CANNARA BIOTECH INC.

Condensed Interim Consolidated Financial Statements

For the three-month periods ended November 30, 2021 and 2020
(Unaudited)

CANNARA BIOTECH INC.

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(Unaudited)

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Financial Statements of Cannara Biotech Inc.

CANNARA BIOTECH INC.

Condensed Interim Consolidated Statement of Financial Position
As at November 30, 2021 and August 31, 2021
(Unaudited – in Canadian dollars)

	November 30, 2021	August 31, 2021
Assets		
Current assets		
Cash	$ 14,143,313	$ 8,159,305
Accounts receivable	3,609,827	2,847,725
Sales tax receivable	–	47,756
Lease receivable	100,468	72,680
Biological assets (note 3)	1,654,558	1,902,206
Inventory (note 4)	6,471,033	5,508,258
Prepaid expenses and other assets	822,424	708,803
	26,801,623	19,246,733
Lease receivable	65,632	73,164
Deposits	396,114	396,114
Deposits on property, plant and equipment	1,387,977	556,803
Property, plant and equipment (note 5)	73,313,054	71,517,251
Right-of-use asset (note 6)	176,175	232,548
	$ 102,140,575	$ 92,022,613
Liabilities and Shareholders' Equity		
Current liabilities		
Accounts payable and accrued liabilities	$ 6,256,122	$ 6,263,201
Sales tax payable	171,284	–
Deferred lease revenue	293,636	3,348
Current portion of long-term debt	3,386	9,564
Current portion of deferred grant income	38,101	32,043
Current portion of lease liabilities (note 6)	237,561	225,642
Current portion of mortgages payable (note 7)	1,100,000	300,000
	8,100,090	6,833,798
Long-term debt (note 7)	2,046	2,611
Lease liabilities (note 6)	152,667	216,854
Convertible debentures (note 7)	8,733,193	8,466,008
Deferred grant income	829,142	705,079
Mortgages payable (note 7)	20,801,628	11,682,451
	38,618,766	27,906,801
Shareholders' equity		
Share capital	83,208,150	83,208,150
Contributed surplus	9,378,622	9,412,746
Deficit	(29,135,648)	(28,605,149)
Accumulated other comprehensive income	70,685	100,065
Total equity	63,521,809	64,115,812
Contingencies (note 15)		
Subsequent events (note 17)		
	$ 102,140,575	$ 92,022,613

See accompanying notes to condensed interim consolidated financial statements.

CANNARA BIOTECH INC.

Condensed Interim Consolidated Statement of Net Loss and Comprehensive Loss
For the three-month periods ended November 30, 2021 and 2020
(Unaudited)

	Three-month periods ended November 30, 2021	Three-month periods ended November 30, 2020
Revenue		
Revenue from sale of goods (note 12)	$ 6,967,318	$ 777,406
Excise taxes	(1,538,987)	–
Net revenue from sale of goods	5,428,331	777,406
Lease revenue (note 12)	899,004	556,932
Other income	237,241	33,843
	6,564,576	1,368,181
Cost of sales		
Cost of goods sold (note 4)	3,480,123	773,189
Lease operating costs	70,428	98,847
Gross profit before fair value adjustments	3,014,025	496,145
Changes in fair value of inventory sold (note 4)	(1,866,480)	(203,310)
Unrealized gain (loss) on changes in fair value of biological assets (note 3)	1,472,497	(790,195)
Gross profit (loss)	2,620,042	(497,360)
Operating expenses		
General and administrative (note 10)	1,605,257	1,143,535
Research and development	256,495	550,394
Selling, marketing and promotion	299,592	265,079
Professional and legal fees	232,380	323,344
Share-based compensation (note 9)	(34,124)	103,721
Amortization (note 5 and 6)	231,901	274,489
Gain on sublease agreement (note 6)	(12,876)	–
Loss on disposal of property, plant and equipment	24,662	–
	2,603,287	2,660,562
Operating income (loss)	16,755	(3,157,922)
Net finance expense (note 11)	547,254	337,111
Net loss	(530,499)	(3,495,033)
Other comprehensive income (loss)		
Foreign currency translation adjustments	(29,380)	13,787
Total comprehensive loss	$ (559,879)	$ (3,481,246)
Basic and diluted loss per share	$ (0.01)	(0.01)
Weighted average number of outstanding shares	876,481,321	737,746,649

See accompanying notes to condensed interim consolidated financial statements.

CANNARA BIOTECH INC.

Condensed Interim Consolidated Statement of Changes in Equity
For the three-month periods ended November 30, 2021 and 2020
(Unaudited)

	Shares		Share capital		Contributed surplus		Deficit		Accumulated other comprehensive income		Total equity
As at August 31, 2021	876,481,321	$	83,208,150	$	9,412,746	$	(28,605,149)	$	100,065	$	64,115,812
Net loss	–		–		–		(530,499)		–		(530,499)
Other comprehensive loss											
Foreign currency translation adjustments	–		–		–		–		(29,380)		(29,380)
Comprehensive loss	–		–		–		(530,499)		(29,380)		(559,879)
Share-based compensation (note 9)											
Employee compensation	–		–		(34,983)		–		–		(34,983)
Other services	–		–		859		–		–		859
	–		–		(34,124)		–		–		(34,124)
As at November 30, 2021	876,481,321	$	83,208,150	$	9,378,622	$	(29,135,648)	$	70,685	$	63,521,809

	Shares		Share capital		Contributed surplus		Deficit		Accumulated other comprehensive income		Total equity
As at August 31, 2020	737,738,815	$	58,361,592	$	7,034,550	$	(27,077,006)	$	45,725	$	38,364,861
Net loss	–		–		–		(3,495,033)		–		(3,495,033)
Other comprehensive income											
Foreign currency translation adjustments	–		–		–		–		13,787		13,787
Comprehensive loss	–		–		–		–		13,787		13,787
Share-based compensation (note 9)											
Employee compensation	–		–		131,836		–		–		131,836
Other services	–		–		3,888		–		–		3,888
	–		–		135,724		–		–		135,724
Issuance of shares to settle a liability	100,720		10,072		–		–		–		10,072
As at November 30, 2020	737,839,535	$	58,371,664	$	7,170,274	$	(30,572,039)	$	59,512	$	35,029,411

See accompanying notes to condensed interim consolidated financial statements.

CANNARA BIOTECH INC.

Condensed Interim Consolidated Statement of Cash Flows
For the three-month periods ended November 30, 2021 and 2020
(Unaudited)

	November 30, 2021	November 30, 2020
Cash provided by (used in):		
Operating		
Net loss	$ (530,499)	$ (3,495,033)
Items not involving cash:		
Changes in fair value of inventory sold (note 4)	1,866,480	203,310
Unrealized (gain) loss on changes in fair value of biological assets (note 3)	(1,472,497)	790,195
Amortization of property, plant and equipment (note 5)	745,255	621,221
Amortization of right-of-use asset (note 6)	29,796	45,534
Amortization of intangible asset	–	41,047
Interest expense (note 11)	376,370	299,467
Interest on lease liabilities (note 6)	19,642	29,685
Accretion on financing and amortization of financing costs (note 7)	178,091	6,672
Share-based compensation (note 9)	(34,124)	135,724
Gain on sublease (note 6)	(12,876)	–
Loss on disposal of property, plant and equipment	24,662	–
Interest income (note 11)	(15,839)	(16,946)
Other	58	154
Net change in non-cash operating working capital items (note 16)	(1,061,059)	(2,152,407)
	113,460	(3,491,377)
Financing		
Private placement issuance costs	(25,250)	–
Convertible debenture issuance costs	(24,888)	–
Proceeds from mortgage (note 7)	22,000,000	–
Mortgage payments (note 7)	(12,000,000)	(75,000)
Deferred mortgage costs	(98,372)	–
Proceeds from credit facilities	–	1,000,000
Deferred credit facilities costs	–	(31,238)
Interest paid on financing (note 7)	(269,663)	(191,088)
Lease payments (note 6)	(71,910)	(80,394)
Long-term debt payments	(591)	(886)
	9,509,326	621,394
Investing		
Interest received	5,164	15,114
Deposits on property, plant and equipment	(831,174)	(31,475)
Acquisitions of property, plant and equipment (note 5)	(2,817,344)	(827,922)
Proceeds from disposal of property, plant and equipment	33,956	–
	(3,609,398)	(844,283)
Net change in cash	6,013,388	(3,714,266)
Effect of foreign exchange on cash	(29,380)	13,841
Cash, beginning of period	8,159,305	7,771,177
Cash, end of period	$ 14,143,313	$ 4,070,752

See accompanying notes to condensed interim consolidated financial statements.

1. Nature of operations

Cannara Biotech Inc. (hereafter the "Company" or "Cannara") is an emerging vertically integrated cannabis company focused on the cultivation, processing and sale of premium dried cannabis and cannabis derivates under The Cannabis Act, and offers its product for sale to consumers in Québec and throughout Canada. The Company is domiciled in Canada and was incorporated under the laws of British Columbia on October 19, 2017. Its head office is located at 333 Décarie, Suite 200, Ville St-Laurent, Québec, H4N 3M9. The Company's common shares are listed under the symbol "LOVE" on the Canadian Stock Exchange in Canada, "LOVFF" on the OTCQB Venture Market in the United States and "8CB" on the Frankfurt Stock Exchange in Germany.

Cannara owns and operates two Quebec-based cultivation facilities spanning over 1,650,000 square feet. Cannara's first purpose-built, modern indoor cultivation facility is located in Farnham, Quebec and measures 625,000 square feet, comprising 170,000 square feet of operational licensed area and 455,000 square feet of leased warehouse space ("Farnham Facility"). The second facility, acquired in June 2021 is a hybrid greenhouse facility that is being redesigned by zone to replicate the indoor cultivation environment, including growing without utilizing the sun. The redesign of its two first zones have been completed to date, with the first zone fully planted at the end of November 2021. The facility is comprised of 24 independent growing zones totaling 600,000 square feet, a 200,000 square feet cannabis 2.0 processing center and a 200,000 square feet rooftop greenhouse located in Valleyfield, Quebec ("Valleyfield Facility"). Cannara operates through its wholly owned subsidiaries, Cannara Biotech (Quebec) Inc. and Cannara Biotech (Valleyfield) Inc., both holding active licenses issued by Health Canada under the Cannabis Act.

The Company commenced its first commercial retail sale at the end of February 2021 and continues to fulfill market demand with weekly reorders. The Company is currently focused on its expansion with the Valleyfield Facility in order to be able to respond to current market demand for its products. During the first quarter of 2022, capital expenditures and start-up costs were incurred to render the Valleyfield Facility operational. The Company incurred a net loss of approximately $0.5 million during the three-month period ended November 30, 2021 (2021 – net loss of $3.5 million). The Company expects to have its first finished product available for sale from the Valleyfield Facility in the third quarter of 2022. The Company expects that its existing cash resources of $14.1 million as at November 30, 2021, along with the forecasted cash flows that occurred subsequent to quarter-end, will enable it to fund its planned operating expenses for at least the next twelve months from November 30, 2021. The Company has a deficit of approximately $29.1 million as at November 30, 2021 (August 31, 2021 - $28.6 million).

The ability of the Company to ultimately achieve future profitable operations is dependent upon the continued success of its product from its two facilities and brand pipeline in addition to maintaining the consistency of its grow operations and lean cost. The Company expects to finance its operations through its wholesale and retail sales, existing cash, and/or a combination of public or private equity and debt financing or other sources.

1. Nature of operations

COVID-19

The effects of COVID-19 have had limited impact on the business; however, the situation is dynamic, and the ultimate duration and magnitude of the impact on the economy and on the Company’s business are not known at this time.

2. Basis of preparation and significant accounting policies

(a) Statement of compliance

These condensed interim consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS") and International Accounting Standard ("IAS") 34, *Interim Financial Reporting*, as issued by the International Accounting Standards Board ("IASB").

These condensed interim financial statements were approved by the Board of Directors and authorized for issuance on January 20, 2022.

(b) Basis of preparation

The condensed interim consolidated financial statements were prepared using the same accounting policies as set forth in Notes 2 and 3 in the audited financial statements of the Company for the year ended August 31, 2021. These condensed interim consolidated financial statements do not include all the notes required in annual consolidated financial statements. Therefore, these condensed interim consolidated financial statements should be read in conjunction with the audited consolidated financial statements and notes thereto of the Company for the year ended August 31, 2021.

The preparation of the Company’s condensed interim consolidated financial statements in conformity with IFRS requires management to make judgements, estimates and assumptions that affect the application of accounting policies and the reported amounts of expenditures, assets and liabilities. Actual results could differ from those estimates.

On an ongoing basis, estimates and judgements are evaluated. The Company bases its estimates on the most probable set of economic conditions and planned course of action, historical experience, known trends and events, and various other factors believed to be reasonable under the circumstances, the results of which form the basis for making judgements about the carrying values of assets and liabilities that are not readily apparent from other sources. Actual results may differ from these estimates under different assumptions or conditions. Uncertainty about these assumptions and estimates could result in an outcome that requires material adjustments to the carrying amount of the asset or liability affected in future periods. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to accounting estimates are recognized in the period in which these estimates are revised and in any future periods affected.

2. Basis of preparation and significant accounting policies (continued)

(b) Basis of preparation

The critical accounting judgements and key sources of estimate uncertainty are consistent with those in the audited consolidated financial statements and notes thereto to the Company for the year ended August 31, 2021.

3. Biological assets

The Company's biological assets consist of cannabis plants up to the point of harvest. The changes in the carrying values of biological assets are as follows:

Carrying amount, August 31, 2020	$	1,313,370
Production costs capitalized		6,164,853
Net change in fair value due to biological transformation, less cost to sell		6,015,165
Transferred to cost of good sold – sale of clones		(72,000)
Transferred to inventory upon harvest		(11,519,182)
Carrying amount, August 31, 2021	$	1,902,206
Production costs capitalized		1,516,262
Net change in fair value due to biological transformation, less cost to sell		1,472,497
Transferred to inventory upon harvest		(3,236,407)
Carrying amount, November 30, 2021	$	1,654,558

The estimates used in determining the fair value of cannabis plants are as follows:

- expected average wholesale and retail selling price per gram of harvested cannabis;
- expected cost to complete and cost to sell;
- expected yield per cannabis plant;
- stage of completion in the production process (days remaining until harvest); and
- expected plant loss based on their various stages of growth.

The valuation of biological assets is based on an income approach in which the fair value at the point of harvesting is estimated based on selling prices less the costs to sell. For in-process biological assets, the fair value at point of harvest is adjusted based on the stage of growth at period-end. Stage of growth is determined by reference to the time incurred as a percentage of total weeks of growth as applied to estimated total fair value per gram (less costs to complete and costs to sell) to arrive at an in-process fair value for estimated biological assets, which have not yet been harvested.

3. Biological assets (continued)

Because there is no actively traded commodity market for cannabis plants and dried products, the valuation of the biological assets is obtained using valuations techniques where the inputs are based upon unobservable market data and are classified as level 3 in the fair market value hierarchy. There has been no transfer between levels as at November 30, 2021.

Management's identified significant unobservable inputs, their values and sensitivity analysis are presented in the tables below.

The income approach calculates the present value of expected future cash flows from the Company's biological assets using the following inputs for the period ended November 30, 2021:

Unobservable inputs	Input values	Sensitivity analysis
Average selling price Represents the average expected selling price per gram of dried cannabis, excluding excise taxes, where applicable, which is expected to approximate future selling prices.	$1.90 to $4.80 per gram (August 31, 2021 - $1.30 to $4.80 per gram)	An increase or decrease of 5% applied to the average selling price would result in a change of approximately $126,000 to the valuation (August 31, 2021 - $161,000).
Yield per plant Represents the average number of grams of dried cannabis expected to be harvested from each cannabis plant.	82 grams per plant (August 31, 2021 – 86 grams per plant)	An increase or decrease of 5% applied to the average yield per plant would result in a change of approximately $74,000 to the valuation (August 31, 2021 - $97,000).
Stage of completion Calculated by taking the average number of days in the cultivation cycle over the total estimated duration of a cultivation cycle which is currently approximately 13 to 14 weeks from clone to harvest.	Weighted average stage of completion is 37% (August 31, 2021 – 47%)	An increase or decrease of 5% applied to the average stage of growth per plant would result in a change of approximately $71,000 to the valuation (August 31, 2021 - $92,000).

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.

As at November 30, 2021, it is expected that the Company's biological assets will yield approximately 1,916 kilograms of dried cannabis when harvested (August 31, 2021 – 1,926 kilograms of dried cannabis).

4. Inventory

The inventory consists of the following:

	Capitalized cost	Fair value adjustment[1]	November 30, 2021 Total
Raw materials - cultivation and supplies	$ 1,155,529	$ –	$ 1,155,529
Harvested cannabis			
Dried cannabis and work-in-progress	2,085,195	1,674,516	3,759,711
Finished goods	676,772	388,543	1,065,315
Derivative products			
Work-in-progress	423,329	(87,417)	335,912
Finished goods	107,750	(33,089)	74,661
Finished goods - U.S. hemp-based CBD products for resale	79,905	–	79,905
	$ 4,528,480	$ 1,942,553	$ 6,471,033

	Capitalized cost	Fair value adjustment[1]	August 31, 2021 Total
Raw materials - cultivation and supplies	$ 656,027	$ –	$ 656,027
Harvested cannabis			
Dried cannabis and work-in-progress	2,065,248	2,058,053	4,123,301
Finished goods	247,373	173,180	420,553
Derivative products	349,742	(122,712)	227,030
Finished goods - U.S. hemp-based CBD products for resale	81,347	–	81,347
	$ 3,399,737	$ 2,108,521	$ 5,508,258

[1] Fair value adjustment represent the fair value adjustment transferred from biological assets at harvest.

The amount of inventory expensed as cost of goods sold during the three-month period ended November 30, 2021 was $3,480,123 (2021 – $773,189), including an impairment loss on inventory of $18,892 for cannabis that cost exceeds its net realizable value (2021 - $210,493).

5. Property, plant and equipment

	Land	Buildings	Facility production equipment	Computer equipment and software	Vehicles	Furniture and fixtures	Construction in progress	Total
Cost								
Balance as at August 31, 2021	$ 2,452,085	$ 44,792,468	$ 5,833,454	$ 1,262,343	$ 18,440	$ 1,352,642	$ 21,234,527	$ 76,945,959
Additions	–	267,971	731,373	75,656	–	25,159	1,499,517	2,599,676
Disposal	–	–	(63,009)	–	–	–	–	(63,009)
Balance as at November 30, 2021	$ 2,452,085	$ 45,060,439	$ 6,501,818	$ 1,337,999	$ 18,440	$ 1,377,801	$ 22,734,044	$ 79,482,626
Accumulated depreciation								
Balance as at August 31, 2021	$ –	$ (3,881,432)	$ (828,841)	$ (421,653)	$ (3,771)	$ (293,011)	$ –	$ (5,428,708)
Amortization	–	(501,504)	(152,331)	(54,709)	(923)	(35,788)	–	(745,255)
Disposal	–	–	4,391	–	–	–	–	4,391
Balance as at November 30, 2021	$ –	$ (4,382,936)	$ (976,781)	$ (476,362)	$ (4,694)	$ (328,799)	$ –	$ (6,169,572)
Net book value								
Balance as at November 30, 2021	$ 2,452,085	$ 40,677,503	$ 5,525,037	$ 861,637	$ 13,746	$ 1,049,002	$ 22,734,044	$ 73,313,054

For the three-month period ended November 30, 2021, the assets included in construction in progress represents the Valleyfield Facility and related capital expenditures incurred to render the facility operational and for the redesign of the cultivation zones in addition to post-harvest capital improvements at the Farnham Facility to process cannabis that will be received from the Valleyfield Facility.

During the three-month period ended November 30, 2021, the Company recognized $745,255 as depreciation, of which $202,105 has been recognized in the consolidated statement of loss and comprehensive loss and $543,150 has been included in the calculation of the cannabis valuation.

5. Property, plant and equipment (continued)

	Land	Buildings	Facility production equipment	Computer equipment and software	Vehicles	Furniture and fixtures	Construction in progress	Total
Cost								
Balance as at August 31, 2020	$ 1,104,963	$ 37,629,164	$ 4,660,531	$ 1,191,489	$ 9,940	$ 1,340,126	$ –	$ 45,936,213
Additions	1,419,032	7,327,991	1,240,969	70,854	8,500	12,516	21,234,527	31,314,389
Disposal	(71,910)	(164,687)	(68,046)	–	–	–	–	(304,643)
Balance as at August 31, 2021	$ 2,452,085	$ 44,792,468	$ 5,833,454	$ 1,262,343	$ 18,440	$ 1,352,642	$ 21,234,527	$ 76,945,959
Accumulated depreciation								
Balance as at August 31, 2020	$ –	$ (2,038,419)	$ (347,506)	$ (211,813)	$ (553)	$ (150,749)	$ –	$ (2,749,040)
Amortization	–	(1,855,733)	(489,536)	(209,840)	(3,218)	(142,262)	–	(2,700,589)
Disposal	–	12,720	8,201	–	–	–	–	20,921
Balance as at August 31, 2021	$ –	$ (3,881,432)	$ (828,841)	$ (421,653)	$ (3,771)	$ (293,011)	$ –	$ (5,428,708)
Net book value								
Balance as at August 31, 2021	$ 2,452,085	$ 40,911,036	$ 5,004,613	$ 840,690	$ 14,669	$ 1,059,631	$ 21,234,527	$ 71,517,251

During the three-month period ended November 30, 2020, the Company recognized $621,221 as depreciation expense, of which $187,908 has been recognized in the consolidated statement of loss and comprehensive loss and $433,313 has been included in the calculation of the cannabis valuation.

6. Right-of-use asset and lease liabilities

(a) Right-of-use asset

		November 30, 2021		August 31, 2021
Cost				
Balance, beginning of period	$	630,024	$	765,780
Derecognition of portion related to sublease agreement [(i)]		(80,038)		(135,756)
Balance, end of period	$	549,986	$	630,024
Accumulated depreciation				
Balance, beginning of period	$	(397,476)	$	(308,881)
Amortization		(29,796)		(167,489)
Derecognition of portion related to sublease agreement [(i)]		53,461		78,894
Balance, end of period	$	(373,811)	$	(397,476)
Net book value				
Balance, end of period	$	176,175	$	232,548

[(i)] Sublease

On November 1, 2021, the Company and a third party entered into a sublease agreement to lease a portion of the Company's head office location. The Company is entitled to equal monthly payments of $2,480 up to the term of the agreement on May 31, 2023.

The Company has classified the sublease as a finance lease because the sub-lease is for the whole of the remaining term on the original lease.

On initial recognition, the portion of the original right-of-use asset subleased for a net total of $26,577 has been derecognized and a lease receivable was recognized of $39,453, which resulted in a gain of $12,876.

6. Right-of-use asset and lease liabilities (continued)

(b) Lease liabilities

		November 30, 2021		August 31, 2021
Maturity analysis - contractual undiscounted cash flows:				
Less than one year	$	289,197	$	288,306
One to five years		160,845		233,589
Total undiscounted lease liabilities	$	450,042	$	521,895
Current	$	237,561	$	225,642
Non-current		152,667		216,854
Lease liabilities included in the condensed interim consolidated statement of financial position	$	390,228	$	442,496

Balance as at August 31, 2021	$	442,496
Rent paid		(71,910)
Interest on lease liabilities		19,642
Balance as at November 30, 2021	$	390,228

7. Financing

(a) Mortgages payable

On November 30, 2021, the Company amended its existing credit agreement with Canadian Imperial Bank of Commerce ("CIBC"), increasing its current installment loan from $5.4 million to $22 million, for which the proceeds were used to repay existing mortgages payable and for capital expenditures required to redesign and render the Valleyfield Facility operational.

Net carrying value, August 31, 2021	$	11,982,451
Proceeds from mortgage		22,000,000
Payments		(12,000,000)
Mortgage issuance costs		(98,372)
Amortization of deferred financing costs		17,549
Net carrying value, November 30, 2021	$	21,901,628

7. Financing (continued)

(a) Mortgages payable (continued)

		November 30, 2021		August 31, 2021
Mortgage payable (i)	$	22,000,000	$	–
Mortgage payable (ii)		–		6,550,000
Mortgage payable (iii)		–		5,450,000
Less: unamortized financing costs		(98,372)		(17,549)
		21,901,628		11,982,451
Short-term portion of mortgages payable		(1,100,000)		(300,000)
	$	20,801,628	$	11,682,451

(i) The interest rate on the mortgage loan with CIBC is prime rate + 2% and/or the banker acceptance (“BA”) rate + 3.5%. As at November 30, 2021, the interest rate related to this mortgage was 4.45%. The term of the mortgage loan is 3 years, renewable for additional 3-year terms at option of the lender. If the loan is always renewed, the final term of the mortgage loan would be November 30, 2041. The loan is reimbursable monthly by 240 equal installments of $91,667 plus accrued interest. The loan is secured by a first ranking mortgage against the Farnham Facility. The mortgage is secured by a guarantee executed by a related party. The mortgage also contains a financial covenant requiring the Company to maintain a debt service ratio of no less than 1.25 to 1.0 at each year-end, relating to its Farnham Facility operations.

(ii) The interest rate on the mortgage is 13% per annum, payable monthly. During the three-month period ended November 30, 2021 the Company recognized $216,958 as interest expense for this mortgage (2021 - $212,292). The mortgage term was due on March 6, 2023 but it was repaid on November 30, 2021 as part of the refinancing arrangement.

(iii) The interest rate on the mortgage loan is prime rate + 2% and/or the banker acceptance (“BA”) rate. As at November 30, 2021, the interest rate related to this mortgage was 4.45%. During the three-month period ended November 30, 2021, the Company recognized $52,706 as interest expense for this mortgage (2021 - $63,312). The mortgage term was October 9, 2039 but it was repaid on November 30, 2021 as part of the refinancing arrangement.

7. Financing (continued)

(b) Convertible debentures

The rollforward of the financial liability component of the convertible debentures is as follows:

Net carrying value, August 31, 2020	$	–
Convertible A		4,448,551
Convertible B		3,902,214
Issuance costs		(59,955)
Interest expense		71,748
Accretion and amortization of deferred issuance costs		103,450
Net carrying value, August 31, 2021		8,466,008
Interest expense		106,707
Accretion and amortization of deferred issuance costs		160,478
Net carrying value, November 30, 2021	$	8,733,193

As at November 30, 2021, accrued interest of $178,455 were included in account payable and accrued liabilities (August 31, 2021 - $71,748).

8. Share capital

(a) Authorized

The Company has an unlimited number of voting and participating common shares.

9. Share-based compensation

The Company has established a share option plan whereby certain personnel may be granted options to acquire shares under the terms of the employee share option plan or shares may be granted to third parties in exchange for services. The number and characteristics of share options granted under the employee share option plan are determined by the Board of Directors of the Company but cannot exceed 10% of the outstanding balance of shares issued. The characteristics of share options granted to third parties for services are determined on a case-by-case basis.

9. Share-based compensation (continued)

The share options granted under the employee share option plan vest 25% after the first anniversary of the grant date with the remainder vesting in 36 monthly consecutive equal installments and expire five years from the date of issue. The plan provides for the issuance of common shares at an exercise price determined by the Board of Directors which is not lower than the fair value of the common shares on the grant date. Outstanding options under the plan are granted with service requirements (or service conditions) and become exercisable upon vesting. The share options granted to third parties for services have vesting terms determined on a case-by-case basis.

The activity of outstanding share options for the three-month period ended November 30, 2021 was as follows:

	November 30, 2021			November 30, 2020		
	Number		Weighted average exercise price	Number		Weighted average exercise price
Outstanding, beginning of period	36,539,337	$	0.21	41,929,793	$	0.20
Granted	–		–	250,000		0.18
Forfeited	(2,420,834)		0.18	(1,019,583)		0.11
Expired	(1,354,170)		0.18	(174,792)		0.18
Outstanding, end of period	32,764,333		0.21	40,985,418		0.20
Exercisable, end of period	26,673,283	$	0.22	25,304,513	$	0.23

During the three-month period ended November 30, 2021, the Company recorded a share-based compensation expense/(recovery) of ($34,124) (2021 - $135,724), for which ($34,124) was recognized in the consolidated statement of loss and comprehensive loss (2021 - $103,721) and nil was classified in the calculation of the cannabis valuation (2021 - $32,003).

10. General and administrative

	Three-month periods ended			
		November 30, 2021		November 30, 2020
Salaries and benefits	$	715,169	$	703,760
Administrative and regulatory expense		317,728		203,056
Facility expense		508,052		216,927
Travel		64,308		19,792
General and administrative	$	1,605,257	$	1,143,535

11. Net finance expense

	Three-month periods ended	
	November 30, 2021	November 30, 2020
Interest income	$ 15,839	$ 16,946
Foreign exchange gain	21,560	–
Finance income	37,399	16,946
Interest on mortgage payable	269,663	275,604
Interest on lease liabilities	19,642	29,685
Interest on credit facilities	–	23,863
Interest on convertible debentures	106,707	–
Accretion and amortization of financing costs	178,091	6,672
Other finance expense	10,550	98
Foreign exchange loss	–	18,135
Finance expense	584,653	354,057
Net finance expense	$ 547,254	$ 337,111

12. Segment disclosures

(a) Reportable segments

The Company operates in two segments: (1) Cannabis operations which encompasses the cultivation, processing and sale of premium dried cannabis and cannabis derivatives exclusively for the Quebec and Canadian market and other related revenues ("Cannabis operations") and (2) Real estate operations related to the Farnham building ("Real estate operations").

The chief operating decision-maker assesses performance based on segment operating results which were defined as segment operating income (loss) before share-based compensation, amortization, net finance expense, gain on sublease initial recognition, loss on disposal of property, plant and equipment and income tax. Categorized as Other are items related to U.S. hemp-based CBD products revenues and related operating costs. The accounting policies of the segments are the same as those described in Note 3 of the audited financial statements of the Company for the year ended August 31, 2021.

12. Segment disclosures (continued)

(a) Reportable segments (continued)

	Three-month period ended November 30, 2021				Three-month period ended November 30, 2020			
	Cannabis operations	Real estate operations	Other	Total	Cannabis operations	Real estate operations	Other	Total
Revenue								
Revenue from sale of goods	$ 6,954,968	$ –	$ 12,350	$ 6,967,318	$ 679,125	$ –	$ 98,281	$ 777,406
Excise taxes	(1,538,987)	–	–	(1,538,987)	–	–	–	–
Net revenue from sale of goods	5,415,981	–	12,350	5,428,331	679,125	–	98,281	777,406
Lease revenue	–	899,004	–	899,004	–	556,932	–	556,932
Other income	237,241	–	–	237,241	33,843	–	–	33,843
	5,653,222	899,004	12,350	6,564,576	712,968	556,932	98,281	1,368,181
Cost of sales								
Cost of goods sold	3,472,934	–	7,189	3,480,123	689,955	–	83,234	773,189
Lease operating costs	–	70,428	–	70,428	–	98,847	–	98,847
Segment gross profit before fair value adjustments	2,180,288	828,576	5,161	3,014,025	23,013	458,085	15,047	496,145
Changes in fair value of inventory sold	(1,866,480)	–	–	(1,866,480)	(203,310)	–	–	(203,310)
Unrealized gain (loss) on changes in fair value of of biological assets	1,472,497	–	–	1,472,497	(790,195)	–	–	(790,195)
Segment gross profit (loss)	1,786,305	828,576	5,161	2,620,042	(970,492)	458,085	15,047	(497,360)
Operating expenses	2,368,704	–	25,020	2,393,724	2,036,321	–	246,031	2,282,352
Segment operating income (loss)	(582,399)	828,576	(19,859)	226,318	(3,006,813)	458,085	(230,984)	(2,779,712)
Share-based compensation	–	–	(34,124)	(34,124)	–	–	103,721	103,721
Amortization	–	–	231,901	231,901	–	–	274,489	274,489
Net finance expense	–	–	547,254	547,254	–	–	337,111	337,111
Gain on sublease on initial recognition	–	–	(12,876)	(12,876)	–	–	–	–
Loss on disposal of property, plant and equipment	–	–	24,662	24,662	–	–	–	–
Net income (loss)	$ (582,399)	$ 828,576	$ (776,676)	$ (530,499)	$ (3,006,813)	$ 458,085	$ (946,305)	$ (3,495,033)

12. Segment disclosures (continued)

(b) Entity-wide disclosures

All property, plant and equipment are located in Canada. All intangible assets are located in the United States.

(c) Sources of lease revenues

The Company leased 425,480 square feet of the total 625,000 available square feet to third parties. For the period ended November 30, 2021, the Company realized 100% of its lease revenue with two lessees:

- Tenant A's lease term is until September 30, 2022. Lease revenues from this tenant for the period ended November 30, 2021 amounted to $67,485.
- Tenant B's leases term ended October 31, 2022, if renewal clauses are not exercised. Lease revenues from this tenant for the period ended November 30, 2021 amounted to $748,186.

In addition, the Company leased 80,000 square feet at its Valleyfield Facility to a third party from June 2021 to September 2021. For the three-month period ended November 30, 2021, lease revenues amounted to $83,333.

Income is generated from customers domiciled in Canada.

(d) Source of cannabis revenues from sale of goods

	Three-month periods ended	
	November 30, 2021	November 30, 2020
Revenue from Canadian retailers	$ 6,664,730	$ –
Excise taxes	(1,538,987)	–
	5,125,743	–
Revenue from wholesale	290,238	679,125
	$ 5,415,981	$ 679,125

For the three-month period ended November 30, 2021, the Company has generated 90% of its cannabis revenues from one provincial distributor.

13. Related parties

(a) Key management personnel compensation

Key management personnel are the people who have the authority and responsibility for planning, directing and controlling the business activities of the Company and include all of its directors and chief executives. The compensations of key management personnel, including directors' fees, salaries and benefits for the three-month periods ended November 30, 2021 and 2020, were as follows:

	Three-month periods ended	
	November 30, 2021	November 30, 2020
Salaries and benefits	$ 107,500	$ 84,000
Shared-based compensation	26,508	16,184
Board of Directors' fees	17,500	11,250
	$ 151,508	$ 111,434

(b) Other transactions with related parties

Related parties include entities related by virtue of key management personnel and directors exercising significant influence or control over the entities' financial and operating policies.

The following provides the transaction amounts by nature with related parties:

	Three-month periods ended	
	November 30, 2021	November 30, 2020
Nature of transactions:		
Other expenses (income) (i)	$ (937)	$ 7,743
Interest on financing instruments (i)	323,664	236,155
	$ 322,727	$ 243,898

13. Related parties (continued)

(b) Other transactions with related parties (continued)

		November 30, 2021		August 31, 2021
Balances due from (due to) related parties is as follows:				
Accounts payable and accrued liabilities (i)	$	(177,518)	$	(434,609)
Accounts payable to key management personnel (ii)		(24,740)		(27,867)
Accounts payable to Board of Directors members		(30,378)		(15,189)
Convertible debentures(i)		(10,700,000)		(10,700,000)
Mortgage payable (i)		–		(6,550,000)

(i) A Director is a shareholder of an entity in which the Company entered into various transactions related to the Farnham Facility, the convertible debentures and the related mortgage payable.

(ii) Accounts payable relates to accrued salary and vacation for key management personnel.

Related party transactions have been recorded at the exchange amount, which is the amount agreed to and established by the related parties.

Along with the Valleyfield Facility acquisition in June 2021, a related party funded certain deposit requirements by a provincial service provider of approximately $5.7 million by the issuance of a letter of credit.

14. Financial instruments

Fair value measurements

The fair value of cash, accounts receivable, leases receivables and accounts payable and accrued liabilities approximates their carrying amounts due to the short-term maturity of those instruments.

The fair value of the long-term debt, convertible debentures and mortgages payable approximates their carrying amounts, as the interest rate approximates the current market rate.

15. Contingencies

In the normal course of business, the Company may be involved in various legal and regulatory proceedings. The Company believes that the resolution of these proceedings will not have a material favourable or unfavourable effect on its condensed interim consolidated statement of financial position or financial performance.

16. Cash flow information

Net change in non-cash working capital items:

	Three-month periods ended November 30, 2021	Three-month periods ended November 30, 2020
Accounts receivable	$ (759,723)	$ (185,083)
Sales tax receivable (payable)	219,040	92,132
Lease receivable	27,435	12,335
Biological assets	(1,516,262)	(1,313,530)
Inventory	407,152	138,557
Prepaid expenses and other assets	(113,621)	(127,502)
Accounts payable and accrued liabilities	260,727	(763,776)
Deferred lease revenue	284,072	–
Deferred grant income	130,121	(5,540)
	$ (1,061,059)	$ (2,152,407)

Supplemental information in the statement of cash flows:

	Three-month periods ended November 30, 2021	Three-month periods ended November 30, 2020
Variation of property, plant and equipment included in accounts payable and accrued liabilities	$ 217,669	$ 127,917

17. Subsequent events

Stock options

During December 2021, the Company granted 7,935,000 options to employees and members of the board of directors at an exercise price of $0.18 that vest in accordance with the terms of the employee share option plan (note 9).

Financing

Subsequent to quarter-end, the Company entered into an interest rate swap agreement with CIBC in order to provide the Company with fixed interest rate payments over the next five years reducing its exposure to expected volatility in interest rates. In addition, the Company was able to reduce its principal payments required on the $22 million mortgage.