

PhotoChannel Networks Inc.
Consolidated Balance Sheet
(Expressed in Canadian Dollars)
(Unaudited - Prepared by Management)

ASSETS	<u>June 30, 2000</u>	<u>June 30, 1999</u>
Current assets		
Cash and cash equivalents	\$ 3,049,447	\$ 226,878
Marketable securities	5,950,000	-
Cash held in escrow (Note 1)	5,000,000	-
Accounts receivable	99,907	53,195
Inventory	14,558	23,031
Prepaid expenses	429,923	34,085
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	14,543,835	337,189
 Capital assets, cost	 1,524,666	 803,849
Less amortization	(529,348)	(443,765)
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	995,318	360,084
 Other assets		
Deferred web site development costs	2,557,370	146,712
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	\$ 18,096,523	\$ 843,985
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LIABILITIES AND SHAREHOLDERS' EQUITY		
Current liabilities		
Accounts payable	\$ 320,669	\$ 395,774
Accrued payables	11,819	145,338
Convertible debentures	-	208,333
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	332,488	749,445
 Shareholders' equity		
Share capital	19,957,277	9,531,186
Special warrants	10,865,302	-
Deficit	(13,058,544)	(9,436,646)
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	17,764,035	94,540
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	\$ 18,096,523	\$ 843,985
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See accompanying notes to the consolidated financial statements

PhotoChannel Networks Inc.
Consolidated Statements of Loss and Deficit
(Expressed in Canadian Dollars)
(Unaudited - Prepared by Management)

	Quarter Ended		Nine Months Ended	
	June 30, 2000	June 30, 1999	June 30, 2000	June 30, 1999
Revenue	\$ 27,429	\$ 31,376	\$ 94,111	\$ 128,630
Cost of goods sold	2,165	2,273	7,304	8,029
Gross profit	25,264	29,103	86,807	120,601
Operating expenses				
Research & development	78,872	69,986	565,992	194,433
Sales & marketing	462,385	82,673	577,043	140,872
General & administration	749,118	405,050	1,703,675	1,045,642
Amortization	23,699	27,206	66,797	82,110
Total expenses	1,314,074	584,915	2,913,507	1,463,057
Loss from operations	(1,188,810)	(555,812)	(2,826,700)	(1,342,456)
Interest income	68,463	18	68,573	9,442
Loss for the period	(1,220,347)	(555,794)	(2,758,127)	(1,333,014)
Deficit, beginning of period	(11,838,197)	(8,880,852)	(10,300,417)	(8,103,632)
Deficit, end of period	\$ (13,058,544)	\$ (9,436,646)	\$ (13,058,544)	\$ (9,436,646)
Loss per share for the period	\$ 0.07	\$ 0.05	\$ 0.15	\$ 0.12
Weighted average number of common shares outstanding	18,257,502	10,795,015	18,257,502	10,795,015

PhotoChannel Networks Inc.
Consolidated Statements of Cash Flows
(Expressed in Canadian Dollars)
(Unaudited - Prepared by Management)

	Nine Months Ended	
	June 30, 2000	June 30, 1999
Cash flows from operating activities		
Loss for the period	\$ (2,758,127)	\$ (1,333,014)
Items not affecting cash		
Amortization	66,797	82,110
Net change in non-cash working capital items		
Change in marketable securities	(5,950,000)	-
Change in accounts receivable	(99,907)	(53,195)
Change in inventory	6,269	7,235
Change in prepaid expenses	(417,447)	79,111
Change in accounts payable	(457,832)	(414,617)
Change in accrued payables	130,338	78,166
	<u>(9,479,909)</u>	<u>(1,554,204)</u>
Cash flows from investing activities		
Purchase of capital assets	(711,553)	(2,368)
Proceeds from sale of capital assets	-	3,603
Deferred web site development costs	(2,557,370)	(146,712)
	<u>(3,268,923)</u>	<u>(145,477)</u>
Cash flows from financing activities		
Issuance of convertible debentures	-	(41,667)
Repayment of convertible debentures	(177,083)	-
Repayment of loan payable	-	(20,000)
Issuance of common shares, net of expenses	9,957,205	2,097,295
Issuance of special warrants, net of expenses	10,865,302	-
Conversion of convertible notes to shares	-	(168,950)
	<u>20,645,424</u>	<u>1,866,678</u>
Increase in cash during the period	7,896,592	166,997
Cash, beginning of period	152,855	59,881
Cash, end of period	<u>\$ 8,049,447</u>	<u>\$ 226,878</u>
Cash consists of		
Cash and cash equivalents	3,049,447	226,878
Cash held in escrow	5,000,000	-
	<u>\$ 8,049,447</u>	<u>\$ 226,878</u>

PhotoChannel Networks Inc.
Notes to Consolidated Financial Statements
(Expressed in Canadian Dollars)
(Unaudited - Prepared by Management)

Unaudited information

The balance sheet as at June 30, 2000 and the statements of loss and deficit, and cash flows for the nine months ended June 30, 2000 and 1999, including the related notes, are unaudited. This unaudited information reflects all adjustments that are, in the opinion of management, necessary to present a fair statement of the results for the interim periods presented. All such adjustments are of a normal recurring nature.

1. Cash held in escrow

Cash held in escrow was released on August 4, 2000.

PhotoChannel Networks Inc. ("PhotoChannel" or the "Company") is an e-commerce company that will be providing online photofinishing services for both digital and conventional photographers from its online photo community at www.photochannel.com. The Company is headquartered in Vancouver, British Columbia, Canada and trades on the Montreal Exchange in Canada (symbol-PNI) and quoted on the OTC-BB (symbol- PHCHF) in the United States.

Company highlights during the quarter include

- On May 1, the Company completed a \$10 million private placement of Special Warrants with Taurus Capital Markets Ltd. ("Taurus"). On May 16, 2000, \$5 million of these funds were released to the Company and the balance placed in escrow pending the fulfillment of certain escrow conditions. These funds were released from escrow on August 4th. Simultaneously, the Company completed a private placement of an additional \$5 million in Special Warrants. These funds were released from escrow on June 19 after the Company received shareholder approval for the financing.
- The Company completed a \$2.3 million private placement of subordinated convertible redeemable debentures with Choices Entertainment Corporation. These debentures were converted to common shares at a price of \$0.50 per share.
- The PhotoChannel.Com Limited Partnership (the "Partnership") was formed and is offering up to a maximum of 2.5 million limited partnership units at a price of \$10 per unit. The net proceeds raised from the sale of these units will be used by the Partnership to develop and operate its on-line photo print business in North America. The Partnership has entered into a joint venture agreement with NewHeights Software Corporation ("NewHeights"), who will undertake the design, development and manufacturing of PhotoChannel USB Card Readers which directly and exclusively batch upload to the PhotoChannel web site images captured with digital cameras on Smart Media and Compact Flash memory cards. The Partnership and NewHeights will participate in the on-line photo print revenue earned from images uploaded to the PhotoChannel web site using the PhotoChannel USB Card Readers.
- The Company entered into a software license agreement with MCL Software Services Inc. ("MCL") whereby MCL grants to PhotoChannel a license to use MCL's print utility software, lab order software and Photoprint 2.1 software to print images uploaded to PhotoChannel's web site. The license grants rights to the Company for a term of five years and contains an exclusivity provision.
- The Company leased office space in Stamford, Connecticut for the US operations headquarters which will serve as the primary on-line photo print fulfillment center. From the data center located in this facility, customers will upload their digital images to the Company's web site, have their print orders processed on the Company's new Fuji Frontier Series 370 Digital Minilabs and receive home delivery of 35 mm quality prints.

Results of Operations

Revenue for the quarter was \$27,429 versus \$31,376 the same quarter last year. Year to date revenue for the nine months ended June 30, 2000 was \$94,111 versus \$128,630 for the nine months ended June 30, 1999. Revenue decreased 27% from the nine month period ended June 30, 1999 due to the absence of several one-time bulk purchase orders of Slides & Sound Plus that occurred in 1999.

The Company's current revenue is generated from the sale of Slides & Sound Plus via orders downloaded from the web site. The Company no longer views Slides & Sound Plus as its' core business and as such, although the product will continue to be advertised for sale, it will not be further developed or supported. Managements' strategy is to earn all future revenue from the sale of online photo print services, the sale of photography equipment and accessories, and revenue from online advertising.

The Company recorded a quarterly loss of \$1,220,347 (\$0.07 per share) compared to a loss of \$555,794 (\$0.05 per share) in the same quarter last year. The year-to-date loss for the nine months ended June 30, 2000 was \$2,758,127

(\$0.15 per share), an increase of 107% as compared to the 1999 year-to-date loss of \$1,333,014 (\$0.12 per share). The increase in the net loss is a result of increased expenditures for research & development, sales & marketing and administration required for the commercial launch of PhotoChannel's online photo print service.

During the quarter ended June 30, 2000, the Company has expensed almost \$80,000 of research & development costs and for the current nine month period, these expenses have increased 191% over the same period last year to \$565,992. This increase is a result of, among other things, additional staffing and consulting expenses, and site peripheral expenses. In addition, \$2,070,000 of research & development costs have been capitalized, of which 1,700,000 pertains to the value of the warrants granted to MCL in consideration for the use and development of their software.

Sales and marketing expenses increased \$436,171 to \$577,043, a 310% increase over the comparable nine months of 1999. This increase was due to the increased focus on investor relations activities for the Company, including the engagement of an outside investor relations consulting firm.

General and administration expenses for the nine months of fiscal 2000, increased 63% over the comparable period in 1999 to the result of higher legal expenses, travel expenses and general corporate administration.

Subsequent Events

- During the third quarter the Company was actively recruiting new executives for the management team. As a result, new management additions include a new President and Chief Operating Officer, as well as Vice Presidents in the areas of Finance, Operations, Corporate Communications, and Marketing.
- The Company has retained the services of Interactive Capital Partners ("ICP"). ICP will assist the Company to expand the services it provides, as well as its customer base, through strategic acquisitions, business combinations, joint ventures or partnering opportunities with other US corporations. ICP is dedicated to growing best-of-breed Internet companies through long-term strategic partnerships with major media and technology companies.

"Geoffrey G. Briant"
Geoffrey G. Briant
Chairman & CEO

"Melvin R. Reeves"
Melvin R. Reeves
Executive Vice President & General Counsel

August 25, 2000



PHOTOCHANNEL NETWORKS INC.

3rd Quarter Report

June 30, 2000