**Avicanna Inc.**
**Condensed Consolidated Interim Financial Statements**
**(Unaudited)**
**For the Three and Six Months Ended June 30, 2021 and 2020**
(expressed in Canadian dollars, except share and per share amounts)

**Avicanna Inc.**
**Condensed Consolidated Interim Statements of Financial Position**
**Unaudited (Expressed in Canadian Dollars)**

| | Note | | June 30, 2021 | | December 31, 2020 |
|---|---|---|---|---|---|
| **ASSETS** | | | | | |
| **Current assets** | | | | | |
| Cash | | $ | 522,462 | $ | 1,266,732 |
| Short-term investments | 4 | | - | | 1,250,000 |
| Amounts receivable | 5 | | 1,515,417 | | 1,005,290 |
| Prepaid assets | | | 982,903 | | 1,321,586 |
| Biological assets | 6 | | 207,452 | | 650,780 |
| Inventory | 7 | | 2,123,720 | | 1,276,078 |
| **Total current assets** | | | **5,351,954** | | **6,770,466** |
| Right of use asset | 10 | | 245,323 | | 343,452 |
| Property and equipment | 8 | | 19,883,042 | | 21,465,199 |
| Intangible assets | 9, 23 | | 391,942 | | 497,468 |
| Deferred tax asset | | | 34,451 | | 34,451 |
| Derivative asset | 11 | | 526,312 | | 526,312 |
| Investment | 20 | | 518,213 | | 518,213 |
| **Total assets** | | **$** | **26,951,237** | **$** | **30,155,561** |
| **LIABILITIES AND SHAREHOLDERS' EQUITY** | | | | | |
| **Current liabilities** | | | | | |
| Trade payables and accrued liabilities | | $ | 6,131,177 | $ | 6,562,339 |
| Lease liability – current portion | 13 | | 203,155 | | 203,155 |
| Income tax payable | | | 20,684 | | 20,684 |
| Convertible debentures | 14 | | 262,781 | | 1,573,695 |
| Derivative liability | 15 | | 61,715 | | 145,151 |
| Due to related party | 16 | | 4,111,725 | | 4,319,545 |
| **Total current liabilities** | | | **10,791,237** | | **12,824,569** |
| Lease liability | 13 | | 56,882 | | 161,061 |
| Deferred revenue | 12 | | 3,058,601 | | 3,260,101 |
| **Total liabilities** | | | **13,906,720** | | **16,245,731** |
| **Shareholders' Equity** | | | | | |
| Share capital | 17 | | 62,851,227 | | 57,468,839 |
| Warrants | 17 | | 8,490,837 | | 6,780,037 |
| Share-based payment reserve | 18 | | 6,102,386 | | 5,916,475 |
| Accumulated other comprehensive loss | | | (3,593,682) | | (2,112,995) |
| Deficit | | | (67,729,314) | | (62,036,238) |
| **Equity attributable to owners of the parent** | | | **6,121,454** | | **6,016,118** |
| Non-controlling interest | 19 | | 6,923,063 | | 7,893,712 |
| **Total equity** | | | **13,044,517** | | **13,909,830** |
| | | **$** | **26,951,237** | **$** | **30,155,561** |

Nature of operations and going concern uncertainty – Note 1
Subsequent events – Note 24

Approved by the Board
/s/ John McVicar, Audit Committee Chair, Director

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

**Avicanna Inc.**
**Condensed Consolidated Interim Statements of Operations and Comprehensive Loss**
**For the Three and Six Months Ended June 30, 2021 and 2020**
**Unaudited**
**(Expressed in Canadian Dollars)**

| | | Three months ended June 30, | | Six months ended June 30, | |
|---|---|---|---|---|---|
| | **Note** | **2021** | **2020** | **2021** | **2020** |
| **Revenue** | | | | | |
| Service Revenue | | $ 576 | $ 92,106 | $ 5,573 | $ 255,658 |
| License Revenue | 11 | 100,750 | - | 201,500 | - |
| Product Sales | | 690,895 | 617,362 | 856,055 | 714,713 |
| **Total Revenue** | | **792,221** | **709,468** | **1,063,128** | **970,371** |
| Cost of goods sold | | (397,045) | (133,481) | (487,587) | (234,288) |
| **Gross margin before the undernoted** | | **395,176** | **575,987** | **575,541** | **736,083** |
| Fair value changes in biological assets included in inventory sold | | (26,338) | (540,884) | (34,646) | (569,552) |
| Unrealized gain on changes in fair value of biological assets | | (135,847) | (88,849) | 95,819 | 1,827,271 |
| **Gross margin** | | 232,991 | **(53,746)** | 636,714 | **1,993,802** |
| **Expenses** | | | | | |
| General and administrative | 22 | 2,519,136 | 2,924,462 | 5,359,692 | 6,110,405 |
| Share-based compensation | 18 | 229,230 | 1,277,770 | 401,011 | 1,615,962 |
| Depreciation and amortization | 8,9,10 | 189,871 | 330,685 | 454,910 | 839,828 |
| Expected credit loss | 5 | - | - | 41,639 | - |
| Loss (Gain) on revaluation of derivative liability | 15 | - | - | 140,568 | - |
| Impairment of goodwill | | - | 686,845 | - | 686,845 |
| **Total Expenses** | | (2,938,237) | (5,219,762) | (6,397,820) | (9,253,040) |
| **Other income (expenses)** | | | | | |
| Foreign exchange loss | | (14,649) | (65,292) | (25,123) | (74,301) |
| Gain on disposal of capital assets | 8 | (1,762) | - | 51,975 | - |
| Other income (expense) | | (16,584) | (2,213,454) | 26,060 | (2,328,251) |
| Interest expense | | (31,270) | (93,928) | (164,079) | (93,928) |
| **Net loss** | | $ (2,769,511) | $ (7,646,182) | $ (5,872,273) | $ (9,755,718) |
| Exchange differences on translation of foreign operations | | (428,106) | (1,322,983) | (2,341,932) | (1,870,105) |
| **Net comprehensive loss** | | **$ (3,197,617)** | **$ (8,969,165)** | **$ (8,214,205)** | **$ (11,625,823)** |
| Net comprehensive loss attributable to non – controlling interest | 19 | (365,101) | (1,237,666) | (970,649) | (1,297,505) |
| Net comprehensive loss attributable to Shareholders of the Company | 19 | (2,832,516) | (7,731,499) | (7,243,556) | (10,328,318) |
| | | $ (3,197,617) | $ (8,969,165) | $ (8,214,205) | $ (11,625,823) |
| **Weighted average number of common shares – basic and diluted** | | 41,271,574 | 24,889,167 | 37,596,974 | 24,345,387 |
| **Net loss per share – basic and diluted** | | $ (0.08) | $ (0.36) | $ (0.22) | $ (0.48) |

The accompanying notes are an integral part of these condensed consolidated interim financial statement

**Avicanna Inc.**
**Condensed Consolidated Interim Statements of Changes in Shareholders' Equity**
**For the Six Months Ended June 30, 2021 and June 30, 2020**
**(Expressed in Canadian Dollars)**

| | | Common Shares | | Common Share to be Issued | | Warrants | Share Based Reserve | Deficit | Accumulated Other Comprehensive Loss | Non-controlling Interest | Total |
|---|---|---|---|---|---|---|---|---|---|---|---|
| | Note | # | $ | # | $ | $ | $ | $ | $ | $ | $ |
| **Balance at December 31, 2020** | | **35,871,941** | **57,355,314** | **101,722** | **113,526** | **6,780,037** | **5,916,475** | **(62,036,238)** | **(2,112,995)** | **7,893,712** | **13,909,830** |
| Settlement of shares to be issued | 17[i] | 101,722 | 113,526 | (101,722) | (113,526) | - | - | - | - | - | - |
| Share based compensation | 18 | - | - | - | - | - | 401,011 | - | - | - | 401,011 |
| Exercise of RSUs | 18 | 104,781 | 136,130 | 10,797 | 9,177 | - | (145,308) | - | - | - | - |
| Conversion of debentures | 14 | 613,535 | 1,513,175 | - | - | - | - | - | - | - | 1,513,175 |
| Exercise of warrants | 17[ii] | 99,595 | 124,883 | - | - | (40,227) | - | - | - | - | 84,656 |
| Issuance of units | 17[iii] | 4,480,000 | 3,599,023 | - | - | 1,751,027 | - | - | - | - | 5,350,050 |
| Forfeiture of RSUs and options | 18 | - | - | - | - | - | (69,793) | 69,793 | - | - | - |
| Foreign exchange translation | | - | - | - | - | - | - | - | (1,480,687) | (861,245) | (2,341,932) |
| Net loss | | - | - | - | - | - | - | (5,762,869) | - | (109,404) | (5,872,273) |
| **Balance at June 30, 2021** | | **41,271,574** | **62,842,050** | **10,797** | **9,177** | **8,490,837** | **6,102,385** | **(67,729,314)** | **(3,593,682)** | **6,923,063** | **13,044,517** |

| | | | | | | | | | | | |
|---|---|---|---|---|---|---|---|---|---|---|---|
| **Balance at December 31, 2019** | | **22,364,723** | **46,033,465** | **-** | **-** | **4,267,996** | **4,010,824** | **(30,800,436)** | **(1,124,524)** | **7,488,456** | **29,875,781** |
| Warrants expired | | - | 6,531 | - | - | (6,531) | - | - | - | - | - |
| Issuance of shares | | 4,022,721 | 4,616,801 | - | - | - | - | - | - | - | 4,616,801 |
| Warrant allocation | | - | (657,611) | - | - | 657,611 | - | - | - | - | - |
| Share based compensation | | - | - | - | - | - | 1,615,962 | - | - | - | 1,615,962 |
| SMGH Recapitalization | | - | - | - | - | - | - | - | - | 2,859,440 | 2,859,440 |
| Foreign exchange translation | | - | - | - | - | - | - | - | (726,612) | (1,143,493) | (1,870,105) |
| Net loss | | - | - | - | - | - | - | (9,601,706) | | (154,012) | (9,755,718) |
| **Balance at June 30, 2020** | | **26,387,444** | **49,999,186** | **-** | **-** | **4,919,076** | **5,626,786** | **(40,402,142)** | **(1,851,136)** | **9,050,391** | **27,342,161** |

The accompanying notes are an integral part of these condensed consolidated interim financial statement.

# Avicanna Inc.
## Condensed Consolidated Interim Statements of Cash Flows
## For the Six months Ended June 30, 2021 and June 30, 2020
## Unaudited
## (Expressed in Canadian Dollars)

| | Note | | For the Six Months Ended June 30, 2021 | | For the Six Months Ended June 30, 2020 |
|---|---|---|---|---|---|
| **Cash flows from operating activities:** | | | | | |
| Net loss | | $ | (8,214,205) | $ | (11,625,823) |
| Depreciation and amortization | 8,9,10 | | 454,910 | | 839,827 |
| Interest on lease liability | 13 | | 12,801 | | 20,627 |
| Accretion of convertible debentures | 5 | | 108,621 | | 27,184 |
| Share-based compensation | 18 | | 401,011 | | 1,615,962 |
| Expected credit losses | | | 41,639 | | - |
| Impairment of goodwill | | | - | | 686,845 |
| Loss on derivative asset | | | - | | 2,279,426 |
| Loss (gain) on fair value of derivative liability | 15 | | 140,568 | | (22,609) |
| Recognition of deferred revenue | | | (201,500) | | (94,926) |
| Changes in non-cash operating elements of working capital | 23 | | (870,313) | | (1,650,215) |
| **Cash used in operating activities** | | | **(8,126,468)** | | **(7,923,702)** |
| **Cash flows from investing activities:** | | | | | |
| Purchase of capital assets | 8 | | (833,705) | | (1,124,218) |
| Proceeds from disposal of capital assets | 8 | | 237,831 | | - |
| Sale of short-term investments | 4 | | 1,250,000 | | - |
| **Cash used in investing activities** | | | **654,126** | | **(1,124,218)** |
| **Cash flows from financing activities:** | | | | | |
| Payment of lease liability | 13 | | (116,980) | | (111,275) |
| Increase in balance due to related parties | 16 | | 191,388 | | 1,790,186 |
| Repayment of debentures | 14 | | (308,610) | | - |
| Exercise of warrants | 17 | | 84,656 | | 4,616,801 |
| Proceeds from issuance of common shares | 17 | | 5,350,050 | | - |
| **Cash provided by financing activities** | | | **5,200,504** | | **6,295,712** |
| **Net decrease in cash** | | | **(2,271,838)** | | **(2,752,208)** |
| **Effect of foreign exchange differences** | | | **1,527,568** | | **2,392,148** |
| **Cash, beginning of year** | | | **1,266,732** | | **441,757** |
| **Cash, end of year** | | **$** | **522,462** | **$** | **81,697** |

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

**NOTICE OF NO AUDITOR REVIEW OF CONDENSED CONSOLIDATED INTERIM FINANCIAL STATEMENTS**

Under National Instrument 51-102, Part 4, subsection 4.3(3) (a), if an auditor has not performed a review of the condensed consolidated interim financial statements, they must be accompanied by a notice indicating that the interim financial statements have not been reviewed by an auditor.

The accompanying unaudited condensed consolidated interim financial statements of the Company have been prepared by and are the responsibility of the Company's management.

The Company's independent auditor has not performed a review of these condensed consolidated interim financial statements in accordance with standards established by the Chartered Professional Accountants Canada for a review of interim financial statements by an entity's auditor.

## 1. NATURE OF OPERATIONS AND GOING CONCERN UNCERTAINTY

Avicanna Inc. ("Avicanna" or the "Company") was incorporated in Ontario, Canada. Avicanna is a Canadian vertically integrated biopharmaceutical company developing and driving biopharmaceutical advancements of plant-derived cannabinoid-based products with operations in both North and South America. To date, the Company has commercialized several product lines in both North and South America.

The registered office of the Company is located at 480 University Avenue, Suite 1502, Toronto, Ontario. The Company's common shares are listed under the symbol "AVCN" on the Toronto Stock Exchange ("TSX"); the OTC US exchange under the symbol "AVCNF"; and the Frankfurt Stock Exchange under the symbol "0NN".

These condensed consolidated interim financial statements have been prepared on a going concern basis which contemplates that the Company will continue operations for the foreseeable future and will be able to realize its assets and discharge its liabilities in the normal course of business. These condensed consolidated interim financial statements do not give effect to adjustments that would be necessary to the carrying values and classification of assets and liabilities should the Company be unable to continue as a going concern.

As at June 30, 2021, the Company has an accumulated deficit of $67,729,314 (December 31, 2020 - $62,036,238), cash of $522,462 (December 31, 2020 – $1,266,732), and a working capital deficit of $5,439,283 (December 31, 2020 – deficit of $6,054,103). Additionally, the Company incurred a net loss after taxes of $5,872,273 and used $8,126,468 of cash from operating activities during the six months ended on June 30, 2021. When compared to the same period in prior year, the Company incurred a net loss of $9,755,718 and used $7,923,702 of cash from operating activities. The Company will need to raise additional financing to continue operations, product development and clinical research. Although the Company has been successful in the past in obtaining financing and it believes that it will continue to be successful, there is no assurance that it will be able to obtain adequate financing in the future or that such financing will be available on terms that are advantageous to the Company. These material uncertainties may cast significant doubt as to the Company's ability to continue as a going concern.

## 2. BASIS OF PRESENTATION

**Statement of compliance**

These condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standard 34 – *Interim Financial Reporting* ("IAS 34") using accounting policies consistent with International Financial Reporting Standards ("IFRS") as issued by the International Accounting Standards Board ("IASB"). Accordingly, certain disclosures normally included in annual financial statements prepared in accordance with IFRS have been omitted or condensed. These condensed consolidated interim financial statements should be read in conjunction with the Company's audited consolidated financial statements for the year ended December 31, 2020.

These condensed consolidated interim financial statements were approved and authorized for issuance by the Company's Board of Directors on September 9, 2021.

**Basis of presentation**

These condensed consolidated interim financial statements have been prepared on a historical cost basis except for biological assets and derivative financial instruments, which are measured at fair value through profit and loss, as explained in the accounting policies below. These condensed consolidated interim financial statements are presented in Canadian dollars, which is the Company's functional currency. The Company currently views the business as one operating segment but expects this to change in future periods.

**Functional and presentation currency**

These condensed consolidated interim financial statements are presented in Canadian dollars, which is the functional currency of the Company. The functional currency of each subsidiary is presented in the table below.

## 2. BASIS OF PRESENTATION (CONTINUED)

**Basis of consolidation**
Subsidiaries are entities controlled by the Company. Control exists when the Company has power, directly or indirectly, over an entity and be is exposed, or has rights, to variable returns from its involvement with the entity and has the ability to affect those returns through the power it has. 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 following is a list of the Company's operating subsidiaries.

| Subsidiaries | Jurisdiction of Incorporation | Ownership Interest | Functional currency |
|---|---|---|---|
| Avicanna UK | England | 100% | British Pound Sterling |
| Avicanna USA | United States of America | 100% | United States Dollar |
| 2516167 Ontario Inc. ("My Cannabis") | Ontario, Canada | 100% | Canadian Dollar |
| Sigma Magdalena Canada Inc. | Ontario, Canada | 60% | Canadian Dollar |
| Sigma Analytical Magdalena S.A.S. ("Sigma Colombia") | Republic of Colombia | 60% | Colombian Peso |
| Santa Marta Golden Hemp S.A.S. ("SMGH") | Republic of Colombia | 60% | Colombian Peso |
| Avicanna LATAM S.A.S. | Republic of Colombia | 100% | Colombian Peso |
| Sativa Nativa S.A.S. ("SN") | Republic of Colombia | 63% | Colombian Peso |

Intragroup balances, and any unrealized gains and losses or income and expenses arising from transactions with jointly controlled entities are eliminated to the extent of the Company's interest in the entity.

Subsequent to acquisition, the carrying amount of non-controlling interests is the amount recognized initially, plus the non-controlling interests' share of changes in the capital of the company in addition to changes in ownership interests. Total comprehensive income or loss is attributed to non-controlling interests, even if this results in the non-controlling interests having a deficit balance.

**Foreign currency transactions**
Foreign currency transactions are translated into Canadian dollars at exchange rates in effect on the date of the transactions. At the end of each reporting period, monetary assets and liabilities denominated in foreign currencies are translated into Canadian dollars at the foreign exchange rate applicable at that period-end date. Non-monetary assets and liabilities that are measured in terms of historical cost in a foreign currency are translated using the exchange rate at the date of the transaction. Foreign currency differences are generally recognized in profit or loss and presented within Gain (loss) on foreign exchange.

**Foreign currency translation**
The assets and liabilities of foreign operations, including goodwill and fair value adjustments arising on acquisition, are translated into Canadian dollars at the exchange rates at the reporting date. The income and expenses of foreign operation are translated into Canadian dollars at the dates of the transactions. Foreign currency differences due to translation are recognized in OCI and accumulated in the translation reserve, except to the extent that the translation difference is allocated to NCI.

**Use of judgments, estimates and assumptions**
The preparation of the condensed consolidated interim financial statements in conformity with IFRS requires management to make judgments, estimates 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.

Estimates are based on management's best knowledge of current events and actions that the Company may undertake in the future. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which the estimate is revised if the revision affects only that period, or in the period of the revision and future periods if the revision affects both current and future periods.

The following are the critical judgments, apart from those involving estimations, that management have made in the process of applying the Company's accounting policies and that have the most significant effect on the amounts recognized in the condensed consolidated interim financial statements:

## 2. BASIS OF PRESENTATION (CONTINUED)

*Business combinations*
Determining whether an acquisition meets the definition of a business combination or represents an asset purchase requires judgment on a case-by-case basis. As outlined in IFRS 3, the components of a business must include inputs, processes and outputs.

In a business combination, substantially all identifiable assets, liabilities and contingent liabilities acquired are recorded at the date of acquisition at their respective fair values. One of the most significant areas of judgment and estimation relates to the determination of the fair value of these assets and liabilities, including the fair value of contingent consideration, if applicable. If any intangible assets are identified, depending on the type of intangible asset and the complexity of determining its fair value, the Company may utilize an independent external valuation expert to develop the fair value, using appropriate valuation techniques, which are generally based on a forecast of the total expected future net cash flows. These valuations are linked closely to the assumptions made by management regarding the future performance of the assets concerned and any changes in the discount rate applied.

*Biological assets and inventory*
In calculating the fair value of the biological assets and inventory, management is required to make a number of estimates, including estimating the stage of growth of the cannabis up to the point of harvest, harvesting costs, selling costs, average or expected selling prices and list prices, expected yields for the cannabis plants, and oil conversion factors. Inventories of harvested cannabis are valued at the lower of cost or net realizable value. The Company estimates the net realizable value of inventories, considering the most reliable evidence available at the reporting date. The future realization of these inventories may be affected by market-driven changes that may reduce future selling prices. A change to these assumptions could impact the Company's inventory valuation and gross profit.

*Estimated useful life of long-lived assets*
Judgment is used to estimate each component of a long-lived asset's useful life and is based on an analysis of all pertinent factors including, but not limited to, the expected use of the asset and in the case of an intangible asset, contractual provisions that enable renewal or extension of the asset's legal or contractual life without substantial cost, and renewal history. If the estimated useful lives were incorrect, it could result in an increase or decrease in the annual amortization expense, and future impairment charges or recoveries.

*Impairment of long-lived assets*
When there are indications that an asset may be impaired, the Company is required to estimate the asset's recoverable amount. The recoverable amount is the greater of value in use and fair value less costs to sell. Fair value is determined as the amount that would be obtained from the sale of the asset in an arm's length transaction between knowledgeable and willing parties. Determining the value in use requires the Company to estimate expected future cash flows associated with the assets and a suitable discount rate to calculate present value.

In addition to assessing evidence of possible impairment, the Company also determines whether there is any indication that a previously recognized impairment loss for an asset other than goodwill no longer exists or may have decreased. The Company determines whether there has been a change in the estimate used to determine the asset's recoverable amount since the last impairment loss is recognized.

*Long-term investment*
The fair value of the Company's long-term investments are subject to limitation as the financial information for private companies in which the Company holds investments may not be readily available. Adjustment to the fair value of a long-term investment is based on management's judgement and may be a result of subsequent equity financing provided by third-party investors resulting in a valuation different than the current value of the investee company, significant events and restructuring of the investment company that may result in a material impact on the company's fair value, and financial information received from the investor company.

*Fair value measurements*
Fair value is the price that would be received to sell an asset or paid to transfer a liability in an orderly transaction between market participants at the measurement date, regardless of whether that price is directly observable or estimated using another valuation technique. In estimating the fair value of an asset or a liability, the Company takes into account the characteristics of the asset or liability if market participants would take those characteristics into account when pricing the asset or liability at the measurement date.

## 2. BASIS OF PRESENTATION (CONTINUED)

*Functional currency*
The functional currency for each of the Company's subsidiaries is the currency of the primary economic environment in which the respective entity operates. Such determination involves certain judgements to identify the primary economic environment. The Company reconsiders the functional currency of its subsidiaries if there is a change in events and/or conditions which determine the primary economic environment.

*Provisions*
Provisions are accrued for liabilities with uncertain timing or amounts, if, in the opinion of management, it is both likely that a future event will confirm that a liability had been incurred at the date of the condensed consolidated interim financial statements and the amount can be reasonably estimated. In cases where it is not possible to determine whether such a liability has occurred, or to reasonably estimate the amount of loss until the performance of some future event, no accrual is made until that time. In the ordinary course of business, the Company may be party to legal proceedings which include claims for monetary damages asserted against the Company. The adequacy of provisions is regularly assessed as new information becomes available.

*Leases*
The Company exercises judgment when contracts are entered into that may give rise to a right-of-use asset that would be accounted for as a lease. Judgment is required in determining the appropriate lease term on a lease-by-lease basis. The Company considers all facts and circumstances that create an economic incentive to exercise a renewal option or to not exercise a termination option at inception and over the term of the lease, including investments in major leaseholds, operating performance, and changed circumstances. The periods covered by renewal or termination options are only included in the lease term if the Company is reasonably certain to exercise that option.

*Income tax provisions*
Provisions for taxes are made using the best estimate of the amount expected to be paid based on a qualitative assessment of all relevant factors. Judgment is required in determining whether deferred income tax assets and liabilities are recognized on the condensed consolidated interim statement of financial position. Deferred income tax assets, including those arising from unutilized tax losses, require management to assess the likelihood that the Company will generate future taxable income in order to utilize the deferred income tax assets. Estimates of future taxable income are based on forecasted cash flows from operations or other activities. To the extent that future cash flows and taxable income differ significantly from estimates, the ability of the Company to realize the net deferred income tax assets recorded on the reporting date could be impacted.

The Company reviews the adequacy of these provisions at the end of the reporting period. However, it is possible that at some future date an additional liability could result from audits by taxing authorities. Where the final outcome of these tax-related matters is different from the amounts that were initially recorded, such differences will affect the tax provisions in the period in which such determination is made.

*Determination of share-based payments*
The estimation of share-based payments (including warrants and stock options) requires the selection of an appropriate valuation model and consideration as to the inputs necessary for the valuation model chosen. The model used by the Company is the Black-Scholes valuation model at the date of the grant. The Company makes estimates as to the volatility, the expected life, dividend yield and the time of exercise, as applicable. The expected volatility is based on the average volatility of share prices of similar companies over the period of the expected life of the applicable warrants and stock options. The expected life is based on historical data. These estimates may not necessarily be indicative of future actual patterns.

## 3. SIGNIFICANT ACCOUNTING POLICIES

These interim condensed consolidation financial statements have been prepared in accordance with the accounting policies adopted in the Company's most recent annual consolidated financial statements for the year ended December 31, 2020.

## 4. SHORT-TERM INVESTMENTS

As at December 31, 2020, the Company held short-term investments which was comprised of guaranteed investment certificates for $1,250,000 maturing in one year, bearing an annual interest of 0.25%. During the six months ended June 30, 2021, the short-term investment matured.

(expressed in Canadian dollars, except share and per share amounts)

## 5. AMOUNTS RECEIVABLE

| | | June 30, 2021 | | December 31, 2020 |
|---|---|---|---|---|
| Trade and other receivables | $ | 1,017,167 | $ | 708,673 |
| Sales tax receivable | | 1,253,471 | | 1,010,199 |
| Expected credit loss provision | | (755,221) | | (713,582) |
| **Total amounts receivable** | **$** | **1,515,417** | **$** | **1,005,290** |

## 6. BIOLOGICAL ASSETS

Biological assets consist of cannabis on plants. The changes in the carrying value of biological assets are as follows:

| | | June 30, 2021 | | December 31, 2020 |
|---|---|---|---|---|
| Balance at the beginning of the year | $ | $591,530 | $ | 108,995 |
| Production costs capitalized | | $226,401 | | 848,931 |
| Gain in fair value less costs to sell due to biological transformation | | $94,157 | | 1,340,996 |
| Transferred to inventory upon harvest | | ($704,636) | | (1,648,142) |
| **Balance at end of the period** | **$** | **$207,452** | **$** | **650,780** |

The Company measures its biological assets at their fair value less costs to sell. This is determined using a model which estimates the expected harvest yield in grams for plants and seeds currently being cultivated, and then adjusts that amount for the expected selling price less costs to sell per gram. During the period, the Company also cultivated seeds which have been transferred into inventory.

The fair value measurements for biological assets have been categorized as Level 3 fair values based on the inputs to the valuation technique used. The Company's method of accounting for biological assets attributes value accretion on a straight-line basis throughout the life of the biological asset from initial cloning to the point of harvest.

The following table quantifies each significant unobservable input and provides the impact that a 10% increase/decrease in each input would have on the fair value of biological assets.

| | | As of June 30, 2021 | | As of December 31, 2020 | |
|---|---|---|---|---|---|
| | **Assumptions: THC Resin** | **Input** | **Effect on Fair Value** | **Input** | **Effect on Fair Value** |
| [i] | THC Resin Yield | 11.9% | $13,000 | 12.0% | $65,324 |
| [ii] | THC Resin Price (USD/KG) | $4,400 | $13,263 | $4,400 | $65,306 |
| [iii] | Weighted average of expected loss of plants until harvest | 5.0% | $589 | 28.9% | $173 |
| [iv] | Expected yields for cannabis plants (average grams per plant) | 100 | $11,191 | 134 | $53,173 |
| [v] | Weighted average number of growing weeks completed as a percentage of total growing weeks as at period end | 28% | $11,191 | 88% | $53,173 |
| [vi] | Estimated fair value less costs to complete and sell (per gram) | $0.58 | $12,494 | $0.63 | $63,271 |
| [vii] | After harvest cost to complete and sell (per gram) | $0.06 | $1,304 | $0.10 | $10,097 |

(expressed in Canadian dollars, except share and per share amounts)

## 6. BIOLOGICAL ASSETS (CONTINUED)

| | Assumptions: CBD Isolate | As of June 30, 2021 | | As of December 31, 2020 | |
|---|---|---|---|---|---|
| | | Input | Effect on Fair Value | Input | Effect on Fair Value |
| [i] | CBD Isolate Yield | 4% | $2,110 | 6% | $2,465 |
| [ii] | CBD Isolate Price (USD/KG) | $1,100 | $2,293 | $1,100 | $2,462 |
| [iii] | Weighted average of expected loss of plants until harvest | 2.0% | $14 | 3% | $58 |
| [iv] | Expected yields for cannabis plants (average grams per plant) | 100 | $676 | 112 | $1,893 |
| [v] | Weighted average number of growing weeks completed as a percentage of total growing weeks as at period end | 96% | $676 | 56% | $1,893 |
| [vi] | Estimated fair value less costs to complete and sell (per gram) | $0.00 | $196 | $0.04 | $1,165 |
| [vii] | After harvest cost to complete and sell (per gram) | $0.02 | $873 | $0.10 | $3,057 |

| | Assumptions: CBD Seeds | As of June 30, 2021 | | As of December 31, 2020 | |
|---|---|---|---|---|---|
| | | Input | Effect on Fair Value | Input | Effect on Fair Value |
| [i] | CBD Seeds Price (USD/UN) | $0.50 | $10,615 | $0.50 | $2,506 |
| [ii] | Weighted average of expected loss of plants until harvest | 25.9% | $3,709 | 11.1% | $311 |
| [iii] | Expected yields for cannabis plants (average units per plant) | 3,000 | $10,597 | 2,500 | $2,491 |
| [iv] | Weighted average number of growing weeks completed as a percentage of total growing weeks as at period end | 76% | $10,597 | 26% | $2,491 |
| [v] | Estimated fair value less costs to complete and sell (per gram) | $0.58 | $10,609 | $0.62 | $2,504 |
| [vi] | After harvest cost to complete and sell (per gram) | $0.00 | $12 | $0.00 | $13 |

Weighted average of expected loss of plants until harvest represents loss via plants that do not survive to the point of harvest. It does not include any financial loss on a surviving plant.

The estimated fair value less costs to complete and sell (per gram) represents the expected sales price for the Company's active ingredients including isolate and resins less the remaining costs to complete and sell that product as finished product which is inclusive of all production activities.

These estimates are subject to volatility in market prices and several uncontrollable factors, which could significantly affect the fair value of biological assets in future periods.

The Company estimates the harvest yields for cannabis at various stages of growth. As of June 30, 2021, it is expected that the Company's cannabis plants biological assets will yield approximately 1,265,312 grams of dry cannabis and 1,290,000 seeds in Santa Marta Golden Hemp. As of June 30th, 2021, Sativa Nativa is only growing R&D batches to enhance its genetic base.

The company has decided not to value at fair value certain seeds batches given the novelty of the market it will trade once harvested.

The Company's estimates are, by their nature, subject to change and differences from the anticipated yield will be reflected in the gain or loss on biological assets in future periods.

(expressed in Canadian dollars, except share and per share amounts)

## 7. INVENTORY

| | | Capitalized Cost | Biological assets fair value adjustment | Impairment | Carrying Value |
|---|---|---|---|---|---|
| **Harvested Cannabis** | | | | | |
| Seeds | $ | 390,613 | - | (400,179) | (9,566) |
| Wet Flower | | 85,785 | 65,844 | (4,416) | 147,213 |
| Dried Flower | | 141,363 | 333,465 | (183,388) | 291,440 |
| | | **617,761** | **399,309** | **(587,983)** | **429,087** |
| **Active Pharmaceutical Ingredients** | | | | | |
| Work in process | | 475,336 | 299,228 | (397,634) | 376,930 |
| Finished goods | | 101,736 | (53,265) | (47,611) | 860 |
| | | **577,072** | **245,963** | **(445,245)** | **377,790** |
| Supplies and consumables | | **1,657,964** | **-** | **(640,886)** | **1,017.068** |
| Finished goods | | **391,681** | **-** | **(91,916)** | **299,765** |
| **At June 30, 2021** | **$** | **3,244,478** | **645,272** | **(1,766,030)** | **2,123,720** |

| | | Capitalized Cost | Biological assets fair value adjustment | Impairment | Carrying Value |
|---|---|---|---|---|---|
| **Harvested Cannabis** | | | | | |
| Seeds | $ | 440,950 | (3,266) | (437,598) | 86 |
| Wet Flower | | 72,550 | 103,751 | (12,651) | 163,650 |
| Dried Flower | | 153,998 | 188,943 | (276,501) | 66,440 |
| | | **667,498** | **289,428** | **(726,750)** | **230,176** |
| **Active Pharmaceutical Ingredients** | | | | | |
| Work in process | | 891,575 | (92,736) | (793,801) | 5,038 |
| Finished goods | | 870,755 | 50,347 | (179,810) | 741,291 |
| | | **1,762,330** | **(42,389)** | **(973,611)** | **746,330** |
| Supplies and consumables | | **816,559** | **-** | **(596,560)** | **219,999** |
| Finished goods | | **180,466** | **-** | **(101,004)** | **79,462** |
| **At December 31, 2020** | **$** | **3,426,853** | **247,039** | **(2,397,925)** | **1,275,967** |

As of June 30, 2021 the Company had accumulated impairment of $1,766,030 (June 30, 2020 - $nil) due to the costs capitalized exceeding the net realizable value of the inventory. The impairment recovery has been included in the cost of goods sold in the condensed consolidated interim statement of operations and comprehensive loss.

The Company recorded unrealized gain on biological assets of $645,272 (June 30, 2020 – $1,827,271) during the period ended June 30, 2021 and $487,587 in cost of sales (June 30, 2020 - $234,288).

(expressed in Canadian dollars, except share and per share amounts)

## 8. PROPERTY AND EQUIPMENT

| | | Equipment | Land | Construction in Progress | Infrastructure and Buildings | Total |
|---|---|---|---|---|---|---|
| **Cost** | | | | | | |
| Balance at, December 31, 2020 | $ | 3,016,452 | 9,088,419 | 4,973,217 | 5,604,076 | 22,682,164 |
| Additions | | 14,394 | - | 819,311 | - | 833,705 |
| Disposals | | (497,038) | - | - | - | (497,038) |
| Foreign exchange translation | | (185,774) | (921,522) | (587,335) | (558,263) | (2,252,894) |
| **At June 30, 2021** | $ | 2,348,034 | 8,166,897 | 5,205,193 | 5,045,813 | 20,765,937 |
| **Accumulated Depreciation** | | | | | | |
| Balance at, December 31, 2020 | $ | 992,635 | - | - | 224,330 | 1,216,965 |
| Depreciation | | 134,520 | - | - | 104,821 | 239,341 |
| Disposals | | (259,207) | - | - | - | (259,207) |
| Foreign exchange translation | | (294,426) | - | - | (19,778) | (314,204) |
| **At June 30, 2021** | | 573,522 | - | - | 309,373 | 882,895 |
| **Net Book Value** | | | | | | |
| December 31, 2020 | $ | 2,023,817 | 9,088,419 | 4,973,217 | 5,379,746 | 21,465,199 |
| June 30, 2021 | $ | 1,774,512 | 8,166,897 | 5,205,193 | 4,736,440 | 19,883,042 |

During the six months ended June 30, 2021, the Company recognized depreciation expense on its property and equipment of $239,341 (June 30, 2020 - $389,235) on the condensed consolidated interim statement of operations and comprehensive loss.

## 9. INTANGIBLE ASSETS

| | | Customer Relationships | Ecommerce Platform | Licenses and Permits | Software Licenses | Intellectual Property | Total |
|---|---|---|---|---|---|---|---|
| **Cost** | | | | | | | |
| At December 31, 2020 | $ | 141,327 | 455,994 | 50,177 | 83,321 | 100,551 | 831,370 |
| Additions | | - | - | - | - | - | - |
| Disposals | | - | - | - | - | - | - |
| Foreign exchange translation | | - | - | (1,008) | (1,674) | (2,022) | (4,704) |
| At June 30, 2021 | $ | 141,327 | 455,994 | 49,169 | 81,647 | 98,529 | 826,666 |
| **Accumulated Amortization** | | | | | | | |
| At December 31, 2020 | $ | 96,613 | 103,501 | 17,860 | 38,669 | 77,259 | 333,902 |
| Amortization | | 14,152 | 49,453 | 11,542 | 19,165 | 23,128 | 117,440 |
| Foreign exchange translation | | - | - | (3,563) | (5,916) | (7,139) | (16,618) |
| At June 30, 2021 | $ | 110,765 | 152,954 | 25,839 | 51,918 | 93,248 | 434,724 |
| **Net Book Value** | | | | | | | |
| December 31, 2020 | $ | 44,714 | 352,493 | 32,317 | 44,652 | 23,292 | 497,468 |
| June 30, 2021 | $ | 30,562 | 303,040 | 23,330 | 29,729 | 5,281 | 391,942 |

During the six months ended June 30, 2021, the Company recognized amortization on its intangible assets of $117,440 (June 30, 2020 - $352,464) on condensed consolidated interim statement of operations and comprehensive loss.

(expressed in Canadian dollars, except share and per share amounts)

## 10. RIGHT TO USE ASSETS

As of June 30, 2021, the Company's right to use asset consisted of the following:

| | June 30, 2021 | December 31, 2020 |
|---|---|---|
| **Cost** | $ | $ |
| Balance at beginning of period | 670,549 | 670,549 |
| Additions | - | - |
| Balance at end of period | 670,549 | 670,549 |
| | | |
| **Accumulated Amortization** | | |
| Balance at beginning of period | 327,097 | 130,839 |
| Depreciation | 98,129 | 196,258 |
| Balance at end of period | 425,226 | 327,097 |
| | | |
| **Net Book Value** | **245,323** | **343,452** |

Depreciation expense for the six months ended June 30, 2021 was $98,129 (June 30, 2020 - $98,129).

## 11. DERIVATIVE ASSET

| | | June 30, 2021 | | December 31, 2020 |
|---|---|---|---|---|
| Balance at the beginning of the year | $ | 526,312 | $ | 3,780,000 |
| Change in fair value | | - | | (3,253,688) |
| **Balance at end of period** | **$** | **526,312** | **$** | **526,312** |

On November 26, 2019, the Company entered into a license agreement (the "License Agreement") with LC2019, Inc. ("LC2019") pursuant to which the Company has agreed to license certain proprietary formulations and brand elements to LC2019 for commercialization in the United States. As consideration for entering into the License Agreement, LC2019 and its shareholders have entered into a definitive option agreement (the "Option Agreement") that grants Avicanna the option (the "Option") to acquire 100 percent of the issued and outstanding shares of LC2019, with such Option to be exercisable in the event that cannabis cultivation, processing, distribution and possession becomes federally legal in the United States (the "Triggering Event"). Avicanna may elect to waive the Triggering Event and exercise the Option at any time. As of June 30, 2021, the Company has not exercised the Option, and therefore does not have control of the entity.

Pursuant to the terms of the Option Agreement, upon the occurrence of the Triggering Event, Avicanna will exercise the Option and purchase all of the issued and outstanding shares of LC2019, as follows: (i) all of the issued and outstanding Class A shares at a nominal amount; (ii) all of the issued and outstanding Class B shares at the applicable subscription price; and (iii) all of the issued and outstanding Class C shares for up to 10% of the increase in the fair market value of LC2019 between the date of the Option Agreement and the date that Avicanna provides notice of exercise to LC2019, up to a maximum aggregate amount of CDN$10,000,000. Avicanna is entitled to elect to satisfy the purchase price in cash or through the issuance of common shares of Avicanna, in its sole discretion, subject to the approval of the Toronto Stock Exchange ("TSX") and in accordance with the policies of the Toronto Stock Exchange at such time. Additionally, Avicanna may elect to exercise the Option prior to the occurrence of the Triggering Event in its sole discretion or to assign the Option at any time.

The Option is exercisable for 10 years from the date of grant. The Option Agreement contains standard negative covenants, representations and warranties.

The Option was classified as a derivative financial instrument and was initially recorded at its fair value of $3,780,000 in the condensed consolidated interim statements of financial position. As of June 30, 2021, the Company determined the fair value of the Option to be $526,312

(expressed in Canadian dollars, except share and per share amounts)

## 12. DEFERRED REVENUE

| | | June 30, 2021 | | December 31, 2020 |
|---|---|---|---|---|
| Balance at the beginning of the year | $ | 3,260,101 | $ | 3,323,518 |
| Additions | | - | | 400,000 |
| Revenue recognized | | (201,500) | | (463,417) |
| **Balance at end of year** | **$** | **3,058,601** | **$** | **3,260,101** |

[i] Pursuant to the terms of the License Agreement with LC2019, the Company transfers brand/ trademark as well as intellectual property related to product development. For LC2019 to benefit from the brand, there are activities that the Company would need to perform in order to support and maintain the value of the brand/ trademark. As ongoing activities are required to maintain the brand, the license to the brand/ trademark would be considered a right to access and therefore would be recognized over time. In addition, given the license is for cannabis related to product development, the company meets the criteria for right of use of intellectual property and recognize at a point time. However, IFRS 15 states that revenue cannot be recognized for a license that provides a right to use intellectual property before the period during which the customer is able to use and benefit from the license. As cannabis remains federally illegal in the US, there exists restrictions in the benefits that the Company can derive from this license. Consequently, the revenue derived from the above license has been recognized as deferred revenue to be recognized into revenue evenly over a period of ten years. For the period ended June 30, 2021, the Company recognized $189,000 into License Revenue in relation to this contract (June 30, 2020- $189,000).

[ii] On August 11, 2020, the Company entered into an exclusive Distribution Agreement with a third-party, granting them the exclusive right to promote, market and sell the Company's products. The Company received $250,000 as consideration of the exclusivity partnership for a period of five years plus an automatic renewal period of five years (the "Exclusivity Fee"). The Company determined that its performance obligation with regards to the contract occurs over a period of time and therefore, revenue is to be recognized straight-line over a ten year period based on the term of the contract and the automatic term renewal. For the period ended June 30, 2021, the Company recognized $12,500 into License Revenue in relation to this contract (June 30, 2020 - $nil).

[iii] On January 7, 2020, the Company entered into a Development Project whereby the Company received $150,000 as consideration for formulation development. As of June 30, 2021, the Company had fulfilled 50% of its performance obligation with regards to the formulation development. The Company has not recognized any revenue from this contract during the period ended June 30, 2021. The Company recognized $75,000 was into license revenue during the year ended December 31, 2020 with the remainder included as deferred revenue.

## 13. LEASE LIABILITY

As of June 30, 2021, the lease liability consisted of the following:

| | | June 30, 2021 | | December 31, 2020 |
|---|---|---|---|---|
| **Balance at the beginning of the year** | **$** | **364,216** | **$** | **555,339** |
| Interest incurred on lease liability | | 12,801 | | 37,552 |
| Lease payments | | (116,980) | | (228,675) |
| **Balance at end of year** | **$** | **260,037** | **$** | **364,216** |
| Lease liability – current portion | | 203,155 | | 203,155 |
| Lease liability – noncurrent portion | | 56,882 | | 161,061 |

The Company has lease liabilities for leases related to its corporate offices. The weighted average discount rate for the six months ended June 30, 2021 was 8% percent.

(expressed in Canadian dollars, except share and per share amounts)

## 13. LEASE LIABILITY (CONTINUED)

The total future minimum rent payable under the Company's lease at June 30, 2021 was as follows:

| | | |
|---|---|---|
| Due in less than 1 year | $ | 224,950 |
| Due between 1 and 2 years | | 56,237 |
| Total lease payments | | 281,187 |
| Amounts representing interest over the term of the lease | | (21,150) |
| **Present value of minimum lease payments** | **$** | **260,037** |

## 14. CONVERTIBLE DEBENTURES

The following table is a break down of the convertible debenture balance on initial recognition and subsequent accretion:

| | | June 30, 2021 | | December 31, 2020 |
|---|---|---|---|---|
| Balance at the beginning of the period | $ | 1,573,695 | $ | 715,626 |
| Additions (ii) | | - | | 754,923 |
| Accretion expense | | 108,621 | | 103,146 |
| Conversion February 25, 2021 (ii) | | (150,268) | | - |
| Conversion March 1, 2021(i) | | (783,000) | | - |
| Conversion March 17, 2021 (ii) | | (239,372) | | - |
| Repayment April 5, 2021 (ii) | | (246,895) | | - |
| **Balance at end of period** | **$** | **262,781** | **$** | **1,573,695** |

(i) On March 1, 2019 ("Closing Date"), the Company completed a convertible debenture offering and raised gross proceeds of $783,000. The debentures incur interest at 8.0% per annum and have a maturity date of March 1, 2021. Each debenture is convertible, at the option of the holder, at any time before the maturity date, into fully paid and non-assessable Common Shares at the conversion price (the "Conversion Price"), representing a conversion rate of 125 Common Shares per $1,000 principal amount of debentures, subject to adjustment in accordance with the debenture certificates. On March 1, 2021 these debentures and accrued interest of $125,280 were converted into 113,535 Common Shares per the terms of the convertible debentures.

(ii) On November 2, 2020, the Company completed a convertible debenture offering and raised gross proceeds of $1,100,000. The debentures bear interest at 8.0% per annum and have a maturity date one year from the date of the issuance of the debentures on November 2, 2021. The first year of interest payable will be capitalized into and added to the principal amount under the Debenture on the date of issuance. Each debenture is convertible in whole or in part, any time while any principal amount or interest remains outstanding, into common shares of the Corporation at $1.00 per Share.

Additionally, each subscriber received one common share purchase warrant per $2.00 of Principal for a period of two years from the date of issuance of the warrants, subject to the Company's right to accelerate the expiry date of the Warrants in the event that the daily volume weighted average trading price is equal to or exceeds $2.00 on the TSX for a minimum of 10 consecutive trading days. Each whole warrant entitles the holder to acquire one common share of the Company at a price of $1.50 per Common Share. Between the issuance date and the date that is 60 days from the issuance date, if the Company issues common shares or securities convertible into common shares at a price or exercise price below $0.80 then the conversion price would be reduced to match that price or exercise price.

The debentures and warrants issued pursuant to the Offering are subject to a statutory hold period in Canada of four months and one day following the closing of the Offering.

Additionally, the Company incurred $199,926 in issuance costs in connection with this offering of convertible debentures. These costs were capitalized with debt and will be accreted over the term of the debentures.

A portion of proceeds is allocated to the Conversion Option and warrants based on the respective fair values of each instrument. The company used the Black-Scholes option pricing model to determine the fair value using the following assumptions: risk-free rate of 0.24-0.26%, volatility of 40% based on comparative companies, a discount for lack of marketability due to the four-month restriction period from the issuance date, and the maturity and exercise prices of the respective options.

(expressed in Canadian dollars, except share and per share amounts)

## 14. CONVERTIBLE DEBENTURES (CONTINUED)

As a result, the Company recognized the following:

| | | |
|---|---|---|
| Convertible debenture | $ | 754,923 |
| Issuance Costs | | 199,926 |
| Derivative liability (Note 15) | | 145,151 |
| | **$** | **1,100,000** |

During the period ended June 30, 2021, the Company recognized accretion expense of $108,621 (June 30, 2020 - $27,185) and interest expense of $43,638 (June 30, 2020 - $31,234) in relation to these convertible debentures.

On February 25, 2021, holders of the convertible debenture exercised $200,000 of principal into 200,000 Common Shares of the Company and on March 17, 2021, an additional $300,000 of principal into 300,000 common shares were issued on the exercise of convertible debentures. On April 5, 2021 the Company repaid $300,000 of the principal amount.

## 15. DERIVATIVE LIABILITIES

| | | June 30, 2021 | | December 31, 2020 |
|---|---|---|---|---|
| Balance at the beginning of the year | $ | 145,151 | $ | 23,434 |
| Additions | | - | | 145,151 |
| Repayment on convertible debenture | | (61,715) | | |
| Conversions | | (162,289) | | |
| Loss on change in fair value | | 140,568 | | (23,434) |
| **Balance at end of year** | **$** | **61,715** | **$** | **145,151** |

On March 1, 2019, the Company completed a convertible debenture offering. The Conversion Option related to the convertible debentures was determined to represent a derivative liability. A portion of the proceeds was allocated to this financial instrument based on its respective fair value. As of June 30, 2021, the conversion option had a fair value of $nil (December 31, 2020 - $nil). During the period ended June 30, 2021, the debentures were fully converted.

On November 2, 2020, the Company completed a convertible debenture offering (note 18). The Conversion Option and the warrants issued in relation to the convertible debentures was determined to represent a derivative liability. A portion of the proceeds was allocated to this financial instrument based on its respective fair value. At inception, the Company used the Black-Scholes option pricing model to determine the fair value using the following assumptions: risk-free rate of 0.26%, volatility of 40% based on comparative companies, a discount for lack of marketability due to the four-month restriction period from the issuance date, and the maturity and exercise prices of the respective options. As a result, the Company recognized, a derivative liability of $145,151, representing the conversion option of $111,297 and warrants of $33,854. At June 30, 2021, the Company determined that the fair value of the derivative liability was $61,715 and a loss of $140,568 was recognized (June 30, 2020 - $nil).

On February 25, 2021, a fair value of $72,714 was transferred to share capital on the conversion of debentures into 200,000 common shares. On March 17,2021, a fair value of $89,575 was transferred to share capital on the conversion of debentures into 300,000 common shares.

(expressed in Canadian dollars, except share and per share amounts)

## 16. RELATED PARTY TRANSACTIONS

The following outlines amounts that were paid to officers of the Company.

| | | June 30, 2021 | | December 31, 2020 |
|---|---|---|---|---|
| Salaries | $ | 380,000 | $ | 798,333 |
| Share-based compensation | | 147,832 | | 671,150 |
| | **$** | **527,832** | **$** | **1,469,483** |

Salaries and shared based compensation include compensation paid to key management personnel. The Company defines key management personnel as the Chief Executive Officer, President, Chief Financial Officer, and President of LATAM.

Additionally, as at June 30, 2021 the Company received advances from certain related parties who represent the minority shareholders of SMGH and Sativa Nativa in the amount of $4,111,725 (December 31, 2020- $4,319,545). The advances relate to minority partners contributions towards the expansion of cultivation facilities. The balance owed to the related party is interest free. As these amounts become due, the outstanding balances are converted into common shares of SMGH, consistent with current ownership splits. During the period ended June 30, 2021, $nil was converted into equity in SMGH (December 31, 2020 - $2,859,440).

Changes in the balances are disclosed in the following table:

| | | June 30, 2021 | | December 31, 2020 |
|---|---|---|---|---|
| Balance at the beginning of the year | $ | 4,319,545 | $ | 3,319,116 |
| Additions | | 191,388 | | 3,859,869 |
| Foreign exchange | | (399,208) | | - |
| Balance recapitalized into shares in SMGH | | - | | (2,859,440) |
| **Balance at end of year** | **$** | **4,111,725** | **$** | **4,319,545** |

## 17. SHARE CAPITAL

**Authorized and outstanding share capital:**

The authorized share capital of the Company consists of an unlimited number of common shares and unlimited number of preferred shares with no par value. As at June 30, 2021, the Company had 41,271,574 common shares issued and outstanding (December 31, 2020 – 35,875,941).

[i] As of December 31, 2020, there were 101,722 Restricted Stock Units ("RSUs") that were exercised but not yet settled. These shares were subsequently issued in January 2021.

[ii] On February 25, 2021, 99,595 common shares were issued on the exercise of common share purchase warrants. A total of 99,595 warrants were exercised at a price of $0.85 per common share for gross proceeds of $84,656. The common share purchase warrants exercised held a fair value of $40,227.

[iii] On March 4, 2021, the Company issued an aggregate of 4,480,000 Units (the "Units") at a price of $1.25 per Unit for net proceeds of $5,350,050, comprised of aggregate gross proceeds of $5,600,000 less share issuance costs of $249,950. Each Unit was comprised of one (1) common share in the capital of the Company each, a "Common Share") and one (1) common share purchase warrant (each whole warrant, a "Warrant"). Each Warrant is exercisable into one common share in the capital of the Company (each, a "Warrant Share") at a price of $1.75 until March 4, 2024.

(expressed in Canadian dollars, except share and per share amounts)

## 17. SHARE CAPITAL (CONTINUED)

The net proceeds of $5,350,050 were allocated between the common shares and the warrants by determining the fair value of the warrants, and allocating the residual to the common shares as follows:

| | | |
|---|---|---|
| Common shares | $ | 3,599,023 |
| Warrants | | 1,751,027 |
| | **$** | **5,350,050** |

The fair value of the common share purchase warrants was determined using the Black-Scholes option pricing model with a market price per common share of $1.17, a risk-free interest rate of 1.62%, an expected annualized volatility of 90% and expected dividend yield of 0%.

### Warrant Reserve

As at June 30, 2021, the following warrants were outstanding and exercisable:

| | **Warrants Issued / Exercised** | **Weighted average exercise price** |
|---|---|---|
| | # | $ |
| **Outstanding as at December 31, 2019** | **1,630,721** | **9.56** |
| Warrants issued | 6,529,335 | 1.28 |
| Warrants expired | (360,008) | 9.91 |
| **Outstanding as at December 31, 2020** | **7,800,048** | **2.62** |
| Warrants issued | 4,480,000 | 1.75 |
| Warrants exercised | (99,595) | 0.85 |
| Warrants expired | (1,245,713) | 1.00 |
| **Outstanding as at June 30, 2021** | **10,934,740** | **1.53** |

The following table is a summary of the Company's warrants outstanding as at June 30, 2021:

| **Warrants Outstanding** | | | **Warrants Exercisable** | |
|---|---|---|---|---|
| **Exercise price range** $ | **Number outstanding** # | **Weighted average remaining life** (years) | **Weighted average exercise price** $ | **Number exercisable** # |
| $ 0.85 | 240,235 | 2.45 | $ 0.02 | 240,235 |
| $ 1.00 | 25,000 | 0.83 | $ 0.00 | 25,000 |
| $ 1.20 | 4,492,325 | 2.09 | $ 0.44 | 4,492,325 |
| $ 1.50 | 550,000 | 1.34 | $ 0.07 | 550,000 |
| $ 1.75 | 4,480,000 | 2.67 | $ 0.64 | 4,480,000 |
| $ 2.00 | 997,180 | 1.13 | $ 0.16 | 997,180 |
| $ 3.00 | 150,000 | 1.57 | $ 0.04 | 150,000 |
| **Balance June 30, 2021** | **10,934,740** | **2.20** | **$ 1.53** | **10,934,740** |

(expressed in Canadian dollars, except share and per share amounts)

## 18. SHARE BASED PAYMENT RESERVE AND STOCK OPTIONS

The Company has established a stock option plan (the "Option Plan") for directors, officers, employees and consultants of the Company. The Company's Board of Directors determines, among other things, the eligibility of individuals to participate in the Option Plan and the term, vesting periods, and the exercise price of options granted to individuals under the Option Plan.

Each share option converts into one common share of the Company on exercise. No amounts are paid or payable by the individual on receipt of the option. The options carry neither the right to dividends nor voting rights. Options may be exercised at any time from the date of vesting to the date of their expiry.

The Company's Option Plan provides that the number of common shares reserved for issuance may not exceed 10% of the number of common shares outstanding. If any options terminate, expire, or are cancelled as contemplated by the Option Plan, the number of options so terminated, expired, or cancelled shall again be available under the Option Plan.

*[i] Measurement of fair values*

There were no options issued during the period ended June 30, 2021. The fair value of share options granted during the periods ended June 30, 2020 was estimated at the date of grant using the Black Scholes option pricing model using the following inputs:

| | **2020** |
|---|---|
| Grant date share price | $1.39 -$2.55 |
| Exercise price | $1.39 - $5.00 |
| Expected dividend yield | 0% |
| Risk-free interest rate | 0.44% - 1.62% |
| Expected option life | 7 – 10 years |
| Expected volatility | 90% |

**Employee and non-employee options**

Expected volatility was estimated by using the historical volatility of other actively traded public companies that the Company considers comparable that have trading and volatility history. The expected option life represents the period of time that options granted are expected to be outstanding. The risk-free interest rate is based on Canada government bonds with a remaining term equal to the expected life of the options.

| | **Options issued/(exercised) / Exercised** | **Weighted average exercise price** |
|---|---|---|
| | # | $ |
| **Outstanding as at December 31, 2019** | **1,627,915** | **8.00** |
| Options issued | 1,030,251 | 2.06 |
| Options cancelled and forfeited | (605,499) | 5.72 |
| Options exercised | (100,000) | 0.10 |
| **Outstanding as at December 31, 2020** | **1,952,667** | **2.94** |
| Options forfeited [i] | (150,250) | 6.87 |
| **Outstanding as at June 30, 2021** | **1,802,417** | **2.61** |

[i] During the six months ended June 30, 2021, 150,250 options were forfeited. The fair value of unvested units are removed from the share base reserve and reduced from retained earnings.

(expressed in Canadian dollars, except share and per share amounts)

## 18. SHARE BASED PAYMENT RESERVE AND STOCK OPTIONS (CONTINUED)

During the six months ended June 30, 2021, the Company recognized a total Share Based Payment expense relating to Options of $280,973 (June 30, 2020 - $971,960).

The following table is a summary of the Company's share options outstanding as at June 30, 2021:

| | Options Outstanding | | Options Exercisable | |
|---|---|---|---|---|
| **Exercise price range** | **Number outstanding** | **Weighted average remaining life** | **Weighted average exercise price** | **Number exercisable** |
| $ | # | (years) | $ | # |
| 1.00 | 623,000 | 1.49 | 0.35 | 406,250 |
| 1.24 | 7,500 | 0.02 | 0.01 | 7,500 |
| 1.39 | 38,000 | 0.10 | 0.03 | 22,167 |
| 2.00 | 367,500 | 0.76 | 0.41 | 367,500 |
| 2.50 | 171,372 | 0.76 | 0.24 | 57,624 |
| 2.75 | 350,950 | 0.89 | 0.54 | 116,983 |
| 5.00 | 14,595 | 0.00 | 0.04 | 13,562 |
| 7.30 | 32,000 | 0.07 | 0.13 | 32,000 |
| 8.00 | 197,500 | 0.48 | 0.88 | 195,833 |
| **Balance June 30, 2021** | **1,802,417** | **4.58** | **2.61** | **1,219,419** |

### Restricted Stock Units

The following table summarized the continuity of the Company's RSUs:

| | **RSUs Issued** | **Weighted average issue price** |
|---|---|---|
| | # | $ |
| **Outstanding as at December 31, 2019** | **98,158** | **8.00** |
| RSUs issued | 946,797 | 1.33 |
| RSUs exercised | (570,153) | 1.73 |
| RSUs forfeited | (34,166) | 2.86 |
| **Outstanding as at December 31, 2020** | 440,636 | 2.30 |
| RSUs exercised [i] | (104,781) | 1.30 |
| RSUs exercised but not yet settled [i] | (10,797) | 0.85 |
| RSUs forfeited [ii] | (23,754) | 3.18 |
| **Outstanding as at June 30, 2021** | 301,304 | 3.40 |

[i] During the six months ended June 30, 2021, 104,781 restricted stock units were exercised. 10,797 units were yet to be settled as of June 30, 2021. The grant price of the exercised units ranged from $0.85 to $1.46.

[ii] During the six months ended June 30, 2021, 23,754 restricted stock units were forfeited. Forfeited units were removed from the share base reserve and reduced from retained earnings.

During the six months ended June 30, 2021, the Company recognized a total Share Based Payment expense relating to Restricted Stock Units of $120,038 (June 30, 2020 - $305,810).

(expressed in Canadian dollars, except share and per share amounts)

## 18. SHARE BASED PAYMENT RESERVE AND STOCK OPTIONS (CONTINUED)

Share based compensation is comprised of the following:

| | For the three months ended June 30, | | For the six months ended June 30 | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| Stock options | $ 155,377 | 971,960 | $ 280,973 | 1,310,152 |
| Restricted Stock Units | 73,853 | 305,810 | 120,038 | 305,810 |
| | **$ 229,230** | **$ 1,277,770** | **$ 401,011** | **$ 1,615,962** |

## 19. NON-CONTROLLING INTEREST

| | June 30, 2021 | December 31, 2020 |
|---|---|---|
| **Opening Balance** | **7,893,712** | 7,488,456 |
| SMGH Recapitalization | - | 2,859,440 |
| Foreign translation | (861,245) | (946,419) |
| Net loss attributed to non-controlling interest | (109,404) | (1,507,765) |
| **Ending Balance** | **6,923,063** | **7,893,712** |

## 20. LONG-TERM INVESTMENT

| | June 30, 2021 | December 31, 2020 |
|---|---|---|
| Balance at the beginning of the year | $ 518,213 | $ 72 |
| Unrealized gain on change in fair value | - | 518,141 |
| **Balance at end of year** | **$ 518,213** | **$ 518,213** |

Long-term investment consists of 720,000 shares in Southern Sun Pharma ("Southern Sun") purchased for a total cost of $72. In 2020, Southern Sun completed a financing through the sale of units at $1.25 per unit. Each unit was comprised of one common share and one-half common share purchase warrant. Each whole warrant entitled the holder to purchase an additional share at $1.50 at any time up to 18 months following the closing date. Due to this financing, the Company recognized an unrealized gain from the change in fair value of $518,141 for the year ended December 31, 2020. As of June 30, 2021, there have been no events which would imply a change in the fair value of the investment.

## 21. FINANCIAL RISK MANAGEMENT AND FINANCIAL INSTRUMENTS

### Credit risk

Credit risk is the risk of financial loss to the Company if a customer or counterparty to a financial instrument fails to meet its contractual obligations and arises principally from deposits with banks and outstanding receivables. The Company does not hold any collateral as security but mitigates this risk by dealing only with what management believes to be financially sound counterparties and, accordingly, does not anticipate significant loss for non-performance.

The Company believes that the trade and other receivables balance is fully collectable. As of June 30, 2021, $1,017,167 in trade and other receivables remained outstanding (December 31, 2020 - $708,673). The Company applies the simplified approach to providing for expected credit losses as prescribed by IFRS 9, which permits the use of lifetime expected loss provision for all trade receivables. The loss allowance is based on the Company's historical collection and loss experience and incorporates forward looking factors, where appropriate.

The Company has recorded an additional loss provision of $41,639 during the six months ended June 30, 2021 (June 30, 2020 - $nil).

(expressed in Canadian dollars, except share and per share amounts)

## 21. FINANCIAL RISK MANAGEMENT AND FINANCIAL INSTRUMENTS (CONTINUED)

### Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its financial obligations as they become due. The Company's exposure to liquidity risk is dependent on the Company's ability to raise additional financing to meet its commitments and sustain operations. The Company mitigates liquidity risk by management of working capital, cash flows and the issuance of share capital.

In addition to the commitments disclosed, the Company is obligated to the following contractual maturities of undiscounted cash flows:

| | Carrying amount | Contractual cash flows | Year 1 | Year 2 | Year 3 |
|---|---|---|---|---|---|
| Amounts payable | $ 6,131,177 | $ 6,131,177 | $ 6,131,177 | $ - | $ - |
| Convertible Debentures | 262,781 | 300,000 | 300,000 | - | - |
| Lease liability | 260,037 | 281,187 | 224,950 | 56,238 | - |
| | $ 6,653,995 | $ 6,712,364 | $ 6,656,127 | $ 56,238 | $ - |

The due to related party balance of $4,111,725 is not intended to be repaid. As these amounts become due, the outstanding balances can be converted into common shares of SMGH, consistent with current ownership splits.

### Market risk

Market risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices. Market risk comprises three types of risk: currency rate risk, interest rate risk and other price risk.

*Currency risk*

Currency risk is the risk to the Company's earnings that arise from fluctuations of foreign exchange rates. The Company is exposed to foreign currency exchange risk as it has substantial operations based out of Colombia and record keeping is denominated in a foreign currency. As such the company has foreign currency risk associated with Colombian Pesos.

*Interest 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 is not exposed to interest rate as it does not have any borrowings.

*Other price risk*

Other price risk is the risk that the fair value or future cash flows of a financial instrument will fluctuate because of changes in market prices of the Company's cannabis products (other than those arising from interest rate risk or currency risk), whether those changes are caused by factors specific to the individual financial instrument or its issuer, or factors affecting all similar financial instruments traded in the market.

### Fair values

The carrying values of cash, amounts receivable, prepaid assets, investments and amounts payable approximate the fair values due to the short-term nature of these items. The risk of material change in fair value is not considered to be significant due to a relatively short-term nature. The Company does not use derivative financial instruments to manage this risk.

Financial instruments recorded at fair value on the condensed consolidated interim statement of financial position are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The Company categorizes its fair value measurements according to a three-level hierarchy as disclosed in Note 3. The hierarchy prioritizes the inputs used by the Company's valuation techniques. A level is assigned to each fair value measurement based on the lowest-level input significant to the fair value measurement in its entirety.

(expressed in Canadian dollars, except share and per share amounts)

## 21. FINANCIAL RISK MANAGEMENT AND FINANCIAL INSTRUMENTS (CONTINUED)

The Company's finance team performs valuations of financial items for financial reporting purposes, including level 3 fair values, in consultation with third party valuation specialists for complex valuations. Valuation techniques are selected based on the characteristics of each instrument, with the overall objective of maximizing the use of market – based information.

The fair value hierarchy requires the use of observable market inputs whenever such inputs exist. A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value. Cash is classified as a Level 1 financial instrument and the derivative asset is classified as a level 3 instrument. During the year, there were no transfers of amounts between Level 1, Level 2 and Level 3.

The value of the derivative instrument was determined using a discounted cash flow model, with assumptions on the discount rate and the probability of the triggering event. The following table provides information about the sensitivity of the fair value measurement to changes in the most significant inputs for the LC2019 derivative asset classified as Level 3. As at June 30, 2021, the assumptions used to determine the fair market value of the derivative instrument were consistent with those used at December 31, 2020.

## 22. GENERAL AND ADMINISTRATIVE EXPENSES

| | For the three months ended June 30, | | For the six months ended June 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| General and administrative | $ 550,092 | $ 1,105,165 | $ 1,273,240 | $ 1,752,932 |
| Selling marketing and promotion | 84,363 | 92,496 | 205,267 | 122,622 |
| Consulting fees | 437,033 | 393,120 | 922,974 | 659,007 |
| Professional fees | 277,447 | 164,318 | 506,329 | 826,670 |
| Salaries and wages | 1,063,229 | 1,079,964 | 2,222,772 | 2,587,467 |
| Research and development | 53,472 | 75,899 | 114,110 | 104,707 |
| Board fees | 53,500 | 13,500 | 115,000 | 57,000 |
| | **$ 2,519,136** | **$ 2,924,462** | **$ 5,359,692** | **$ 6,110,405** |

During the six months ended June 30, 2021, as part of its inventory costing process, the Company capitalized $160.507 of salaries to inventory and biological assets (June 30, 2020 - $264,480).

## 23. NON-CASH OPERATING ELEMENTS OF WORKING CAPITAL

The table is a breakdown of the non-cash elements of working capital presented on the statement of cash flows:

| | For the three months end June 30, | | For the six months end June 30, | |
|---|---|---|---|---|
| | 2021 | 2020 | 2021 | 2020 |
| Amounts receivable | $ 91,448 | $ (757,993) | $ (551,766) | $ (225,566) |
| Biological assets | (39,476) | 2,079,418 | 443,328 | 86,082 |
| Inventory | 230,283 | (2,152,336) | (847,642) | (2,442,320) |
| Prepaid assets | (178,015) | 198,508 | 338,683 | (226,330) |
| Accounts payable | 56,799 | 1,064,111 | (252,916) | 1,157,919 |
| | **$ 161,039** | **$ 431,708** | **$ (870,313)** | **$ (1,650,215)** |

## 24. SUBSEQUENT EVENTS

On August 19, 2021, the Company closed a secured term loan financing of $2,118,000. The Term Loan is subject to an original issue discount of approximately 15%, such that $1,800,000 was advanced by the lender to the Company. The Term Loan is due October 19, 2022.