unique in that at Minago frac sand is a significant co-product of nickel production. And unique in that three of its most significant value drivers – nickel, frac sand and cobalt – play crucial roles in the existing and emerging energy markets.

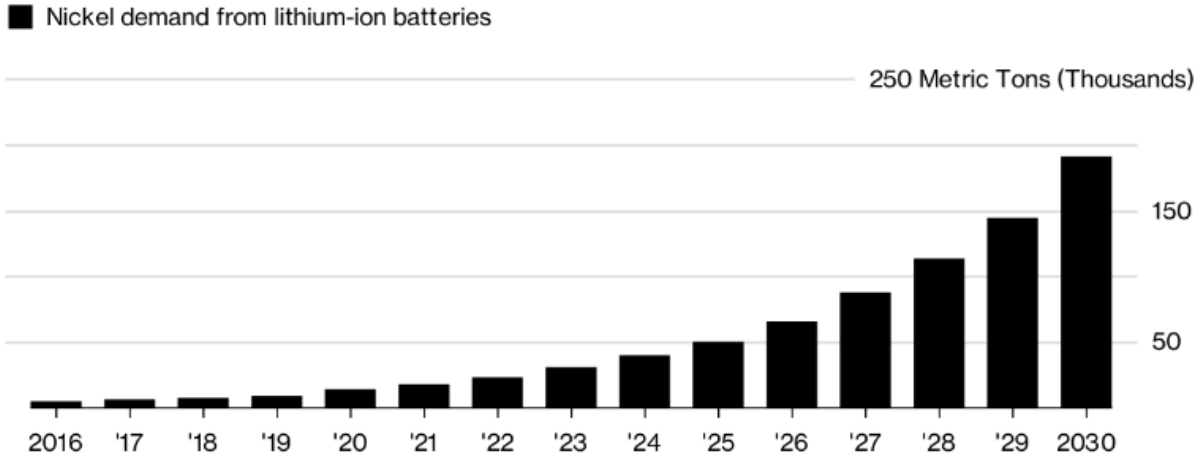
While frac sand has long been known as a key component in improving overall economics in the oil and gas industry, nickel's presence as an "Energy Metal" is just now coming to prominence with the acceleration of worldwide demand for electric vehicles ("EV"). Globally increasing demand for rechargeable batteries due to historic growth in the smartphone market and now increasingly in EVs has led to dramatically growing cobalt demand. According to BMO Capital Markets the demand for cobalt is expected to exceed 100kt in 2018, growth in excess of 150% since 2000, and EVs represent 40% of total cobalt demand by 2025, overtaking portable electronics in terms of cobalt demand by 2022.



Source: CRU, CDI, BMO Capital Markets

Demand growth has led to recent cobalt pricing in excess of \$43.00/lb, dramatically higher than the \$27.73/lb price used in the Minago FS, and BMO Capital Markets states: “a doubling of the cobalt spot price over the coming couple of years is not out of the question.” At the current price \$42.00/lb, the Minago FS indicates that the Minago mine produces approximately \$188,000,000 of cobalt in concentrate over the approximate eight-year mine life making it a significant by-product of nickel production.

According to Bloomberg, demand for nickel is forecast to increase dramatically through 2030 (see graph below), driven in large part by rising sales of EVs and the fact that EV batteries typically contain more nickel than they do lithium.

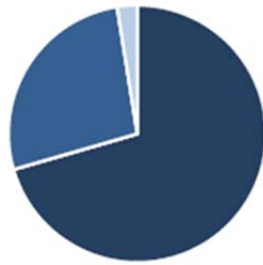


Source: Bloomberg New Energy Finance

UBS concurs, estimating that in a world using only EVs, the increase in sulphide nickel demand relative to today’s global market would be 118%. UBS goes on to point out that as EV technology continues to improve, so too will demand for nickel. Today’s nickel-manganese-cobalt (“NMC”) cathodes used in EVs use a 1:1:1 ratio between nickel, manganese and cobalt. By 2021 this materials mix is expected to be optimized at 8:1:1.

In its report “*Nickel – A Class of its Own*” published on November 7, 2017, Canaccord Genuity agrees, forecasting that in the 2020s battery demand for nickel will rise ~6.5x times and comprise ~14% of nickel demand in 2025.

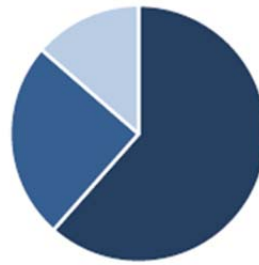
Figure 1: Nickel use, 2017e



■ Stainless Steel  
 ■ APFO (Alloy, Plating, Foundry, Others)  
 ■ Battery

Source: Canaccord Genuity estimates

Figure 2: Nickel use, 2025e

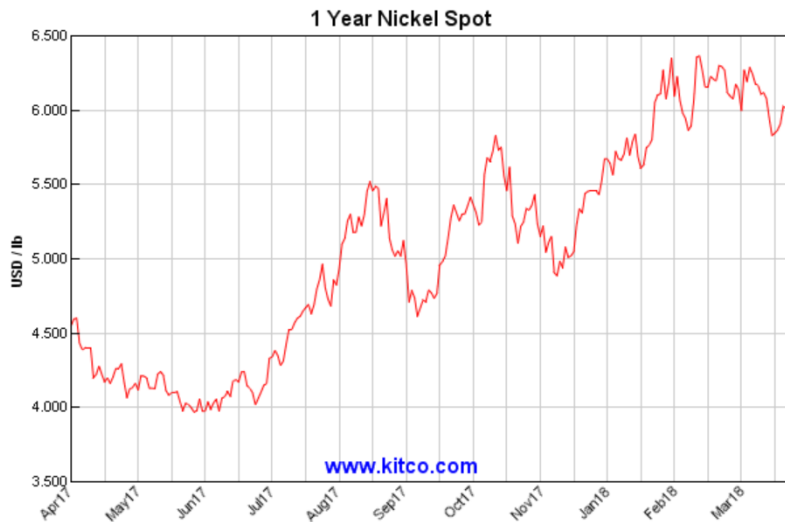


■ Stainless Steel  
 ■ APFO (Alloy, Plating, Foundry, Others)  
 ■ Battery

Source: Canaccord Genuity estimates

In addition, BMO, Canaccord and UBS concur that due to the quality requirements of battery producers the winners in this new demand environment will be **sulphide nickel** producers such as Victory Nickel's projects which, unlike laterite deposits, have an economic advantage in the competition for EV battery market share.

And nickel buyers are starting to take notice (see graph below).



With one of the largest in-situ sulphide nickel resources in Canada, situated in two of the world's top ten most favourable mining jurisdictions – Manitoba and Quebec – Victory Nickel is well positioned in both nickel and cobalt to take advantage of the significant market shift toward EVs.

The Minago FS was based on an open pit mining project with a nickel reserve of approximately 30 million tonnes to be mined over about eight years. Beneath the proposed pit exists another potential 30 million tonnes for potential future mining. Immediately to the north of the pit, the Company has identified an additional potential 30 million tonnes. The Minago project was permitted in 2011 and is shovel-ready. With the frac sand co-product credit, the C1 cost to produce a pound of nickel, is projected to be \$2.20 per pound. As at December 31, 2017, the long-term forecasted price by a third party was \$8 per pound of nickel. Using this price at an exchange rate of US\$0.775:CAD\$1.00 and other forecasted metal prices at December 31, 2017, the Internal Rate of Return ("IRR") of the Minago project based on the Minago FS was 19.35%. As at the date of this MD&A, the IRR is 13.34% (with no adjustments made to the frac sand market), based on current metal prices and the exchange rate, with the price per pound of nickel at \$6.41. The IRR reflected in the Minago FS is 22.4% and the breakeven price of nickel is \$3.80 per pound. The value of cobalt in nickel concentrate alone has increased to \$188,000,000 at the recent price of \$42.00 per pound.

Frac sand contributes approximately \$2.90 per pound of nickel based on the Minago FS, and therefore is a substantial contributor to the overall economics as projected in the Minago FS. Persistent weakness in worldwide nickel pricing in the early part of the decade, the resulting contraction in capital markets for nickel project financing, an estimated \$500,000,000 capital cost to build a nickel mine at Minago and a robust market for frac sand led the Company to evaluate alternatives to generate cash flow and also to prove the value of the frac sand co-product at Minago.

### *Frac Sand*

In 2012, the Company announced its intention to enter the frac sand business with a plan that was certainly considered very aggressive and a vision at best. That vision became a reality in 2014 when the Company completed construction and commissioning of its 7P Plant in Alberta.

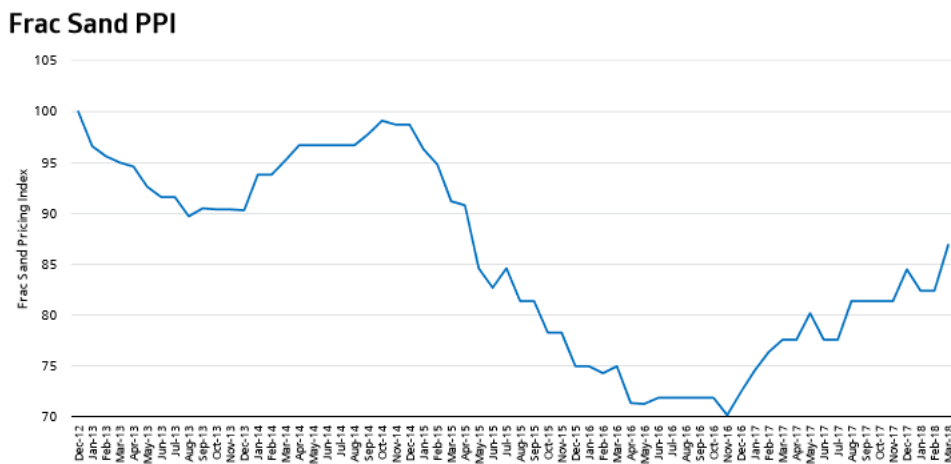
Choosing to enter the frac sand business was not without reason. The strong market fundamentals for frac sand suggested continuing growth of the industry, and new public information combined with strong peer group valuations indicated the potential for near-term cash flow. With an entry fee of approximately \$6,000,000 to build a frac sand processing facility, the risk was considered acceptable based on projected cash flows. Soon after commissioning, toward the end of 2014, the bottom fell out of the oil industry and the price of oil crashed from in excess of \$100.00 per barrel to below \$30.00 per barrel of oil. Except for a few short signs of recovery, the price of oil remained around the \$40.00 to \$50.00 level since that time until mid-2017 when it broke the \$50.00 price level and has continued to rise to in excess of \$71.00 today for Brent Crude. Whether this is an indication of bottoming out with a gradual recovery is uncertain. The price decrease is similar for natural gas.

As a result of the oil and gas price drop, drill rig utilization decreased substantially. In direct response to the declining utilization, E&P companies reduced, cancelled or deferred capital programs. All of this led to an unprecedented decline in the pricing of drilling and well completions, putting downward pressure on the price of frac sand.

During this period, E&P companies looked for ways to improve their economics by reducing costs and enhancing recoveries. Measures include lengthening of both lateral and horizontal drilling, increasing the number of stages per foot and using more sand per stage. These changes have led to an increase in frac sand intensity – using more sand per well – a trend that bodes well for frac sand consumption.

According to Credit Suisse, up to 2,000 pounds of sand per lateral foot is now being used in well completions. On average, each well completed in the US in 2017 required nearly 4,200 tons of frac sand. The demand for US proppant is projected to rebound to 73,000,000 tons in 2017, 30% higher than 2014 peak consumption of 56,000,000 tons and a 115% increase over the 34,000,000 tons consumed in 2016, according to Credit Suisse. Estimates of 2018 US frac sand demand range between 90,000,000 and 120,000,000 tons.

Not surprisingly, increased consumption, combined with a rising North American rig count – up 15% year-over-year at March 31 2018, has had a positive impact on frac sand pricing as demonstrated by the price index chart below.



Source: Bureau of Labor Statistics and Cowen and Company



For Victory Nickel, frac sand activity picked up during 2017 and continues to improve into the first quarter of 2018. Frac sand sales and pricing have shown improvement in 2017, however demand has been for the coarser fractions. As a result the Company has drawn down its inventory of coarser frac sand and is in the process of replenishing this inventory at the 7P Plant to ensure its ability to serve customers. To accomplish this, the Company completed the refurbishment of its existing wash plant at the 7P Plant. When the 7P Plant was acquired by the Company in 2012, the facilities included a wash plant and a dry plant. Since the acquisition, the Company had processed only washed sand concentrate purchased from Wisconsin through its dry plant and had never operated its wash plant. With the wash plant now operational, the Company was able to recover approximately 4,000 tons of high-quality Northern White Wisconsin frac sand that was spilled as a natural outcome of dry sand processing and which comprises the highest margin portion of inventory. An additional 14,000 tons is available for washing as soon as the weather improves.

The softness in the frac sand market over the past several years led to declining valuations of frac sand assets throughout North America. Management has been evaluating opportunities to take advantage of market opportunities to build its presence in the frac sand business by acquiring undervalued North American frac sand production assets that offer immediate potential to expand sales and open new markets, while at the same time being complementary to the Company's existing production activities. Management has identified potential acquisition targets and is now in discussions for financing to acquire one of these facilities. This acquisition would add another 1,000,000 tons of production capacity.

As discussed above, management is developing plans to implement strategies to take full advantage of a resurgent frac sand market. In addition, we remain confident that sulphide nickel demand will improve, such that not only the Minago nickel project can be developed, but that the Company's other nickel projects, Mel, Lac Rocher and Lynn Lake, can be advanced as potential producers.

The Company plans to participate in the turnaround in not only the oil and gas industry, but also the nickel industry and we thank our shareholders, lenders and suppliers for their continued patience and support.

## RESULTS OF OPERATIONS

| Year ended December 31, 2017                  | Corporate      | Exploration and<br>Development | Frac Sand       | Total          |
|---|----------------|--------------------------------|-----------------|----------------|
| <b>Revenues</b>                               | \$ -           | \$ -                           | \$ 879          | \$ 879         |
| Cost of goods sold                            | -              | -                              | (690)           | (690)          |
| <b>Gross margin</b>                           | -              | -                              | 189             | 189            |
| <b>Operating expenses</b>                     |                |                                |                 |                |
| General and administrative                    | (340)          | (32)                           | (219)           | (591)          |
| Share-based payments                          | (444)          | -                              | -               | (444)          |
| Amortization of property, plant and equipment | (1)            | (3)                            | (586)           | (590)          |
| <b>Operating loss</b>                         | <b>(785)</b>   | <b>(35)</b>                    | <b>(616)</b>    | <b>(1,436)</b> |
| Finance income                                | 488            | -                              | -               | 488            |
| Finance costs                                 | (1,998)        | -                              | -               | (1,998)        |
| <b>Net finance costs</b>                      | <b>(1,510)</b> | -                              | -               | <b>(1,510)</b> |
| <b>Loss before income taxes</b>               | <b>(2,295)</b> | <b>(35)</b>                    | <b>(616)</b>    | <b>(2,946)</b> |
| Income tax recovery                           | 2,898          | -                              | -               | 2,898          |
| <b>Net loss for the year</b>                  | <b>\$ 603</b>  | <b>\$ (35)</b>                 | <b>\$ (616)</b> | <b>\$ (48)</b> |

| Year ended December 31, 2016                     | Corporate  | Exploration and<br>Development | Frac Sand  | Total      |
|--|------------|--------------------------------|------------|------------|
| Revenues   | \$ -       | \$ -                           | \$ 100     | \$ 100     |
| Cost of goods sold                               | -          | -                              | (644)      | (644)      |
| Gross margin                                     | -          | -                              | (544)      | (544)      |
| Operating expenses                               |            |                                |            |            |
| General and administrative                       | (559)      | (25)                           | (267)      | (851)      |
| Amortization of property, plant and equipment    | (1)        | (3)                            | (607)      | (611)      |
| Writedown of exploration and evaluation project: | -          | (4,700)                        | -          | (4,700)    |
| Operating loss                                   | (560)      | (4,728)                        | (1,418)    | (6,706)    |
| Finance income                                   | 3,783      | -                              | -          | 3,783      |
| Finance costs                                    | (1,891)    | -                              | -          | (1,891)    |
| Net finance income                               | 1,892      | -                              | -          | 1,892      |
| Income (loss) before income taxes                | 1,332      | (4,728)                        | (1,418)    | (4,814)    |
| Income tax expense                               | (3,813)    | -                              | -          | (3,813)    |
| Net loss for the year                            | \$ (2,481) | \$ (4,728)                     | \$ (1,418) | \$ (8,627) |

### Overall

For the year ended December 31, 2017, the Company had a net loss of \$48,000 or a loss of \$0.00 per share (December 31, 2016 - \$8,627,000 or a loss of \$0.10 per share). The following narrative discusses the relevant operations of the Frac Sand and Exploration and Development segments first, and then addresses the corporate segment.

### Frac Sand Segment

Due to the decline in the price of oil beginning in 2014, demand for frac sand in the Company's target markets was under pressure throughout 2017 and 2016. The Company holds inventory in excess of 22,000 tons at the end of 2017 (2016 – 39,000 tons) at various stages of the process and made sales of 10,310 tons of various grades of frac sand during 2017 (2016 – 1,238 tons) by drawing down inventories, generating a gross margin of \$189,000 (2016 – \$544,000 loss). During 2017, ownership of 8,000 tons of sand stored in Wisconsin was transferred to the storage facilities in lieu of paying storage charges, resulting with a reduction in the Company's inventory balances. Inventory is valued at the lower of cost or net realizable value, and is being sold as the market recovers.

### Revenues

The Company recognized revenue on frac sand sales during 2017 aggregating \$879,000, or \$85.22 per ton, on sales of 10,310 tons (2016 - \$100,000, or \$80 per ton, on sales of 1,238 tons). Revenue includes periodic freight for sales delivered to customers. While sales and pricing are showing signs of improvement, the market has not improved sufficiently in the Company's target areas where it can generate positive cash flow sufficient to service debt.

### Cost of goods sold

The cost of goods sold includes the cost of concentrated sand purchased in Wisconsin, the cost of delivery to the 7P Plant including handling and trans-loading costs and the operating cost to dry and screen the concentrated sand into four main dry products. These costs are capitalized as a component of inventory on a normalized basis and are charged to cost of goods sold when title to the product passes to the customer. Cost of goods sold also includes any write-down or recovery of previous impairment of inventory values to the lower of cost or net realizable value.

The cost of goods sold was \$690,000 during 2017 (2016 - \$644,000), including an inventory recovery of previous impairment of \$495,000 (2016 – impairment write-down of \$517,000), as the Company revalued inventory to net realizable value and recorded finished inventory at the lower of cost or net realizable value. During 2017, the Company sold most of its 20/40 grade in finished goods inventory, requiring the start-up of the 7P Plant to replenish this particular grade of sand, in anticipation of a continued improvement in sales. The 7P Plant continues to operate on an as needed basis, resulting in higher operating costs per ton of product produced than what is expected on a continuous operating basis. The Company has reduced manpower to a skeleton crew sufficient to start production as demand returns on a consistent basis. The Company suspended deliveries of concentrated sand in 2015 and will resume deliveries once demand is sufficient to

utilize existing inventories at the 7P Plant. Finished goods inventory was revalued to the net realizable value of \$92.50 per ton (2016 - \$85.80 per ton) to reflect current market conditions.

Costs per ton are per dry ton, unless otherwise stated.

### **Gross margin**

The 7P Plant generated a gross margin in 2017 and a negative gross margin in 2016. The negative gross margin in 2016 was the result of a combination of price reductions and cost increases due to the low production level during the respective years. The 7P Plant continues to operate on an as-needed basis, resulting in higher operating costs per ton of product produced than what is expected on a continuous operating basis, while finished goods inventory is written-down to the lower of cost or net realizable value.

### **General and administrative and other costs**

General and administrative ("G&A") costs for the frac segment amounted to \$219,000 for the year ended December 31, 2017 (2016 - \$267,000). These costs include Victory Silica administration, marketing and logistics management. The Company reduced manpower to a skeleton crew and overhead sufficient to operate the 7P Plant as demand requires.

Amortization of property, plant and equipment of \$586,000 was recorded for the year (2016 - \$607,000), for items in use at the 7P Plant.

### **Net loss**

All of the above items combined to produce a net loss for the frac sand segment of \$616,000 for the year ended December 31, 2017 (2016 - \$1,418,000).

### **Exploration and Development Segment**

At December 31, 2016, the Company recorded an impairment of \$4,700,000 on its Lac Rocher property. No impairment was recorded during 2017. During 2017 and 2016, there were no pre-exploration expenditures.

In November 2014, the Company announced it had optioned the Lynn Lake project to Corazon. As part of that transaction, the Company received 40,000,000 shares of Corazon in April 2015. The shares were sold in 2016 for net proceeds of AU\$515,000.

### **Corporate Segment**

The corporate component of net loss for the year ended December 31, 2017 was income of \$603,000 (2016 - Loss of \$2,481,000), including operating expenses of \$785,000 (2016 - \$560,000), net finance costs of \$1,510,000 (2016 - net finance income of \$1,892,000) and an income tax recovery of \$2,898,000 (2015 - income tax expense of \$3,813,000). Operating expenses include \$444,000 non-cash share based payments in 2017 compared to \$nil in 2016.

G&A expenses were \$340,000 (2016 - \$559,000) as the Company has reduced its overhead due to the slowdown in the market for frac sands. These costs include statutory costs incurred as a public company, general investor relations expenses, consulting, travel, health benefits, salaries and director costs. Costs during 2016 were already reduced from the prior year, to reflect the market drop at that time.

### **Net finance income (costs)**

The Company considers financing activities, other than those related to equipment leased in the frac sand segment, to be part of the Corporate segment.

Finance income in 2017 was \$488,000 and was primary due to the change in the fair value of the estimated cash flows from the Participating Interest (as defined further below) of \$404,000 and the change in value of embedded derivatives of \$76,000. In 2016, finance income of \$3,783,000 was related to the gain on the Debt Restructuring Agreement of \$2,545,000, the change in the fair value of the estimated cash flows from the Participating Interest of \$769,000, the gain on the sale of the Partnership of \$283,000, and the change in value of embedded derivatives \$186,000.

The recent slowdown in demand and the losses incurred during 2017 and 2016 necessitated deferral for payment of the Participating Interest and resulted in a gain. The Company applied probability weightings of 50%, 25% and 25% as risk factors to varying levels of expected cash flows. The percentage participation in net cash flows under the Participating Interest is 52.16%. As at December 31, 2017 the carrying value of the Participating Interest was valued to \$529,000 (2016 - \$933,000) to take into account future expected cash flows based on current market information.

Finance costs were \$1,998,000 for the year ended December 31, 2017 (2016 - \$1,891,000). Cash and accrued interest expense was \$1,617,000 for the year ended December 31, 2017 (2016 - \$1,422,000). The increase in interest expense during 2017 compared with 2016 is mainly related to the compounding of interest outstanding on various debts.

During 2016, the Company issued several tranches of New Promissory Convertible Notes (as defined below). There are several elements of finance costs associated with these notes: accrued and cash-settled interest expense, non-cash amortization of loan fees, non-cash amortization of the embedded derivatives related to the value of the convertibility feature at inception, and the non-cash amortization of the present value discount on the New Promissory Convertible Notes. All amortizable elements are calculated using the effective interest rate method. As at December 31, 2017 the amortization of the embedded derivatives on the New Promissory Convertible Notes amounted to \$260,000 (2016 - \$340,000).

The embedded derivatives are calculated using the Black-Scholes option-pricing methodology and are a function of share price, the conversion price, risk-free interest rate, length of time to expiry and share price volatility as well as the US dollar exchange rate for loans denominated in US dollars, but convertible using a Canadian dollar price. All other things being equal, one would expect the value of the option to decline as time approaches the expiry date. However, because of the volatility of exchange rates and the Company's share price, this may not always be the case. The Secured Senior Debt does not contain an embedded derivative feature; however, the warrants which were issued therewith may be exercised on a cashless basis. The value of the warrants is considered to be debt rather than equity and changes in the fair value of the warrants is also recorded through net finance income or cost.

#### ***Income tax expense (recovery)***

The Company does not allocate income taxes between segments. In 2017, the Company confirmed that its election to use US dollars as its functional currency for income taxes had been received and processed. As a result, the Company recorded a tax recovery of \$2,898,000 mainly due to foreign exchange, to adjust the rate used to convert its various tax pools from Canadian dollars to US dollars. The change has been treated as a change in accounting estimate. The income tax expense of \$3,813,000 in 2016 is mainly a result of the significant taxable income generated on the sale of the Partnership. Certain components of finance income and finance costs are not taxable and their volatility has an apparent effect on the effective income tax rate.

#### ***Other comprehensive income***

Other comprehensive income ("OCI") for the year ended December 31, 2017 relates to an increase of \$143,000 in the market value of the Company's financial assets at fair value through OCI (2016 - \$347,000). These changes are a result of the sales and net market value changes in the Company's marketable securities. During 2017, the Company sold a portion of its holdings in marketable securities for net proceeds of \$46,000. In 2016, the Company sold all of its holdings in Corazon and a small portion of its holdings in other marketable securities for total net proceeds of \$404,000. Furthermore, foreign exchange loss in OCI of \$65,000 was incurred in 2017 (2016 - \$76,000), mainly due to the translation of the Company's subsidiaries' functional currency of CAD\$ to the Company's functional currency of US\$.

#### ***Deferred tax liability***

Deferred income tax assets and liabilities are recognized for temporary differences between the carrying value of the balance sheet items and their corresponding tax values, as well as for the benefit of losses available to be carried forward to future years for tax purposes that are considered probable to be realized. The deferred tax amount reflects a rate of 27% (2016 - 27%).

During 2016, the partnership generated income for tax purposes significantly in excess of its accounting income on the sale of the Partnership. As a result, the Company utilized the majority of its non-capital tax losses carried forward from prior years and the deferred tax liability balance in 2016 was partly offset against the balance of deferred tax assets from non-capital tax losses carried forward, resulting in a net deferred tax liability of \$3,809,000 as at December 31, 2016. As at December 31, 2017, the deferred tax liability was decreased to \$911,000 after applying non-capital tax losses generated during the year and accounting for the change in accounting estimate of various tax pools, as discussed above.

## SUMMARY OF QUARTERLY RESULTS

Selected financial information for each of the last eight quarters ended December 31, 2017 is as follows:

| <u>Fiscal year 2017</u>                       | <u>4<sup>th</sup> Quarter</u> | <u>3rd Quarter</u> | <u>2<sup>nd</sup> Quarter</u> | <u>1<sup>st</sup> Quarter</u> |
|---|-------------------------------|--------------------|-------------------------------|-------------------------------|
| Sales   | \$ 156                        | \$ 428             | \$ 46                         | \$ 249                        |
| Gross margin                                  | \$ 455                        | \$ (116)           | \$ (158)                      | \$ 8                          |
| General and administrative                    | \$ (133)                      | \$ (120)           | \$ (199)                      | \$ (139)                      |
| Net finance costs                             | \$ (34)                       | \$ (448)           | \$ (255)                      | \$ (773)                      |
| Net income (loss)                             | \$ 2,091                      | \$ (577)           | \$ (654)                      | \$ (908)                      |
| Total comprehensive income (loss)             | \$ 2,131                      | \$ (571)           | \$ (691)                      | \$ (839)                      |
| Earnings (loss) per share - basic and diluted | \$ 0.02                       | (0.00)             | \$ (0.01)                     | \$ (0.01)                     |
| <br>  |                               |                    |                               |                               |
| <u>Fiscal year 2016</u>                       | <u>4<sup>th</sup> Quarter</u> | <u>3rd Quarter</u> | <u>2<sup>nd</sup> Quarter</u> | <u>1<sup>st</sup> Quarter</u> |
| Sales   | \$ 31                         | \$ -               | \$ 4                          | \$ 65                         |
| Gross margin                                  | \$ (640)                      | \$ -               | \$ 116                        | \$ (20)                       |
| General and administrative                    | \$ (61)                       | \$ (212)           | \$ (249)                      | \$ (329)                      |
| Net finance (costs) income                    | \$ (1,350)                    | \$ (560)           | \$ 2,203                      | \$ 1,599                      |
| Net loss                                      | \$ (7,647)                    | \$ (924)           | \$ (1,117)                    | \$ 1,061                      |
| Total comprehensive (loss) income             | \$ (7,598)                    | \$ (853)           | \$ (1,047)                    | \$ 1,146                      |
| Loss (earnings) per share - basic and diluted | \$ (0.10)                     | \$ (0.01)          | \$ (0.01)                     | \$ 0.02                       |

Revenues from the sales of frac sand increased in 2017, compared with 2016, as mentioned earlier. The gross margin includes cost of goods sold, which contain operating costs for a full period despite production being at less-than-full capacity. In addition, the increase in the market value of frac sand required an impairment recovery of inventory values to the lower of cost or net realizable value during 2017 (impairment write-down during 2016). Net finance income and costs have fluctuated period-over-period, due to the change in the fair value of the embedded derivatives related to the Debt Restructuring Agreement, change in the fair value of the Participating Interest (defined below), gain on the Debt Restructuring Agreement during 2016, and amortization of embedded derivatives and loan fees on the New Promissory Convertible Notes (as defined below). During 2017, the Company recorded an income tax recovery as a result of adjusting the foreign exchange rate on various tax pools (as discussed above).

## LIQUIDITY AND CAPITAL RESOURCES

As at December 31, 2017, the Company had a working capital deficiency of \$6,406,000, compared with a working capital deficiency of \$5,558,000 as at December 31, 2016. The increase in the working capital deficiency resulted mainly from the decrease in inventory and increase in the carrying value of the New Promissory Convertible Notes for accrued interest.

### Participating Interest

Pursuant to a participating interest loan (the "Participating Interest") with Nuinsco Resources Limited (or the "Lender"), the Lender has the right to convert the outstanding balance into a limited participating interest (the "Conversion"), whereby the Lender is entitled to receive a share of cash flows earned from the sale of frac sand from the 7P Plant. On April 22, 2014, the Lender exercised the Conversion. The Conversion constituted payment of the loan in full. This obligation will be settled through a 52.16% participation in net operating cash flows from the frac sand business after recoupment of capital costs for phase one and pre-operating expenses. The participation is capped at CAD\$7,667,124 provided the Company proceeds with phase two (see FRAC SAND SEGMENT below for a description of phases one, two and three), otherwise the cap is approximately CAD\$10,222,831. Distributions under the Participating Interest terms are calculated based on operating cash flow after recovery of capital and pre-operating costs and take into account working capital. The continuing uncertainty surrounding the oil and gas industry and the related use of frac sand has made the determination of the timing of the first payment under the Participating Interest highly unlikely to occur in the next couple of years. As a result, at December 31, 2017, the carrying value of the Participating Interest was \$529,000, compared with \$933,000 at December 31, 2016. Any change in value is recorded through Finance Income or Cost in the statement of operations. The Company will continue to reassess the carrying value of the Participating Interest as circumstances warrant.

### **Senior Secured Debt**

In May 2014 the Company announced that it had executed the SPA Loan (“SPA Loan”), to issue and sell to the purchaser senior secured 14.8% notes in the aggregate principal amount of \$4,000,000. In June 2015, the Company announced it had entered into an amending agreement (the “SPA Amended Loan”) with respect to the SPA Loan, for an additional sum of \$1,150,000. The aggregate principal amount of \$5,150,000 under the SPA Amended Loan was due July 30, 2015.

On March 3, 2016 the Company announced that it had completed the restructuring of the SPA Amended Loan per the terms of the Debt Restructuring Agreement. The SPA Amended Loan was increased to \$5,500,000 and the maturity date extended to January 31, 2018. On December 31, 2017, the Senior Secured Debt was increased to \$7,050,000 and the maturity date was extended to July 31, 2019.

The interest rate on the Senior Secured Debt remained unchanged at 14.8% with interest payable in arrears. The Senior Secured Debt will be due in full on the date of maturity, subject to a cash sweep of 75% of free cash flow (“Free Cash Flow”) payable within 45 days following the end of each fiscal quarter and 90 days from each fiscal year end. Free Cash Flow will be calculated based on the Company’s quarterly unaudited and annually audited consolidated statement of cash flows, as net cash from operating and investing activities, plus interest and lease payments from financing activities. Allowable investing activities must be approved in advance by the Secured Lender.

During 2016, the Secured Lender received a fee in common shares equal to 4% of outstanding common shares of the Company, prior to the restructuring of the SPA Amended Loan. Accordingly, 2,305,404 common shares were issued. On December 31, 2017, the Secured Lender received a fee in common shares of 2,500,000 common shares on the amended Senior Secured Debt. Under the terms of the amendment, if the Senior Secured Debt is outstanding on December 31, 2018, an additional fee of 2,500,000 common shares will be issued by the Company to the Secured Lender. In addition, the Company agreed to not make any payments to settle past unsecured debt prior to the repayment of the secured debt, without the Secured Lender’s approval.

### ***Warrants issued to the Secured Lender***

Under the terms of the SPA Loan, the Company issued 2,000,000 common share purchase warrants. The number of warrants is subject to an increase from 500,000 to 1,000,000 warrants for each \$1,000,000 note issued under the SPA Loan, if any of the notes are prepaid and the closing price of the Company’s share price is CAD\$2.00 or lower on the trading day preceding the date of such prepayment (the “Original Warrants”). Given that there are costs associated with the prepayment right, the Company has valued the prepayment right at \$nil.

Pursuant to the terms under the SPA Amended Loan, the Company issued an additional 575,000 common share purchase warrants on the same terms as the Original Warrants (together with the Original Warrants, the “Warrants”).

Under the terms of the Senior Secured Debt, the Warrants were amended to reduce the exercise price to CAD\$0.25 and to extend the expiry date to January 31, 2018. Additionally, as partial consideration for entering into the Senior Secured Debt, the Company issued an additional 175,000 common share purchase warrants on the same terms as the Warrants (together with the Warrants, the “New Warrants”).

The New Warrants are subject to a cashless exercise provision and are considered a component of debt rather than equity; the fair value at inception of the Senior Secured Debt was calculated at \$26,000 and was revalued at December 31, 2017 to \$nil (2016 - \$6,000), with the change in fair value of \$6,000 (2016 - \$20,000) being recorded in finance income. Subsequent to December 31, 2017, the Warrants expired unexercised on January 31, 2018.

### **Promissory Convertible Notes**

During 2013 and 2014, the Company entered into several unsecured Promissory Convertible Notes and incurred interest payable quarterly at 14.8%. All Promissory Convertible Notes had a two-year term.

During 2016, the Company announced that it had restructured a portion of its debt through private placements of common shares and unsecured promissory convertible notes (the “New Promissory Convertible Notes”) in settlement of current indebtedness to certain of its unsecured lenders and trade creditors (collectively the “Unsecured Debt Restructuring”). Completion of the Unsecured Debt Restructuring represented 50% of the value owed to the Promissory Convertible Note holders and trade creditors. The Unsecured Debt Restructuring included issuing a total of 27,698,443 common shares of the Company and New Promissory Convertible Notes for a total of \$1,481,000 and CAD\$933,000.

The market prices of the Company's common shares on the dates of issuance during 2016 were lower than the calculated cost per common share upon conversion to the New Promissory Convertible Notes and settlement of outstanding interest, resulting in an increase in share capital of \$637,000 and a non-cash gain on settlement of debt of \$2,545,000.

The Company has not made any interest payments due on its New Promissory Convertible Notes, which has resulted in the Company defaulting on the New Promissory Convertible Notes.

#### ***Promissory Convertible Note Holders***

During 2016, unsecured debt of \$2,750,000 and CAD\$265,000 held by the Promissory Convertible Note holders was repaid under the following terms:

- 1) 50% of the value of the Promissory Convertible Notes issued during 2013 and 2014, with an interest rate of 14.8% per annum, was converted to 8,876,350 of common shares of the Company.
- 2) Outstanding interest on the Promissory Convertible Notes were settled with the issuance of 4,732,028 common shares of the Company.
- 3) The remaining 50% of the value of the Promissory Convertible Notes were replaced with the New Promissory Convertible Notes for a total of \$1,375,000 and CAD\$133,000, having the following terms:
  - A maturity date of July 31, 2018;
  - An interest rate of 7% per annum, payable annually or at any time in cash or in common shares valued at market, at the option of the Company;
  - Convertible at CAD\$0.25 per share, at the option of the holder; and
  - Holders of the New Promissory Convertible Notes will also receive one common share purchase warrant for every four common shares acquired upon conversion of the New Promissory Convertible Notes, with an exercise price of CAD\$0.50 per share, exercisable for a five year period from the date of conversion.

#### ***Outstanding Note***

All of the Promissory Convertible Note holders participated in the Debt Restructuring Agreement, except for one holder of the Outstanding Note of \$3,000,000. In March 2016, the Company announced that it had received notice that the holder of the Outstanding Note had filed a statement of claim concerning non-payment of principal and interest. The Company has reviewed the statement of claim with legal counsel to assess its impact on the Company and has concluded that there is no significant impact on the status of the Company's debt. Pursuant to the terms of the Senior Secured Debt, the Company is prevented from making payments under outstanding unsecured debt until the Senior Secured Debt is repaid. As a result, the Company has not paid interest accrued on the Outstanding Note. The Outstanding Note matured in July 2016 and the Company has been unable to repay the amounts owing and interest payments due. This has resulted in the Company defaulting on the Outstanding Note.

#### ***Debt Owed to Trade Creditors, Directors and Management***

During 2016, \$211,000 and CAD\$1,600,000 of debt owed to certain trade creditors, directors and management of was restructured and repaid under the following terms:

- 1) 50% of debt owed to trade creditors, directors and management was converted to 18,822,093 of common shares of the Company.
- 2) The remaining 50% of the debt owed to trade creditors was paid with the New Promissory Convertible Notes for a total of \$106,000 and CAD\$533,000, having the same terms as outlined above in the section *Promissory Convertible Note Holders* above.
- 3) The remaining 50% of debt owed to directors and management amounting to CAD\$267,000 was deferred for payment until January 31, 2018.

As at December 31, 2017, current directors and management agreed to defer payment of all outstanding debt and director fees until July 2019. As a result, the long-term debt of \$318,000 owed to directors and management is comprised of a portion of the restructured debt owed to current directors and management amounting to CAD\$224,000, and director fees incurred by current directors during 2016 and 2017 totalling CAD\$175,000.

### Cash flows in the year

Cash and cash equivalents as at December 31, 2017 and 2016 were held with major Canadian banks. The Company has a policy of investing its available cash in Canadian government instruments and certificates of deposit or other direct obligations of major Canadian banks.

For the year ended December 31, 2017, the Company generated cash of \$183,000 through operating activities (2016 - \$311,000 used by operating activities). Sale of frac sand inventory improved cash by \$679,000, while decreased payments of trade payables and deferred salaries also improved cash by \$289,000. During 2016, operating activity was minimal and revenues were limited, due to the low price environment in the oil and gas sector and the protracted period of minimal drilling activity in the Company's market area.

During the year ended December 31, 2017, net cash used by investing activities was \$53,000 (2016 - \$656,000). In 2017, the Company used \$77,000 towards refurbishment of the frac sand wash plant at 7P Plant and generated \$46,000 in net proceeds on the sale of marketable securities. During 2016, the Company received cash proceeds of \$283,000 on the sale of the partnership and \$404,000 on the sale of various marketable securities. Other amounts used in investing activities include minimal costs incurred to maintain the Company's mine property and development project in good-standing.

The Company used \$137,000 in financing activities during 2017 (2016 - \$148,000), mainly related to the payments of interest and lease obligations. During 2017, the Company issued a current promissory note of \$55,000 to a company in the Frac Sand business. The Company has committed to provide up to \$200,000 in funding under certain terms of this note. The note has interest bearing at 15%, is secured and matures June 22, 2018. Any proceeds received from repayment of this loan must be used to repay the other current loan of \$65,000 received during 2017.

The Company's activities during the year ended December 31, 2017 used cash and cash equivalents of \$7,000, with a foreign exchange loss effect of \$65,000.

### Table of Contractual Commitments

|   | Due Date          | Currency        | December 31, 2017 | December 31, 2016 |
|---|-------------------|-----------------|-------------------|-------------------|
| Promissory Convertible Note                     | July 7, 2016      | US Dollar       | \$ 3,000          | \$ 3,000          |
| Leased mobile equipment                         | Within one year   | Canadian Dollar | \$ 5              | \$ 125            |
|   | One to five years | Canadian Dollar | \$ -              | \$ 5              |
| Other current loan                              | June 28, 2018     | US Dollar       | \$ 65             | N/A               |
| New Promissory Convertible Notes <sup>(1)</sup> | July 31, 2018     | US Dollar       | \$ 1,375          | \$ 1,375          |
| New Promissory Convertible Notes <sup>(1)</sup> | July 31, 2018     | Canadian Dollar | \$ 133            | \$ 133            |
| New Promissory Convertible Notes <sup>(1)</sup> | July 31, 2018     | Canadian Dollar | \$ 800            | \$ 800            |
| New Promissory Convertible Notes <sup>(1)</sup> | July 31, 2018     | US Dollar       | \$ 106            | \$ 106            |
| Senior Secured Debt <sup>(2)</sup>              | July 31, 2019     | US Dollar       | \$ 7,050          | \$ 5,500          |

(1) New Promissory Convertible Notes part of the Debt Restructuring Agreements closing on March 7, March 31 and June 7, 2016.

(2) On December 31, 2017, the Senior Secured Debt was increased to \$7,070,000 and its maturity was extended to July 31, 2019.

### Other potential sources of cash flow

The aggregate market value of the Company's marketable securities held in public company shares is approximately \$167,000 as at the date of this MD&A.

As at April 16, 2018, the Company had options outstanding that could bring in additional funds. All of those instruments are not "in-the-money", with the exception of 11,900,000 exercisable options with an aggregate value of CAD\$595,000. However, the receipt of such funds cannot be relied upon.

The Company's title to its projects is in good-standing and management will continue to maintain the projects in good-standing.



The Company has approximately 22,000 tons of sand in inventory at December 31, 2017. The Company has eliminated all discretionary costs that should not have a negative impact on its ability to resume production. Staffing, salaries and director fees have been reduced or accrued and deferred where possible.

## REPORTING SEGMENT

The Company is engaged in the exploration, evaluation and development of properties for the mining and production of nickel and associated products. The Company also produces frac sand for the oil and gas industry in Canada and the northern US. The Company has three reporting segments: Corporate, Exploration and Development, and Frac Sand. The Corporate segment supports all of the Company's activities.

Senior management makes decisions with respect to Exploration and Development by considering exploration and development potential and results on a project basis. The exploration and development projects are all located in Canada.

The Frac Sand segment is managed and operated by Victory Silica's executives and employees although the business and operating assets are part of Victory Nickel. The segment is located in Canada although sand as raw material is imported from the United States.

The following table provides additional information on the Company's total segment assets:

| As at December 31,          | 2017             | 2016             |
|-----------------------------|------------------|------------------|
| <b>Canada</b>               |                  |                  |
| Corporate                   | \$ 2,020         | \$ 1,863         |
| Exploration and Development | 43,714           | 43,692           |
| Frac Sand                   | 4,858            | 5,803            |
| Intersegment elimination    | (1,502)          | (1,443)          |
| <b>Total Assets</b>         | <b>\$ 49,090</b> | <b>\$ 49,915</b> |

## EXPLORATION AND DEVELOPMENT ACTIVITIES

*Paul Jones is a "qualified person" as defined under NI-43-101 and has approved the preparation of the information relating to the material mineral projects of the Company described herein.*

## MINE PROPERTY AND DEVELOPMENT ACTIVITIES

### Minago Project

During the year ended December 31, 2017, \$22,000 was incurred on the Minago project (2016 - \$22,000).

The Company's 100%-owned Minago project is a permitted project ready for development. It is located on the unexposed southern part of the Thompson Nickel Belt in Manitoba, and is one of Canada's largest undeveloped sulphide nickel deposits. Minago has been shown to be capable of producing a nickel concentrate grading from 22.3% up to 35.0%, making it reportedly the world's highest grade nickel concentrate. In addition to metal by-products such as copper, cobalt, gold, platinum, palladium, silver and rhodium, a layer of silica sand averaging approximately nine metres thick overlies the nickel mineralization within the open pit. Approximately 84% of the sand is marketable as frac sand. The frac sand forms part of the overburden that must be removed prior to mining the nickel ore. According to the Minago FS, production of frac sand could begin 20 months after the start of mine development. As noted in Outlook above, the value of the cobalt alone in the Minago concentrate has increased to \$188,000,000 at the recent cobalt price of \$42.00.

The analytical data and geological interpretations obtained from a work program in 2010 were incorporated into an updated geological model and resource estimate. The updated resource incorporates a 24% increase (over the previous resource estimate) in the NI 43-101 compliant measured and indicated and pit-constrained sulphide nickel resource used in the Minago FS. The Minago FS is available at [www.sedar.com](http://www.sedar.com). Note that all resources are contained in the Nose Deposit and the update below does not include the results of the 2011 drilling program.

|           | April 2011 Pit-Constrained Resource <sup>1</sup> |                   |            | March 2010 In-Pit Resource <sup>2</sup> |                   |            | Increase (Decrease) in Contained Metal |        |
|-----------|--|-------------------|------------|---|-------------------|------------|--|--------|
|           | Tonnes   | Grade             | Ni Content | Tonnes                                  | Grade             | Ni Content | Ni Content                             | Change |
| Category  | Millions   | %NiS <sup>3</sup> | M Lb       | Millions                                | %NiS <sup>3</sup> | M Lb       | M Lb                                   | %      |
| Measured  | 8.2  | 0.473             | 85.0       | 6.6                                     | 0.488             | 71.4       | 13.7                                   | 19.2   |
| Indicated | 22.8   | 0.432             | 217.2      | 19.1                                    | 0.410             | 172.6      | 44.6                                   | 25.9   |
| M&I       | 31.0   | 0.443             | 302.2      | 25.7                                    | 0.430             | 243.9      | 58.3                                   | 23.9   |
| Inferred  | 0.2  | 0.380             | 1.4        | 1.4                                     | 0.402             | 12.2       | (10.8)                                 | (88.4) |

<sup>1</sup> Lerch-Grossman pit optimization shell

<sup>2</sup> Whittle pit optimization shell

<sup>3</sup> Nickel in sulphide form

On August 23, 2011, the Manitoba Government issued Victory Nickel's final EAL for the Minago project. The licence was to expire on August 22, 2014 unless the Company completes a certain amount of work to move the project forward. During 2014, the Company complied with the conditions of the EAL and, in December 2014, filed an Environmental Act Proposal ("EAP") to amend the EAL to relocate the proposed tailings and waste rock management facility. The construction of drainage ditches installed to lower down the water table within the pit shell limits, the installation of Flow Gauging and Telemetry systems and the implementation of a comprehensive environmental monitoring program are considered part of the site development necessary to maintain the EAL. Consultations with First Nations by the government of Manitoba continue. The existing EAL continues to be valid and on completion of consultations, the government is expected to issue the amendment to the existing EAL.

#### *Minago Frac Sand*

An indicated resource of 15 million tonnes of sandstone has been estimated to occur within the current Minago pit shell. The frac sand component of this resource is approximately 11 million tonnes and is a significant contributor to the positive economics at Minago. As part of the FS, Outotec produced a feasibility-level design for a frac sand plant complete with capital and operating costs to produce 1,140,000 tonnes of frac sand annually for a ten-year period. Considerable potential exists to expand the resource beyond the limits of the current pit.

## EXPLORATION AND EVALUATION ACTIVITIES

For the year ended December 31, 2017, the Company did not record an impairment (2016 - \$4,700,000 on its Lac Rocher property) or incur exploration expenditures on its E&E projects (2016 - \$9,000). Expenditures have been reduced due to the tight equity markets and management's focus on Victory Silica and the frac sand business.

### **Frac Sand**

#### *Bear Coulee Property*

In October 2014, the Company entered into an option to acquire a 100% interest in a frac sand land package totaling over 300 acres in Trempeleau County Wisconsin, USA (the "Bear Coulee Property"). The option agreement provides for a cash payment of \$10,000 on signing of the agreement (paid in 2014), a second cash payment on delivery of permits (which has not yet been completed) and a third cash payment on exercise of the option. The option is valid for six months following receipt of permits with two equivalent extensions available under certain circumstances. Prior to production, the Company will be required to pay \$40,000 per annum as advance royalties on the initial 20,000 tons of sand production. Once the Bear Coulee Property is in production, the Company will be required to pay a royalty of \$2.00 per ton of frac sand sold from the property.

In February 2015, the Company announced the completion of a National Instrument 43-101 technical report describing a resource estimate of approximately 11 million tons of frac sand on the Bear Coulee Property.

### **Nickel**

#### *Lac Rocher*

Lac Rocher, with year-round access, is located in northwestern Québec and has measured (0.29 million tonnes grading 1.23% Ni) and indicated (0.51 million tonnes grading 1.05% Ni) resources of 0.80 million tonnes grading 1.12% nickel, at a 0.5% nickel cutoff, for approximately 20 million pounds of in-situ nickel located between surface and 125 vertical metres. Additional inferred resources total 0.44 million tonnes grading 0.65% Ni. Mineralization remains open to the southwest. The breakeven price of nickel per pound in the Lac Rocher PEA was US\$9.74 with copper at US\$3.65 with an exchange of CAD\$0.95 / US\$1.00.



The Lac Rocher property is subject to a discovery incentive plan (the “DIP”) to reward certain individuals involved in the discovery of Lac Rocher with a 2% net smelter royalty (“NSR”) for mines that were discovered on certain properties prior to the expiry of the DIP. The NSR is payable only on revenues earned after recovery of all development costs for any mine on the property. The terms of the DIP provide the Company with a right of first refusal on any proposed disposition of the NSR. In addition, the DIP contains put/call provisions under which the Company may be required to purchase, or may exercise an option to purchase, the NSR at the value of its discounted cash flows, as defined therein. The Lac Rocher property is the only property subject to the DIP. As the Lac Rocher property is not yet in production, no royalties are currently payable. No work has been conducted on site since December 2009.

As at December 31, 2016, the Company recorded an impairment of \$4,700,000 on its Lac Rocher property (refer to IMPAIRMENT ANALYSIS UPDATE section below). No impairment was recorded during 2017.

#### *Mel Project*

The 100% owned Mel project is located on the Thompson Nickel Belt, just north of Thompson, Manitoba and remains underexplored.

Mel has an indicated resource of 4.3 million tonnes grading 0.88% nickel (approximately 83 million pounds in-situ nickel) and an additional inferred resource of one million tonnes grading 0.84% nickel (approximately 19 million pounds in-situ nickel) and offers significant exploration upside as well as near-term production potential.

The re-evaluation of the Mel dataset has been completed for both the drill hole data on the Mel deposit and the considerable drilling (111 drill holes) conducted on the claims portion of the property. The study has included reinterpretation of the geological context in order to evaluate new or under-tested target areas for future work that can be incorporated into further, more refined, modelling of the Mel resource. No fieldwork has been conducted since 2011. An application to renew Mel mining lease ML-007 was successful and the lease has been renewed for a 21-year term.

Under the terms of the Mel option agreement with Vale, Vale must mill ore from the Mel project at cash costs plus 5% subject to capacity availability and metallurgy – this is unaffected by Vale’s decision not to exercise its back-in right. Furthermore, in accordance with the terms of the agreement with Vale, they now are entitled to a 10% royalty on “distributable earnings” as defined in the agreement. Distributable earnings is defined as net revenue less operating expenses, before federal and provincial income taxes, after provincial mining taxes and less aggregate pre-production capital but before depreciation.

#### *Lynn Lake*

The Lynn Lake property is located in the historic mining town of Lynn Lake in northern Manitoba, about 320km by road northwest of the Thompson mining camp. The property is the former Sherritt Gordon Mines Limited (“Sherritt”) mine site known as the Lynn Lake A Mine and Farley Mine, comprised of 13 mining claims, 14 mining claim leases and 2 mineral leases covering an area of 2,170.26 hectares. The property was operated by Sherritt from 1953 to 1976 with reported production of 22.2 million tons at an average grade of 1.023% nickel and 0.535% copper.

On November 4, 2014, the Company announced that it had optioned the Lynn Lake project to Corazon, an Australian listed public company with assets in the Lynn Lake area. Under the terms of the agreement, Corazon can acquire a 100% interest in Lynn Lake by issuing 40,000,000 Corazon shares to the Company upon closing and incurring AU\$3,500,000 in exploration expenditures or in payments (in cash or Corazon shares at Corazon’s option) to Victory Nickel before November 2019. In addition, Victory Nickel will retain a 1.5% net smelter royalty on production from the Lynn Lake nickel project, and receive a payment of AU\$1,000,000 (in cash or Corazon shares at Corazon’s option) within 30 days of the commencement of ore processing activities at the Lynn Lake nickel project. On April 6, 2015 Corazon issued 40,000,000 Corazon shares to Victory Nickel as part of the terms of the option agreement between the two companies. In October 2016, the shares were sold for net proceeds of AU\$515,000.

## **FRAC SAND SEGMENT**

As explained above, the Frac Sand segment is managed and operated by Victory Silica, although the business and operating assets are part of Victory Nickel. The segment is located in Canada although sand as raw material is currently imported from the United States. The plan is to eventually produce both domestic and imported sand.

The Company completed phase one of its three phase business plan. Phase one provided for the refurbishment and upgrading of the 7P Plant to a capacity of 500,000 tpa of high-quality frac sand. Phase one was completed in 2014.

The Board of Directors approved proceeding with phase two, provided non-dilutive financing could be arranged. However, in 2015, the Company announced that phase two had been deferred due to the uncertainty caused by the drop in the price of oil. However, phase two remains a desirable next step which would not only make the Company more competitive, but also provide significant flexibility to target certain markets which often require different grades of sand.

Phase two is to build a wash plant on a Wisconsin sand resource. Frac sand production is a two-stage process: the wet stage (washing) and the dry stage. The Company has historically contracted out the wet stage in Wisconsin prior to shipping the wet sand to its plant in Alberta. The wet stage removes impurities, enabling transport of only the desired sand size fractions. The dry stage, where the sand is dried and separated into several products of different sizes, is completed at the Company's 7P Plant.

Phase three of the business plan is to build a second dry processing facility in or around Winnipeg, Manitoba capable of producing 1,000,000 tpa. A site serviced by multiple rail carriers would give the Company more flexibility in accessing only the highest quality sand from the Wisconsin/Minnesota region. The ultimate plan is to provide customers with a variety of qualities, which would include domestic sand from the Company's Minago project in Manitoba (see above). The Minago project is a nickel project overlain by overburden, which includes sand meeting the tier two frac sand specs. The Winnipeg formation sand located at Minago is the highest-quality domestic sand and would be a welcome addition to the Company's mix of products as not all of the Company's customers' applications require Wisconsin sand.

As a result of commodity market uncertainty, the 7P Plant operates on an as-needed basis only. Due to continued uncertainty in the oil price E&P companies have reduced capital expenditure programs, placing pressure on Victory Nickel's oilfield service company customers to reduce E&P company drilling costs. These companies, in turn, look to their suppliers, including frac sand producers, to help lower their costs. Accordingly, frac sand prices in Canada have decreased to levels that do not appear to be sustainable over the long term.

During 2017, the Company sold most of the coarser fractions of its finished goods inventory requiring the start-up of the 7P Plant to replenish finished goods, in anticipation of a continued improvement in sales.

## **IMPAIRMENT ANALYSIS UPDATE**

The Company performed a detailed impairment analysis on each of its E&E projects and the MP&D project as at December 31, 2017. The Company does not believe that there have been any material changes to date which would adversely affect this analysis. Furthermore, there has been no change in management's plans for the projects which would cause a reassessment.

The challenge facing all junior resource companies remains to find financing for development of projects. This difficulty is not a reflection of the quality of the Company's projects, but is indicative of a continued general malaise affecting the junior resources sector in general. The Company performed a detailed impairment analysis at the project level.

An initial indicator of impairment considers the market capitalization of a company compared with its net book value. At and around the end of December 2017, the Company's market capitalization was below its net book value. Many resource companies continue to experience similar circumstances in present markets despite having good projects. An analysis was performed on each of the Company's E&E projects and the MP&D project.

The impairment analysis reviewed historic expenditures recorded on each project along with any purchase price allocations from acquisitions, reflected the existence of previous writedowns or reversals of impairment and also considered the existence of any economic studies which had been performed. The assumptions used in such studies were reviewed for such factors as: forecast metals prices, foreign exchange rates, changes in resource and/or cost estimates, changes in royalty arrangements, the existence of significant by-products and other matters as necessary.

Forecast metals prices were estimated from third-party sources such as analyst consensus reports and other available documentation which were considered to be reasonable by management. In particular, for the Minago FS base case,

long-term annual forecast nickel prices averaging \$11.19 and an exchange rate of US\$0.9116:CAD\$1.00 were used. Since the Minago FS was performed, metals prices and exchange rates have changed. The Company continues to work on updating the Minago FS for improved economics and announced updated resource estimates in 2011 as a result of the drilling performed in 2010.

For the purposes of impairment testing, the economic model in the Minago FS was used as a base. The business model used in the Minago FS and the intention of management is to develop and produce the nickel and frac sand co-product simultaneously. For the purposes of assessing the impairment of Minago, frac sand is treated as a raw material for sale into the market and is not processed to a finished product. This required elimination from the Minago FS economic model of the following: processing plant capital, processing operating costs, transportation costs and the finished goods margin. This does not reflect how management intends to develop Minago, nor, in management's opinion, does it reflect how any other organization would develop the project.

In addition, adjustments were made for prices derived from the forecasted average of \$8 per pound for nickel and an exchange rate of US\$0.775:CAD\$1.00. A discount rate of 11% was used in the analysis and includes estimates for income taxes.

Capital and operating cost estimates generally were reduced from those used in historic studies if documentary evidence supporting such reductions had recently been obtained as part of the review work which had been undertaken for the Minago FS. Used equipment prices cannot be typically reflected in a feasibility study, as the market for such equipment is unpredictable, except where firm pricing has been negotiated. Often cost estimates used in previous studies had been derived when such were universally recognized to be at historic highs. The Company continues to see evidence of engineering firms broadly announcing price freezes. Experience with equipment strategies at the 7P Plant has proved that good quality used equipment can be sourced and that equipment financing is available. This represents an additional cost-saving opportunity which has not been quantified in the impairment analysis. These factors resulted in a recoverable amount in excess of the book value of Minago. Accordingly, no impairment exists on the Minago project.

The impairment model is sensitive to several of the model key input variables. The following table indicates the estimated impact on the recoverable amount:

| Change in Model Key Input      | Change in Recoverable Amount of Minago |
|--------------------------------|--|
| Effect of:                     |  |
| Increase discount rate by 1%   | (24%)                                  |
| Increase exchange rate by 0.05 | (23%)                                  |
| Increase nickel prices by 1%   | 4%                                     |
| Increase operating costs by 5% | (9%)                                   |

Furthermore, management's intentions with respect to future expenditures and plans for the projects were considered. With the exception of some small projects, all projects have had recent expenditures and are considered to be active.

All of the Company's projects were tested for impairment as at December 31, 2017. As a result of the tests, management concluded that no impairment existed on the Company's other projects as at December 31, 2017 and that costs incurred to date are recoverable. The Company will continue to monitor developments as they occur in the metals markets and the economy and will update its impairment analysis to take account of any such changes, as appropriate.

At December 31, 2016, the Company tested the Lac Rocher project for impairment. A discounted cash flow model was used as a base. Adjustments were made for prices derived from the forecasted average of \$7.40 per pound for nickel and an exchange rate of US\$0.731:CAD\$1.00. The forecasted average price and exchange rate were obtained from third-party reports. A discount rate of 15% was used in the analysis. These factors resulted in a recoverable amount below the book value of Lac Rocher. Accordingly, an impairment of \$4,700,000 was recorded on the Lac Rocher project. During 2017, no impairment was recorded on the Lac Rocher project.

## TRANSACTIONS WITH RELATED PARTIES

### *Related Party Balances and Transactions for Services*

Short-term employee benefits provided by the Company to key management personnel include salaries, directors' fees, statutory contributions, paid annual vacation and paid sick leave as well as non-monetary benefits such as medical care. In addition to short-term employee benefits, the Company may also issue options and common shares as part of the stock option plan and share bonus plan. Payables to key management personnel generally relate to directors' fees, consulting fees and expense reimbursements.

Balances and transactions with related parties as at December 31, 2017 and 2016 are shown in the following tables:

| As at December 31,                             | 2017   | 2016   |
|--|--------|--------|
| <b>Balances Outstanding</b>                    |        |        |
| Debt due to key management personnel           | \$ 318 | \$ 280 |
| Other payables due to key management personnel | 173    | 160    |
|  | \$ 491 | \$ 440 |

Key management personnel compensation is comprised of:

| Years ended December 31,     | 2017   | 2016   |
|------------------------------|--------|--------|
| Short-term employee benefits | \$ 362 | \$ 371 |
|                              | \$ 362 | \$ 371 |

## OUTSTANDING SHARE DATA

As at April 16, 2018, the Company had 94,870,968 common shares issued and outstanding. In addition, there were 12,625,000 stock options outstanding with a weighted average exercise price of CAD\$0.07. Of the outstanding options, 11,900,000 options were "in-the-money," exercisable at CAD\$0.05 and CAD\$0.06 per share.

## CRITICAL ACCOUNTING ESTIMATES AND JUDGEMENTS

Critical accounting estimates and judgements used in the preparation of the consolidated financial statements include determining the carrying value of investments, MP&D and E&E projects, assessing the impairment and classification of long-lived assets, determining the recoverability of deferred income tax assets, the valuation of the convertibility feature of the New Promissory Convertible Notes, the valuation of share-based payments and the disclosure of contingencies and going concern matters. These estimates involve considerable judgement and are, or could be, affected by significant factors that are out of the Company's control.

For a complete list of the significant accounting policies as well as information concerning the use of estimates, judgments and measurement uncertainty, reference should be made to Note 3 to the Company's 2017 Audited Consolidated Financial Statements. The Company's 2017 Audited Consolidated Financial Statements have been prepared using the going concern assumption; reference should be made to Note 1 to the Company's 2017 Audited Consolidated Financial Statements.

The recorded value of the Company's E&E projects and the MP&D project is based on historic costs that are expected to be recovered in the future. The Company's recoverability evaluation is based on market conditions for minerals, underlying mineral resources associated with the properties and future costs that may be required for ultimate realization through mining operations or by sale. The Company is in an industry that is exposed to a number of risks and there is always the potential for a material adjustment to the value assigned to these assets. Such risks also extend to the evaluation of fair values of net assets upon acquisition.

The value of the Participating Interest is a significant estimate which uses a model of estimated cash flows and applies probability-weighted estimates to the model. Assumptions are made about the phase at which the frac sand business will be when payments are being made as well as production costs and volumes and sales prices and volumes.

The fair value of the stock options and warrants, as well as the embedded derivatives in the New Promissory Convertible Notes, is calculated using the Black-Scholes option-pricing model that takes into account the exercise price, expected life, expected volatility of the underlying common shares, expected dividend yield and the risk-free interest rate for the term of the option, warrant or embedded derivative.

The Company has determined that it is probable that Victory Nickel will generate returns sufficient to utilize its taxable losses prior to their expiry. This is a significant judgement that, dependent upon future events, may turn out to be incorrect. Presently, since Victory Silica is not generating profit, a full valuation allowance has been recorded against losses incurred in that subsidiary. The Company will monitor any changes in circumstances which could require a reversal of the valuation allowance.

## **NEW ACCOUNTING PRONOUNCEMENTS**

### **Accounting Standards Issued But Not Yet Applied**

The Company has not yet adopted the following new accounting pronouncements which are effective for fiscal periods of the Company beginning on or after January 1, 2018:

#### ***IFRS 15, Revenue from Contracts with Customers***

IFRS 15 deals with revenue recognition and establishes principles for reporting useful information to users of financial statements about the nature, amount, timing and uncertainty of revenue and cash flows arising from an entity's contracts with customers. Under IFRS 15, revenue is recognized when a customer obtains control of a good or service. The standard replaces IAS 18 "Revenue" and IAS 11 "Construction Contracts" and related interpretations. The standard is effective for annual periods beginning on or after January 1, 2018 and earlier application is permitted.

The Company has not identified any differences between the new standard and its current revenue recognition policy.

#### ***IFRS 16, Leases***

In 2016, the IASB issued its new leasing standard. IFRS 16 eliminates the classification of leases as either operating leases or finance leases as previously required by IAS 17. Instead, it introduces a single lease accounting model that requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value, and to depreciate the lease assets separately from interest on the lease liabilities on the income statement. IFRS 16 will be effective for the Company's fiscal year beginning January 1, 2019, with earlier adoption permitted if the entity also adopts IFRS15.

The Company has evaluated the impact of adopting this standard and does not believe it will have a material effect on its financial statements.

## **CORPORATE GOVERNANCE**

The Company's Board of Directors is responsible for ensuring that management fulfils its responsibilities for financial reporting and internal control and exercises this responsibility principally through the Audit Committee. The Audit Committee, which is comprised of directors, none of whom are employees or officers of the Company, meets with management to review the 2017 Audited Consolidated Financial Statements to satisfy itself that management is properly discharging its responsibilities to the directors who approve the financial statements. The Board of Directors has also appointed a Compensation committee, a Corporate Governance and Nominating committee composed of non-executive directors, and a Health, Safety & Environment committee.

### ***Disclosure Controls and Procedures***

The Company's Chief Executive Officer and Chief Financial Officer (collectively, the "Certifying Officers"), are responsible for designing a system of disclosure controls and procedures, or causing them to be designed under their supervision, to provide reasonable assurance that information required to be disclosed in reports filed with or submitted to, securities regulatory authorities is recorded, processed, summarized and reported within the time periods specified under Canadian securities laws and that material information relating to the Company is made known to them with respect to financial and operational conditions to allow timely decisions regarding required disclosure. Such controls are facilitated by the small size of the Company's senior management team and their access to material information.

### ***Internal Control over Financial Reporting***

The Company's Certifying Officers are responsible for designing a system of internal controls over financial reporting, or causing them to be designed under their supervision, to provide reasonable assurance regarding the reliability of financial reporting and the preparation of consolidated financial statements for external purposes in accordance with Canadian GAAP. Management of the Company was required to apply its judgement in evaluating the cost-benefit relationship of possible controls and procedures. The result of the inherent limitations in all control systems means no evaluation of controls can provide absolute assurance that all control issues and instances of fraud, if any, have been detected.

## **RISKS AND UNCERTAINTIES**

The exploration and development of natural resources are speculative activities that involve a high degree of financial risk. Additionally, there are specific risks related to the Company's presence in the frac sand market. The risk factors which should be taken into account in assessing Victory Nickel's activities and an investment in its securities include, but are not necessarily limited to, those set out in detail below.

The relative significance of each risk described below will vary as a function of several factors including, but not limited to, the state of the economy, the stage of Victory Nickel's projects, the availability of financing on acceptable terms and other matters.

Any one or more of these risks could have a material adverse effect on the value of any investment in Victory Nickel and the business, financial condition, operating results or prospects of Victory Nickel and should be taken into account in assessing Victory Nickel's activities.

### **Financial and Investment Risks**

#### ***Going Concern***

Readers are encouraged to read and consider the going concern note specifically described at the beginning of the MD&A and contained in the 2017 Audited Consolidated Financial Statements.

#### ***Substantial Debt and Loss from Operations***

As reflected in the accompanying consolidated financial statements and notes, the Company's outstanding debt balance, both secured and unsecured, raises substantial doubt about our ability to continue as a going concern and to generate sufficient liquidity to meet our operating needs. While the Company is attempting to generate sufficient revenue and reduce costs, the cash position may not be sufficient to support ongoing daily operations and the Company cannot ensure that the business will generate sufficient cash flows from operations or future borrowings. As noted above, readers are encouraged to read and consider the going concern note specifically described at the beginning of the MD&A and contained in the 2017 Audited Consolidated Financial Statements.

#### ***Substantial Capital Requirements***

Victory Nickel will have to make substantial capital expenditures for the development of, and to achieve production from, its nickel projects. Production will only be reached a number of years following the start of development. Until that time, the Company is reliant on cash flows generated by its frac sand business, on the equity markets and asset sales to generate cash for ongoing operations and programs. There can be no assurance that any debt or equity financing or cash generated by operations or asset sales will be available or sufficient to meet these requirements or for other corporate purposes or, if debt or equity financing is available, that it will be on terms acceptable to Victory Nickel. Moreover, future activities may require Victory Nickel to alter its capitalization significantly. The inability of Victory Nickel to access sufficient capital for its operations could have a material adverse effect on its financial condition, results of operations or prospects. Flow-through financing cannot be used to fund the Company's corporate costs.

The 7P Plant has been substantially completed, however additional capital will be required. Future phases of the business plan as outlined earlier in this MD&A will require additional capital; these phases are independent of the 7P Plant. This capital requirement may be in excess of the net funds generated by the business. The frac sand operations have ongoing requirements for working capital financing. There is a risk that sufficient working capital financing may not be available at suitable prices.

The Company recognizes the requirement to repay outstanding principal and interest on existing debt and is actively working on restructuring its obligations. To date, the Company has entered into the Debt Restructuring Agreement



under which its secured and certain of its unsecured creditors have participated. There can be no assurance that the Company will be able to restructure its debt with any or all of the remaining unsecured creditors per the terms of the Debt Restructuring Agreement and/or recapitalize and there is no certainty as to what steps the unsecured lenders may take as a result.

### ***Market Perception***

Market perception of junior exploration, development and mining companies and frac sand companies may continue to shift such that companies in these sectors continue to be viewed unfavourably by investors. This could impact the value of investors' holdings and Victory Nickel's ability to raise further funds by issue of additional securities or debt.

### ***Metal and Frac Sand Prices***

There is no assurance that, even if commercial quantities of mineral resources are developed, a profitable market will exist for the sale of such product. Nickel and by-product prices fluctuate on a daily basis and are affected by numerous factors beyond Victory Nickel's control – including factors which are influenced by worldwide circumstances. The level of interest rates, the rate of inflation, world supply and demand for commodities and stability of exchange rates can all cause significant fluctuations in commodity prices. Such external economic factors are in turn influenced by changes in international investment patterns and monetary systems and political developments. The prices of nickel and by-products have historically fluctuated widely and future price declines could cause commercial production to be uneconomical and such fluctuations could have a material adverse effect on Victory Nickel's business, financial condition and prospects. As Victory Nickel has historically been in the exploration and development stage, the above factors have had no material impact on present operations but must be considered in evaluating the impairment of long-lived assets. These factors are of significant importance for the Minago FS and decisions related thereto as well as being important to the developing frac sand business.

The business case developed to support the Company's entry into the frac sand business made significant assumptions on pricing of frac sand as well as for important cost elements of production and transportation. The price of frac sand is subject to market forces beyond the Company's control. Over the past 30 months or more, the impact of such market forces has negatively impacted demand and pricing for frac sand and there can be no assurance that these impacts will not continue in the future.

### ***Areas of Investment Risk***

The Company's common shares are listed on the CSE. The share prices of publicly-traded companies can be volatile as the price of common shares is dependent upon a number of factors, some of which are general or market or sector specific and others that are specific to Victory Nickel. The market for shares in small public companies is less liquid than for large public companies. Investors should be aware that the value of the Company's common shares may be volatile and may go down as well as up and investors may therefore not recover their original investment.

The market price of the Company's common shares may not reflect the underlying value of the Company's net assets. The price at which investors may dispose of their securities may be influenced by a number of factors, some of which may pertain to the Company and others of which are extraneous. On any disposal of their common shares, investors may realize less than the original amount invested.

### ***Industry Risks***

#### ***Speculative Nature of Mineral Exploration***

Mineral exploration is highly speculative in nature, involves many risks and frequently is non-productive. There is no assurance that Victory Nickel's exploration efforts will be successful. Few properties that are explored are ultimately developed into economically-viable operating mines. Success in establishing reserves is a result of a number of factors, including the quality of Victory Nickel's management, level of geological and technical expertise and the quality of land available for exploration and other factors. Once mineralization is discovered, it may take several years in the initial phases of drilling until production is possible, during which time the economic feasibility of production may change. Substantial expenditures are required to establish proven and probable reserves through drilling to determine the optimal extraction method for the ore and the metallurgical process to extract the metals from the ore and, in the case of new properties, to construct mining and processing facilities. It is possible that even preliminary due diligence will show adverse results, leading to the abandonment of projects. It is impossible to ensure that preliminary feasibility studies or full feasibility studies, such as to the Minago FS, on Victory Nickel's projects or the current or proposed exploration programs on any of the properties in which Victory Nickel has exploration rights will result in a profitable commercial mining operation. As a result of these uncertainties, no assurance can be given that Victory Nickel's exploration programs will result in the establishment or expansion of resources or reserves.

### ***Evaluation and Development Projects***

In general, evaluation and development projects have no operating history upon which to base estimates of future cash operating costs. For evaluation and development projects such as the mineral resource properties owned by Victory Nickel, estimates of proven and probable reserves are, to a large extent, based upon the interpretation of geological data obtained from drill holes and other sampling techniques and feasibility studies. This information is used to calculate estimates of the capital cost, cash operating costs based upon anticipated tonnage and grades of ore to be mined and processed, the configuration of the ore body, expected recovery rates, comparable facility and equipment operating costs, anticipated climatic conditions and other factors. In addition, there remains to be undertaken certain feasibility and/or development preparation work on the projects that could adversely impact estimates of capital and operating costs required for the development of the projects. Costs necessary to develop the projects could be significant and have a direct impact on the economic evaluation of the projects. As a result, it is possible that the actual capital cost, cash operating costs and economic returns of the projects may differ from those currently estimated. The costs estimated under the Minago FS for Minago differed from the Preliminary Economic Assessment and may differ again upon actual development.

### ***Frac Sand Industry***

Frac sand processing is a new business for Victory Nickel. The industry is closely linked to the oil and gas industry and is therefore affected by economic factors impacting that industry, including the effect of future cycles based on historic experience. Demand for frac sand is influenced by many factors, including: global and regional economic and political events and conditions, fluctuations in pricing and availability of oil and gas and other energy sources, demand for oil and gas products, demand for cars and other vehicles, technological innovation impacting alternative energy sources, changes in the regulatory framework for mining and processing frac sand and the hydraulic fracturing industry. The oil and gas industry can be prone to sudden, unexpected production slowdowns which may impact exploration, development, production and well completion activities. These factors, such continuing low price of oil, cannot readily be predicted or controlled. Negative developments could cause the demand for frac sand products to decline which could have and have had adverse effects on business, financial condition, results of operations, cash flows and prospects.

With respect to the frac sand industry itself, risks include: changes in transportation availability and pricing, inclement or hazardous weather conditions from flooding or climate change, environmental hazards, industrial accidents, changes in the regulatory framework impacting mining, processing and the fracking industries in both Canada and the US, inability to procure sand in the required quantities or qualities, inability to obtain replacement parts or equipment on a timely basis, reduction in the availability of water for processing, inability to hire, train and retain qualified staff at acceptable rates; and other technical difficulties or failures. Any prolonged downtime could impact deliveries and reputation.

The fracking industry has been hailed as significantly contributing to North America's energy self-sufficiency. A combination of techniques is used, any changes impacting the use of frac sand as a proppant through regulation or technological innovation may negatively impact the frac sand industry. In addition, heightened political, regulatory and public scrutiny of hydraulic fracturing practices could potentially expose the Company or its customers to increased legal and regulatory proceedings, and any such proceedings could be time-consuming, costly or result in substantial legal liability or significant reputational harm.

### ***Competition***

The mineral exploration business is highly competitive in all of its phases. Victory Nickel competes with numerous other companies and individuals, including competitors with greater financial, technical and other resources than Victory Nickel, in the search for and acquisition of exploration and development rights on attractive mineral properties. Victory Nickel's ability to acquire exploration and development rights in the future will depend not only on its ability to develop the properties on which it currently has exploration and development rights, but also on its ability to select and acquire exploration and development rights on other suitable properties. There is no assurance that Victory Nickel will compete successfully in acquiring exploration and development rights on such other properties or in securing customers, sand supplies or other resources such as transportation.

Victory Nickel also faces competition in the frac sand market with respect to its frac sand business and there is no assurance that Victory Nickel will compete successfully in processing and selling frac sand in such market. Frac sand is a proppant used in the completion and re-completion of oil and natural gas wells to stimulate and maintain oil and natural gas production through the process of hydraulic fracturing. Frac sand is the most commonly used proppant and is less expensive than other proppants, such as resin-coated sand and manufactured ceramics. A significant shift in demand from frac sand to other proppants; from the Company's Northern White frac sand sourced in the United States

which is generally of higher quality than, and sells at higher prices than, Canadian domestically-sourced frac sand; or the development of new processes to replace hydraulic fracturing altogether, could cause a decline in the demand for the frac sand the Company processes and result in a material adverse effect on the Company's financial condition and results of operations. If significant new reserves of raw frac sand are discovered and developed, and those frac sands have similar characteristics to the raw frac sand processed by the Company, the Company's ability to maintain or acquire contracts may be negatively impacted which could have a material adverse effect on the Company's results of operations and cash flows over the long term. Additionally, quality sand supply is a limited resource and the presently-identified sources are a significant distance away from the 7P Plant which provides logistical challenges in securing timely railcar and other transportation at acceptable prices.

## **Operational Risks**

### ***Limited History of Operations***

Victory Nickel has no history of earnings and limited financial resources. Victory Nickel currently has no operating mines and its ultimate success may depend on the ability of active mining operations to generate cash flow in the future, as well as its ability to access capital markets for its development requirements. There is no assurance that Victory Nickel will earn profits in the future. Significant capital investment will be required to achieve commercial production at Victory Nickel's existing nickel projects. There is no assurance that Victory Nickel will be able to raise the required funds to continue these activities.

Frac sand processing represents a relatively new initiative for Victory Nickel. While the Company attempted to mitigate the risks of entering the frac sand market through the hiring of experienced personnel, initial business projections have not yet been achieved primarily due to circumstances outside of the Company's control, as discussed above. While the 7P Plant continues to operate on an as-needed basis, there can be no assurance when or if full-time operations will resume.

### ***Frac Sand Processing Operations***

The 7P Plant is the Company's only frac sand processing facility. Any adverse development at the 7P Plant or in the end markets the 7P Plant serves, including adverse developments due to catastrophic events or weather, decreased demand for commercial silica products, a decrease in the availability of transportation services or adverse developments affecting the Company's customers, as has occurred, could, and have, had a material adverse effect on the Company's financial condition and results of operations. The availability of suitably-qualified staff at acceptable prices also represents a risk.

The procurement, production and delivery of frac sand can be logistically complex – transportation costs represent a significant portion of frac sand costs. Unavailability of appropriate transportation and rail cars or lines on a timely basis may impact turnaround and cause delays in deliveries. Changes in respective transportation costs or decreases in dependability may, and have, impaired the Company's ability to receive and/or deliver product with adverse effects on costs, revenues and reputation. Further, changes to logistics to reflect changed demand may not be able to occur on a timely basis, resulting in adverse effects on the cost profile.

Processing frac sand includes substantial costs for energy – electricity and gas – as well as water. Problems in securing sufficient energy supply at appropriate prices would have impact on operating costs and the ability to recover those increased costs may be impaired.

The specifications for frac sand are detailed; maintaining a robust quality control process is key to producing a high-quality product. Failure to do so could cause lost revenues and lost reputation.

### ***Development Targets, Permitting and Operational Delays***

There can be no assurance that Victory Nickel will be able to complete the planned development of its projects on time or on budget due to, among other things, delays in receiving required consents, permits and registrations, the delivery and installation of plant and equipment and cost overruns, or that the current personnel, systems, procedures and controls will be adequate to support Victory Nickel's operations. Any failure to meet development targets or other operational delays or inadequacies could have a material adverse effect. In particular, while the Company is confident it has complied with the conditions of the EAL and has filed, with the government of Manitoba, an EAP to amend its EAL providing for the relocation of the Minago project tailings impoundment to an area much more suitable than previously proposed in the Minago FS, there is no guarantee that the EAP will be approved or that an amendment to the EAL will be granted.

The Company's frac sand business has since its inception been reliant upon third parties to supply northern white feedstock for its 7P Plant. Any difficulties on the part of these suppliers with respect to securing, maintaining or extending permits for its properties and operations, including appropriate water rights, may have adverse effects on the supply of sand.

### **Resources and Reserves**

The figures for mineral resources and mineral reserves are estimates and no assurance can be given that the anticipated level of recovery and/or grades of mineral reserves or mineral resources will be realized. Moreover, short-term operating factors relating to ore reserves and resources, such as the need for orderly development of an ore body or the processing of new or different ore grades, may cause a mining operation to be unprofitable in any particular accounting period.

The Company's frac sand business in its present phase is reliant upon a handful of suppliers for its product. The Company has no resources or reserves of its own that can presently be exploited; although it has announced resources on the Bear Coulee option in Wisconsin. Permitting this property for production is expected to take several years. The frac sand resource at Minago is not contemplated to be developed until either phase three of the frac sand initiative or as part of the Minago FS which requires significant financing to be developed.

### **Title Risks**

Victory Nickel's ability to hold various mineral rights require licences, permits and authorizations and, in some cases, renewals of existing licences, permits and authorizations from various governmental and quasi-governmental authorities. Management believes that Victory Nickel currently holds or has applied for all necessary licences, permits and authorizations to carry on the activities which Victory Nickel is currently conducting and to hold the mineral rights Victory Nickel currently holds under applicable laws and regulations in effect at the present time. Management also believes that Victory Nickel is complying in all material respects with the terms of such licences, permits and authorizations. However, Victory Nickel's ability to obtain, sustain or renew such licences, permits and authorizations on acceptable terms is subject to changes in regulations and policies and to the discretion of the applicable governmental and quasi-governmental bodies.

### **Insurance Risk**

Victory Nickel faces all of the hazards and risks normally incidental to the exploration and development of base metals, any of which could result in damage to life or property, environmental damage and possible legal liability for any or all such damage caused. Victory Nickel's activities may be subject to prolonged disruptions due to weather conditions depending on the location of operations in which Victory Nickel has interests; not all such risks are insurable.

Similarly, the frac sand processing plant faces many hazards and risks arising from the transportation and processing of frac sand materials, any of which could result in the matters described above. Again, not all such risks are insurable.

### **Regulatory Risks**

#### **Government Regulation**

Existing and possible future environmental and social impact legislation, regulations and actions, including the regulation of air and water quality, mining reclamation, solid and hazardous waste handling and disposal, the promotion of occupational health and safety, the protection of wildlife and ecological systems and the protection of the societies and communities of indigenous peoples, could cause significant expense, capital expenditures, restrictions and delays in activities, the extent of which cannot be predicted and which may well be beyond Victory Nickel's capacity to fund. Environmental laws are becoming more stringent and actively enforced. Environmental and social impact studies may be required for some operations and significant fines and clean-up responsibilities may be assessed for companies causing damage to the environment in the course of their activities.

#### **Economic, Political, Judicial, Administrative, Taxation or Other Regulatory Factors**

Victory Nickel may be adversely affected by changes in economic, political, judicial, administrative, taxation or other regulatory factors in the areas in which Victory Nickel does or will operate and holds its interests, as well as unforeseen matters. In particular, the fracking industry is often at the forefront of public attention whether or not deserved. Nonetheless, this provokes attention and scrutiny.

### **Other Risks**

#### **Environmental and Health Risks**

The Company has no significant exposure to environmental or health risks from its exploration and development activities, although this will change as the Company's projects approach production (a normal characteristic of mineral

industry projects). Lynn Lake, acquired pursuant to a takeover bid and recently subject to option with Corazon, is a former operating mine; however indemnifications exist from the Manitoba Government with respect to any pre-existing environmental concerns at that property.

The frac sand operation involves processing silica sand. In addition to environmental regulation, the Company is subject to laws and regulations relating to human exposure to crystalline silica under the Occupational Health and Safety Act. Workplace exposure to crystalline silica is monitored; the occupational exposure limits in Alberta for respirable crystalline silica are among the lowest in Canada and the US.

### ***Key Personnel***

Victory Nickel relies on a limited number of key consultants and senior management and there is no assurance that Victory Nickel will be able to retain such key consultants or other senior management. The loss of one or more such key consultants or members of senior management, if not replaced, could have a material adverse effect on Victory Nickel's business, financial condition and prospects. Directors and management have accepted deferrals of remuneration in order to assist the Company through the economic turmoil; however, this potentially adds to the risk of losing experienced personnel.

### ***Conflicts of Interest***

Certain of the Company's directors and officers are also directors and officers of other natural resource companies. Consequently, there exists the possibility for such directors and officers to be in a position of conflict. Any decision made by any of such directors and officers relating to Victory Nickel will be made in accordance with their duties and obligations to deal fairly and in good faith with Victory Nickel and such other companies.

### ***Investments and Other Agreements with Resource Companies***

In addition, Victory Nickel makes, from time to time, investments in the common shares of publicly-traded companies in the junior natural resources sector or may enter into option or other agreements therewith. These companies are subject to similar risks and uncertainties as is Victory Nickel, and Victory Nickel's investments in and agreements with these companies are subject to similar areas of risk as noted above. Victory Nickel seeks to manage its exposure by ensuring that appropriate recourse is included in such agreements upon the counterparty's or assignee's failure to meet contractual obligations.

### **Summary**

The future success of the Company is subject to a number of risk factors that are common to the junior natural resources sector and frac sand producers. These include the extent to which it can outline natural resources on its properties and establish the economic viability of developing those properties and the political, economic and legislative stability of the territories in which the Company's interests are located. Another significant factor is the ability of the Company to obtain necessary financing or to find strategic partners to fund expenditure commitments as they fall due, as the Company currently has limited funds. Furthermore, the development of any nickel resource interest may take years to complete and the resulting income, if any, from the sale of any nickel or by- or co-products produced by the Company is largely dependent upon factors that are beyond its control, such as costs of development, operating costs and the market value of the end product.

The Company has attempted to mitigate some of the risks associated with securing financing for the maintenance and advancement of its nickel properties through its entry into the frac sand processing business, however the frac sand business also has its own set of risks as indicated earlier, and of which investors should be aware.

## **FORWARD-LOOKING STATEMENTS**

This MD&A contains forward-looking information. All statements, other than statements of historic fact, that address activities, events or developments that the Company believes, expects or anticipates will or may occur in the future (including, without limitation, statements regarding estimates and/or assumptions in respect of production, revenue, cash flow, costs, economic return, net present value, mine life and financial models, mineral resource estimates, potential mineralization, potential mineral resources, timing of possible production, the Company's development plans and objectives and the ability of the Company to restructure its debt with the relevant lenders and the ability of the Company to pay future interest and other payments in connection with such debts) constitute forward-looking information

The forward-looking information contained in this MD&A reflects the current expectations or beliefs of the Company based on information currently available to the Company. Forward-looking information is subject to a number of risks



and uncertainties that may cause the actual results of the Company to differ materially from current expectations, including, but not limited to, an unwillingness of the Company's lenders to refinance the Company's debts on terms favourable to the Company or at all and the ability of the Company to continue selling frac sand. Additionally, if the Company is unable to restructure its debts, obtain additional financing and/or continue generating revenue through the sale of frac sand, the Company may be required to curtail activities and/or liquidate its assets or the Company's creditors may seek to seize its assets.

Factors that could cause actual results or events to differ materially from current expectations include, among other things: uncertainty of estimates of capital and operating costs, production estimates and estimated economic return; the possibility that actual circumstances will differ from estimates and assumptions; uncertainties relating to the availability and costs of financing needed in the future; failure to establish estimated mineral resources; fluctuations in commodity prices and currency exchange rates; inflation; recoveries being less than those indicated by the testwork carried out to date (there can be no assurance that recoveries in small scale laboratory tests will be duplicated in large tests under on - site conditions or during production); changes in equity markets; operating performance of facilities; environmental and safety risks; delays in obtaining or failure to obtain necessary permits and approvals from government authorities ; unavailability of plant, equipment or labour; inability to retain key management and personnel; changes to regulations or policies affecting the Company's activities in exploration and development and the frac sand processing business; the uncertainties involved in interpreting geological data; and the other risks disclosed under the heading "Risks and Uncertainties" and elsewhere. Any forward-looking statement speaks only as of the date on which it is made and, except as may be required by applicable securities laws, the Company disclaims any intent or obligation to update any forward- looking information, whether as a result of new information, future events or results or otherwise. Although the Company believes that the assumptions inherent in the forward-looking information are reasonable, forward-looking information is not a guarantee of future performance and accordingly undue reliance should not be put on such information due to the inherent uncertainty therein.

**April 16, 2018**