

Hydro66 Holdings Corp

Management Discussion & Analysis For the nine months ended September 30, 2018

1. Date - November 27, 2018

This Management's Discussion and Analysis ("MD&A") is dated November 27, 2018, unless otherwise indicated, and should be read in conjunction with the accompanying unaudited condensed interim consolidated financial statements for the three and nine months ended September 30, 2018 ("Q3 2018") and the audited financial statements of Hydro66 UK Limited for the year ended December 31, 2017. This MD&A was written to comply with the requirements of National Instrument 51-102 – Continuous Disclosure Obligations. Results are reported in Canadian dollars, unless otherwise noted. In the opinion of management, all adjustments (which consist only of normal recurring adjustments) considered necessary for a fair presentation have been included. The results presented for Q3 2018 are not necessarily indicative of the results that may be expected for any future period.

The Company applies International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board and interpretations issued by the IFRS Interpretations Committee.

Cautionary Note Regarding Forward-Looking Information

This MD&A contains certain forward-looking information and forward-looking statements, as defined in applicable securities laws (collectively referred to herein as "forward-looking statements"). These statements relate to future events or the Company's future performance. All statements other than statements of historical fact are forward-looking statements. Often, but not always, forward-looking statements can be identified by the use of words such as "plans", "expects", "is expected", "budget", "scheduled", "estimates", "continues", "forecasts", "projects", "predicts", "intends", "anticipates" or "believes", or variations of, or the negatives of, such words and phrases, or state that certain actions, events or results "may", "could", "would", "should", "might" or "will" be taken, occur or be achieved. Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results to differ materially from those anticipated in such forward-looking statements. The forward-looking statements in this MD&A speak only as of the date of this MD&A or as of the date specified in such statement.

Inherent in forward-looking statements are risks, uncertainties and other factors beyond the Company's ability to predict or control. For a complete list of the factors that could affect the Company, please make reference to those risk factors referenced in Part VI – "Risk Factors" of the Filing Statement of the Company dated June 8, 2018. Readers are cautioned that such risk factors, uncertainties and other factors are not exhaustive. Actual results and developments are likely to differ, and may differ materially, from those expressed or implied by the forward-looking statements contained in this MD&A.

Forward-looking statements involve known and unknown risks, uncertainties and other factors that may cause actual results to differ materially from those anticipated in such forward-looking statements. The forward-looking statements in this MD&A speak only as of the date of this MD&A or as of the date specified in such statement. Specifically, this MD&A includes, but is not limited to, forward-looking statements regarding: the Company's ability to meet its working capital needs at the current level for the next twelve-month period; management's outlook regarding future trends; sensitivity analysis on financial instruments, which may vary from amounts disclosed; and general business and economic conditions.

All forward-looking statements herein are qualified by this cautionary statement. Accordingly, readers should not place undue reliance on forward-looking statements. The Company undertakes no obligation to update publicly, or otherwise revise, any forward-looking statements, whether as a result of new information or future events or otherwise, except as may be required by law. If the Company does update one or more forward-looking statements, no inference should be drawn that it will make additional updates with respect to those or other forward-looking statements, unless required by law.

Steps to the Listing of Hydro66 Holdings Corp.

(i) Corporate Reorganization

On February 28, 2018 Hydro66 UK Limited was acquired by Arctic Blockchain Limited. The Acquisition resulted in the former shareholders of Hydro66 UK Limited holding the majority interest in the Company. A timeline of events and details of the net assets which were acquired are detailed below.

Hydro66 UK Limited and the shareholders of Hydro66 UK Limited entered into a share purchase agreement, dated February 15, 2018 pursuant to which Arctic issued 100,000,000 common shares to the Hydro66 UK Limited shareholders to acquire (the “Acquisition”) all of the issued and outstanding common shares of Hydro66 UK Limited. The Acquisition was completed on February 28, 2018.

The Acquisition resulted in the former shareholders of Hydro66 UK Limited holding the majority interest in Arctic. The Acquisition is not considered to be a business combination for accounting purposes as Arctic is not considered to be a business for accounting purposes. The Acquisition has been accounted for in the condensed consolidated interim financial statements as the continuation of the financial statements of Hydro66 UK Limited together with an issuance of common shares, equivalent to the common shares held by the former shareholders of Arctic, and a recapitalization of the equity of Hydro66 UK Limited. In accounting for this transaction:

- Hydro66 UK Limited was deemed to be the parent company for accounting purposes. Accordingly, its net assets were included in the Consolidated Interim Statement of Financial Position at their historical book value; and
- control of the net assets of Arctic was acquired on the Effective Date.

For comparative purposes, the condensed consolidated interim financial statements continuity presented herein is that of Hydro66 UK Limited.

The table below shows the net assets of Arctic which were effectively acquired by Hydro66 UK Limited on February 28, 2018.

	\$
ASSETS	
Cash	35,503
GST receivable	41,758
Trade and other receivables	704,024
Advance to Hydro66 UK Limited	<u>9,000,000</u>
Total current assets	<u>9,781,285</u>
TOTAL ASSETS	<u><u>9,781,285</u></u>
Accounts payable and accrued liabilities	<u>11,492</u>
TOTAL LIABILITIES	<u>11,492</u>
SHAREHOLDERS’ EQUITY	
Share capital	50,000
Debenture subscriptions	10,000,000
Deficit	<u>(280,207)</u>
TOTAL SHAREHOLDERS’ EQUITY	<u>9,769,793</u>
TOTAL LIABILITIES AND SHAREHOLDERS’ EQUITY	<u><u>9,781,285</u></u>

(ii) *Transaction*

On March 12, 2018, Arctic entered into a letter of intent with Caza providing for the amalgamation of Caza and Arctic to form the Company. On June 6, 2018, Caza and Arctic entered into a business combination agreement (the “Amalgamation Agreement”) whereby Arctic would complete an amalgamation pursuant to the Amalgamation Agreement under the provisions of the BCBCA (the “**Amalgamation**”) and upon the completion of the Amalgamation, Arctic would become a reporting issuer listed on the CSE. The Amalgamation was completed on June 8, 2018 and on June 13, 2018 Hydro66 Holdings Corp listed on the Canadian Securities Exchange (CSE:SIX). Prior to the Amalgamation, the common shares of Caza were consolidated on a 76.3945 to 1 basis, following which there were 2,000,000 common shares issued and outstanding immediately prior to the Amalgamation.

The condensed consolidated interim statement of financial position gives effect to the following assumptions and adjustments:

- (a) Arctic is the deemed acquirer and issued 2,000,000 common shares to acquire 100% of the issued and outstanding common shares of Caza.
- (b) Share capital, contributed surplus and the deficit of Caza are eliminated.

The fair value of the consideration was as follows:

<u>Issuance of 2,000,000 common shares to the former shareholders of Caza</u>	<u>\$1,000,000</u>
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The allocation of the consideration is as follows:

Trade and other receivables	\$3,699
Trade and other payables	(\$30,895)
Listing costs expensed	\$972,804
<u>Value attributed to shares issued</u>	<u>\$1,000,000</u>

Pursuant to the terms of the Amalgamation Agreement, each former shareholder of Arctic received one (1) post-consolidation common share of Caza for every one (1) Arctic common share held by such shareholder. Arctic had 105,000,000 shares outstanding prior to the completion of the Amalgamation. Immediately prior to listing on the CSE an additional 20,000,000 Caza common shares and 20,000,000 common share purchase warrants, exercisable at \$0.75 for a period of two years from June 8, 2018 in connection with the automatic conversion of the convertible debentures in the principal amount of \$10,000,000 held by Arctic securityholders, were issued.

Non-GAAP Measures

This MD&A presents certain non-GAAP (“GAAP” refers to Generally Accepted Accounting Principles) financial measures to assist readers in understanding the Company’s performance. These non-GAAP measures do not have any standardized meaning and therefore are unlikely to be comparable to similar measures presented by other issuers and should not be considered in isolation or as a substitute for measures of performance prepared in accordance with GAAP. Management uses these non-GAAP measures to supplement the analysis and evaluation of operating performance.

Throughout this MD&A, the following terms are used, which are not found in the Chartered Professional Accountants of Canada Handbook and do not have a standardized meaning under GAAP.

EBITDA (Earnings before Interest, Taxes, Depreciation, and Amortization)

- “EBITDA” represents net income or loss excluding net finance income or expense, income tax or recovery, depreciation, and amortization.
- “Adjusted EBITDA” represents EBITDA adjusted to exclude share-based compensation, and costs associated with one-time transactions (such as listing fees).

2. Overall performance

The principal activities of Hydro66 during the period were, and will continue to be, the provision of colocation services. The Company also contributes a small amount of its computing power to digital currency pools. For its contribution to the pools the Company receives income in the form of digital currencies.

The Company continues to enhance its position in the North of Sweden. During the nine-month period ended September 30, 2018 Hydro66 opened three new data halls with a total capacity of 11.6 MW (Megawatts), increasing total capacity to 15.2 MW. A further data hall with 4 MW capacity was completed in October 2018, increasing total capacity to 19.2 MW. Hydro66's growth strategy is largely to attract corporate clients on long term hosting contracts, which in turn aims to fund the delivery of additional data center space.

Data centers are increasingly under the spotlight as being energy-intensive, and with that scrutiny comes the need for innovation and transparency. Large numbers of companies are realising the environmental and cost benefits of locating processing power in a cool climate close to abundant green power. The Hydro66 data centre is ideally located to deliver these benefits. Hydro66 is uniquely positioned to deliver colocation for high performance computing, enterprise data space and digital currency verification services (self-mining).

Cash and digital currencies

The Company closed the period to September 30, 2018 with closing cash and cash equivalents of \$2.2m (December 31, 2017: \$1.7m); and closing digital currencies recorded as intangible assets of \$0.5m (December 31, 2017: \$0.2m).

Net assets

Net assets at September 30, 2018 increased by \$7.1m to \$16.5m (December 31, 2017: \$9.4m). The \$7.1m increase in net assets during the nine-month period to September 30, 2018 was as a result of the expansion of the site to 19.2 MW which was fully completed in the first week of October 2018, adding \$7.9m to Property, Plant and Equipment, and a \$0.8m depreciation charge during the period.

The expansion was funded by the issue of a debenture in Arctic in February 2018 for \$10,000,000. Prior to listing on the CSE an additional 20,000,000 Caza common shares and 20,000,000 common share purchase warrants, exercisable at \$0.75 for a period of two years from June 8, 2018 in connection with the automatic conversion of the convertible debentures in the principal amount of \$10,000,000 held by Arctic securityholders, were issued.

Analysis of financial performance

During the three months to September 30, 2018 ("Q3") Hydro66 recorded its largest revenue quarter with \$2,880,058, a 48% increase from the prior quarter revenue of \$1,949,060.

Operations and execution for our site expansion to 15.2 MW during the quarter (and subsequently to 19.2 MW in the first week of October 2018) went as planned, however, financial performance was negatively impacted by market conditions relating to the price of power. Direct costs of power rose from 66% of revenue to 74% of revenue.

Adjusted EBITDA profit for the quarter was \$71,499 against a prior quarter adjusted EBITDA profit of \$279,599, reflecting the impact of increased power prices in the quarter and additional management fees from operating in Canada.

No dividends were paid during the period.

The table below shows the total and split of revenue by reportable segment for the three-month period to September 2018 compared to the same period in the prior year. The table also shows the total and split of revenue for the nine-month period to September 2018 compared to the same period in the prior year.

	3 months to September 2018		3 months to September 2017		9 months to September 2018		9 months to September 2017	
	\$m	% of total	\$m	% of total	\$m	% of total	\$m	% of total
Colocation	2.8m	97%	0.4m	63%	5.4m	95%	0.8m	53%
Digital currency verification services	0.1m	3%	0.3m	37%	0.3m	5%	0.7m	47%
Total	2.9m		0.7m		5.7m		1.5m	

In the nine-month period to September 2018 colocation made up 95% of the revenue compared to 53% for the same period last year representing the shift of the business from digital currency verification services to the provision of colocation to third party customers.

3. Discussion of operations

The principal activities of Hydro66 during the period were, and will continue to be, the provision of colocation services.

Hydro66 delivers low-cost, environmentally-friendly colocation services. Using locally generated clean green hydropower, Hydro66's first data centre is located in the leading cloud and data centre cluster in the Nordics, in Northern Sweden. This gives customers the ability to reduce their carbon footprint while providing cost savings against the traditional colocation model.

The Company also contributes a small amount of its computing power to digital currency pools. For its contribution to the pools the Company receives income in the form of digital currencies.

Three Months Ended September 30, 2018 Compared to Three Months Ended June 30, 2018

During the three months ended September 30, 2018 ("Q3") Hydro66 reported its largest revenue quarter with \$2,880,058, a 48% increase on the revenue for the three-month period ended June 30 ("Q2"), 2018 of \$1,949,060. The primary factor for the increase in revenue is attributable to the increase in capacity available and sold to customers. During Q3 a total of 30.9 MW was invoiced to customers, a 40% increase on Q2, when 22 MW was invoiced to customers.

During Q3 2018 the Company reported an adjusted EBITDA profit of \$71,499 compared to an adjusted EBITDA profit of \$279,599 for Q2 2018. The primary factor for the reduction in profit is attributable to the lower exchange gains realised from the exchange of digital currency of \$139,265 and the increase in marketing and management fees. During Q3 the Company engaged an investor relations consultant and two market support consultants.

Nine Months Ended September 30, 2018 Compared to Nine Months Ended September 30, 2017

During the nine-month period ended September 30, 2018 (the "2018 period") the Company recorded an adjusted EBITDA loss of \$494,451, an increase of \$190,995 from the adjusted EBITDA loss of \$303,456 reported for the nine months ended September 30, 2017 (the "2017 period"). The increase in loss in the 2018 period is primarily attributed to the increase in staff and operational costs as a result of expanding the site from 3.2 MW capability at the end of September 2017 to 15.2 MW capability at the end of September 2018.

4. Summary of quarterly results

Selected Financial Information

The following selected financial information is derived from the unaudited condensed consolidated interim financial statements of the Company.

	Fiscal 2018			Fiscal 2017				Fiscal 2016
	Sep-18	Jun-18	Mar-18	Dec-17	Sep-17	Jun-17	Mar-17	Dec-16
	2018	2018	2018	2017	2017	2017	2017	2016
	\$	\$	\$	\$	\$	\$	\$	\$
Operations:								
Revenue	2,880,058	1,949,060	875,423	771,117	719,931	589,527	236,087	310,226
Comprehensive income / (loss) from continuing operations	(841,488)	(2,437,858)	(1,402,042)	(848,400)	417,432	301,686	(535,903)	(409,235)
Basic loss per share	(0.007)	(0.019)	(0.013)	(0.780)	0.384	0.278	(0.583)	(0.445)
Diluted loss per share	(0.005)	(0.013)	(0.008)	(0.780)	0.384	0.278	(0.583)	(0.445)
Dividends per share	Nil	Nil	Nil	Nil	Nil	Nil	Nil	Nil

Revenue has increased quarter on quarter for the last six quarters reflecting the increasing amounts of capacity sold to customers. The quarter to June 30, 2018 included acquisition expenses and listing expenses of \$1,413,421 and share-based compensation of \$748,450. The quarter to September 30, 2018 included share-based compensation of \$265,238.

The quarters to June 30, 2017 and September 30, 2017 included exchange gains from the sale of digital currency earned in previous periods.

5. Liquidity

On 15 February 2018, a sale purchase agreement was executed to sell 100% of the company to Arctic Blockchain Ltd. As consideration for the sale the shareholders of Hydro66 UK Ltd were issued 80% of the shares and rights to subscribe to further shares in Arctic Blockchain Ltd.

To accelerate the growth plan, on 1 March 2018 Arctic Blockchain Limited transferred \$9.0m to Hydro66. This ensured that the existing growth plan to 19.2 MW could be delivered in 2018.

Hydro66 has no debt. Hydro66 has no capital lease obligations. Hydro66 has no other material long term obligations.

The Company's principal activity is the provision of colocation services. The condensed consolidated interim financial statements for the three and nine months ended September 30, 2018 have been prepared on a going concern basis which assumes that the Company will be able to realize its assets and discharge its liabilities in the normal course of business operations for the foreseeable future. During the nine months ended September 30, 2018 the Company invested in expanding its capacity. 7.6 MW became available for sale in Q2, a further 4 MW in September 2018 and a further 4 MW in October 2018. The Company expects to realize these assets to discharge its liabilities in the normal course of business operations for the foreseeable future. During the nine months ended September 30, 2018 the Company incurred a loss of \$3,701,158, an adjusted EBITDA loss of \$494,451 and, as at September 30, 2018, the Company had positive working capital of \$1,409,339 and an accumulated deficit of \$8,977,484.

6. Capital Resources

As September 30, 2018 Hydro66 had capital commitments of \$0.3m for the remaining fit out of one data hall and for the completion of the groundworks for three additional data halls. Hydro66 had the funds in place, both in cash and in digital currency assets held, to meet these commitments.

There was no expenditure not yet committed at September 30, 2018 required to complete the expansion to 19.2 MW.

7. Off-Balance Sheet Arrangements

Hydro66 does not have any off-balance sheet arrangements.

8. Transactions with Related Parties

During the nine months ended September 30, 2018, Hydro66 UK Limited repaid a loan note to David Rowe of \$75,575 (nine months to September 30, 2017: nil).

During the nine months ended September 30, 2018, Croft Legal Services Ltd, of which Richard Croft is a Director, provided legal services to Megamining Ltd of \$191,432 (nine months to September 30, 2017: \$100,657).

During the nine months ended September 30, 2018, 0920 Media AB (brand name Meramedia), of which Anne Graf is a director, provided marketing services to Hydro66 Svenska AB of \$33,339 (nine months to September 30, 2017: \$86,845).

During the nine months ended September 30, 2018, Hydro66 Services AB, provided colocation services to B-chain e-services AB, of which Anne Graf was a director, of \$799,904 (nine months to September 30, 2017: \$431,194). Anne Graf resigned as a director from B-chain e-services AB on June 21, 2018.

9. Proposed Transactions

There are no proposed transactions.

10. Basis of Preparation and Critical Accounting Policies

The condensed consolidated interim financial statements have been prepared in accordance with IAS 34, Interim Financial Reporting (“IAS 34”), as issued by the International Accounting Standards Board (“IASB”), and its interpretations, using accounting policies consistent with International Financial Reporting Standards (“IFRS”).

The preparation of the financial statements in conformity with IFRSs requires the use of certain critical accounting estimates which are detailed below. These accounting policies were consistently applied for all the periods presented.

Revenue

Revenue is measured at the fair value of the consideration received or receivable, and represents amounts receivable for services, stated net of discounts and returns. The Company recognises revenue when the amount of revenue can be reliably measured; when it is probable that future economic benefits will flow to the entity; and when specific criteria have been met for each of the Company's activities. Revenue represents amounts invoiced for the provision of data centre services, including space and power.

The Company also recognizes revenue from the provision of transaction verification services within digital currency networks. As consideration for these services, the Company receives digital currency from each specific network in which it participates.

Revenue is measured based on the fair value of the currency received. The fair value is determined using the spot price of the currency on the date of receipt. The currency is recorded on the statement of financial position, as an intangible asset at the spot rate. Realised gains or losses, as well as gains or losses on the sale of currency for traditional (fiat) currencies are included in profit and loss. There is currently no specific definitive guidance in IFRS or alternative accounting frameworks for the accounting of digital currencies and management has exercised significant judgement in determining appropriate accounting treatment. Management has examined various factors surrounding the substance of the Company's operations and the guidance in IAS 18, Revenues, including the stage of completion being the completion and addition of a block to a blockchain and the reliability of the measurement of the digital currency received. In the event authoritative guidance is enacted by the IASB, the Company may be required to change its policies which could result in a change in the Company's financial position and earnings.

Intangible assets - Digital currency valuation

Digital currencies consist of cryptocurrency denominated assets such as Bitcoin and Litecoin; and are included in non-current assets as an intangible asset. Digital currencies are treated as intangible assets and carried at the spot rate they were earned at. The fair value is determined using the spot price of the currency on the date of receipt. Gain or loss is recognised in the profit and loss account at the point of sale. Digital currency is not amortised as the directors consider that it has an indefinite useful life. The digital currency market is still a new market and is highly volatile; historical prices are not necessarily indicative of future value; a significant change in the market prices for digital currencies would have a significant impact on the Company's earnings and financial position.

11. Changes in accounting policies

No changes in accounting policies are expected.

12. Share Capital

As at the date of this MD&A, the Company has issued, and outstanding share capital comprised of 127,000,000 Common Shares, 8,275,000 Stock Options all at an exercise price of \$0.50, and 50,096,000 Warrants outstanding at exercise prices ranging from \$0.50 to \$0.75 per share.