Condensed Consolidated Interim Financial Statements of

POLLARD BANKNOTE LIMITED

(unaudited)

Six months ended June 30, 2019

These condensed consolidated interim financial statements have not been audited or reviewed by the Company's independent external auditors, KPMG LLP.

Pollard Banknote Limited
Condensed Consolidated Statements of Financial Position
(*In thousands of Canadian dollars*)
(unaudited)

		June 30, 2019		December 31, 2018*
Assets				
Current assets				
Cash	$	1,108	$	11,174
Restricted cash		7,331		10,158
Accounts receivable		53,629		34,675
Inventories (note 5)		43,029		45,353
Prepaid expenses and deposits		8,497		6,943
Income tax receivable		4,864		2,279
Total current assets		118,458		110,582
Non-current assets				
Property, plant and equipment (note 3)		89,321		71,606
Equity investment (note 6)		1,322		1,164
Goodwill		70,120		69,667
Intangible assets		53,575		50,086
Deferred income taxes		4,421		2,495
Total non-current assets		218,759		195,018
Total assets	$	337,217	$	305,600
Liabilities and Shareholders' Equity				
Current liabilities				
Accounts payable and accrued liabilities	$	37,714	$	43,058
Dividends payable		1,025		768
Income taxes payable		357		408
Current portion contract liabilities (note 7)		96		814
Current portion long-term debt (note 8)		–		40
Current portion lease liabilities (note 3)		4,469		–
Total current liabilities		43,661		45,088
Non-current liabilities				
Contract liabilities (note 7)		–		43
Long-term debt (note 8)		126,669		115,756
Other non-current liabilities		349		466
Pension liability (note 9)		30,190		20,357
Deferred income taxes		8,627		6,252
Lease liabilities (note 3)		12,586		–
Total non-current liabilities		178,421		142,874
Shareholders' equity				
Share capital (note 10)		108,642		108,605
Reserves		6,511		12,698
Deficit		(18)		(3,665)
Total shareholders' equity		115,135		117,638
Total liabilities and shareholders' equity	$	337,217	$	305,600

* Pollard has initially applied IFRS 16 *Leases* at January 1, 2019. Under the transition methods chosen, comparative information has not been restated. See note 3.

See accompanying notes to condensed consolidated interim financial statements.

Pollard Banknote Limited
Condensed Consolidated Statements of Income
(*In thousands of Canadian dollars, except for share amounts*)
(unaudited)

		Three months ended June 30, 2019		Three months ended June 30, 2018*		Six months ended June 30, 2019		Six months ended June 30, 2018*
Sales (note 7)	$	97,122	$	86,831	$	194,669	$	167,175
Cost of sales		75,559		66,315		150,174		127,292
Gross profit		21,563		20,516		44,495		39,883
Administration		10,553		7,374		19,204		15,398
Selling		4,064		3,419		7,587		6,181
Other expenses (note 11)		661		101		924		98
Income from operations		6,285		9,622		16,780		18,206
Finance costs (note 12)		1,628		2,363		3,115		4,709
Finance income (note 12)		(1,393)		–		(2,870)		–
Income before income taxes		6,050		7,259		16,535		13,497
Income taxes (note 13)								
Current (recovery)		(722)		401		1,080		3,518
Deferred		1,769		1,825		2,412		407
		1,047		2,226		3,492		3,925
Net income	$	5,003	$	5,033	$	13,043	$	9,572
Net income per share (basic) (note 14)	$	0.20	$	0.20	$	0.51	$	0.38
Net income per share (diluted) (note 14)	$	0.20	$	0.20	$	0.51	$	0.38

* Pollard has initially applied IFRS 16 *Leases* at January 1, 2019. Under the transition methods chosen, comparative information has not been restated. See note 3.

See accompanying notes to condensed consolidated interim financial statements.

Pollard Banknote Limited
Condensed Consolidated Statements of Comprehensive Income (Loss)
(*In thousands of Canadian dollars*)
(unaudited)

	Three months ended June 30, 2019	Three months ended June 30, 2018*	Six months ended June 30, 2019	Six months ended June 30, 2018*
Net income	$ 5,003	$ 5,033	$ 13,043	$ 9,572
Other comprehensive income (loss):				
Items that are or may be reclassified to profit and loss				
Foreign currency translation differences – foreign operations	(3,315)	3,103	(6,187)	5,818
Items that will never be reclassified to profit and loss				
Defined benefit plans remeasurements, net of income tax (note 9)	(3,052)	2,352	(7,364)	3,326
Other comprehensive income (loss)	(6,367)	5,455	(13,551)	9,144
Comprehensive income (loss)	$ (1,364)	$ 10,488	$ (508)	$ 18,716

* Pollard has initially applied IFRS 16 *Leases* at January 1, 2019. Under the transition methods chosen, comparative information has not been restated. See note 3.

See accompanying notes to condensed consolidated interim financial statements.

Pollard Banknote Limited
Condensed Consolidated Statements of Changes in Equity
(*In thousands of Canadian dollars*)
(unaudited)

For the six months ended June 30, 2019

		Share capital	Translation reserve	Deficit	Total equity
Balance at December 31, 2018	$	108,605	12,698	(3,665)	117,638
Net income		–	–	13,043	13,043
Other comprehensive loss					
Foreign currency translation differences – foreign operations		–	(6,187)	–	(6,187)
Defined benefit plans remeasurements, net of income tax (note 9)		–	–	(7,364)	(7,364)
Total other comprehensive loss	$	–	(6,187)	(7,364)	(13,551)
Total comprehensive income (loss)	$	–	(6,187)	5,679	(508)
Issue of common shares (note 10)	$	37	–	(18)	19
Share based compensation		–	–	37	37
Dividends (note 10)		–	–	(2,051)	(2,051)
Balance at June 30, 2019	$	108,642	6,511	(18)	115,135

For the six months ended June 30, 2018

		Share capital	Translation reserve	Deficit	Total equity
Balance at December 31, 2017	$	73,209	2,965	(18,605)	57,569
Adjustment on initial application of IFRS 15, net of income tax of $123		–	–	332	332
Adjusted balance at January 1, 2018	$	73,209	2,965	(18,273)	57,901
Net income		–	–	9,572	9,572
Other comprehensive income					
Foreign currency translation differences – foreign operations		–	5,818	–	5,818
Defined benefit plans remeasurements, net of income tax (note 9)		–	–	3,326	3,326
Total other comprehensive income	$	–	5,818	3,326	9,144
Total comprehensive income	$	–	5,818	12,898	18,716
Issue of common shares (note 10)	$	35,351	–	–	35,351
Share based compensation		–	–	68	68
Dividends		–	–	(1,537)	(1,537)
Balance at June 30, 2018	$	108,560	8,783	(6,844)	110,499

See accompanying notes to condensed consolidated interim financial statements.

Pollard Banknote Limited

Condensed Consolidated Statements of Cash Flows

(*In thousands of Canadian dollars*)

(unaudited)

	Six months ended June 30, 2019	Six months ended June 30, 2018*
Cash increase (decrease)		
Operating activities:		
Net income	$ 13,043	$ 9,572
Adjustments		
Income taxes	3,492	3,925
Amortization and depreciation	12,968	8,368
Interest expense	3,115	2,176
Unrealized foreign exchange (gain) loss	(3,061)	2,354
Loss on equity investment (note 6)	1,993	1,185
Pension expense	3,323	3,182
Contract liabilities	(42)	(584)
Interest paid	(2,724)	(2,258)
Income tax paid	(3,023)	(7,610)
Pension contribution	(3,378)	(2,388)
Change in non-cash operating working capital (note 15)	(22,390)	4,479
	3,316	22,401
Investing activities		
Additions to property, plant and equipment	(7,251)	(6,692)
Acquisition of International Gamco, Inc.	–	(21,558)
Acquisition of Fastrak Retail (UK) Limited (note 4)	(8,501)	–
Equity investments (note 6)	(2,201)	(1,095)
Additions to intangible assets	(4,030)	(2,875)
	(21,983)	(32,220)
Financing activities		
Proceeds from issue of share capital	19	35,351
Net proceeds from (repayments of) long-term debt	13,054	(3,377)
Repayments of subordinated debt	–	(16,734)
Change in other non-current liabilities	(90)	(203)
Lease principal payments	(2,479)	–
Deferred financing charges paid	(53)	(423)
Dividends paid	(1,794)	(1,475)
	8,657	13,139
Foreign exchange gain (loss) on cash held in foreign currency	(56)	105
Change in cash position	(10,066)	3,425
Cash position, beginning of period	11,174	5,603
Cash position, end of period	$ 1,108	$ 9,028

* Pollard has initially applied IFRS 16 *Leases* at January 1, 2019. Under the transition methods chosen, comparative information has not been restated. See note 3.

See accompanying notes to condensed consolidated interim financial statements.

1. Reporting entity:

Pollard Banknote Limited ("Pollard") was incorporated under the laws of Canada on March 26, 2010. The address of Pollard's registered office is 140 Otter Street, Winnipeg, Manitoba, Canada, R3T 0M8.

The condensed consolidated interim financial statements of Pollard as at and for the six months ended June 30, 2019, comprise Pollard, Pollard's subsidiaries and its interest in other entities. Pollard is primarily involved in the manufacture and sale of lottery and gaming products.

The controlling entity of Pollard is Pollard Equities Limited ("Equities"), a privately held company. Equities owns approximately 67.5% of Pollard's outstanding shares.

Pollard's consolidated financial statements as at and for the year ended December 31, 2018, are available at www.sedar.com.

The operations of Fastrak Retail (UK) Limited ("Fastrak"), acquired during the second quarter of 2019, are included in the condensed consolidated interim financial statements from May 1, 2019 (note 4).

The overall impact of seasonality does not have a significant impact on the operations of Pollard.

2. Basis of preparation:

(a) Statement of compliance:

These condensed consolidated interim financial statements have been prepared in accordance with International Accounting Standards ("IAS") 34 *Interim Financial Reporting* and do not include all of the information required for full annual consolidated financial statements.

On August 6, 2019, Pollard's Board of Directors approved these condensed consolidated interim financial statements.

(b) Use of estimates and judgments:

The preparation of condensed consolidated interim financial statements 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.

2. Basis of preparation (continued):

In preparing these condensed consolidated interim financial statements, the significant judgments made by management in applying Pollard's accounting policies and the key sources of estimation uncertainty were the same as those applied to the consolidated financial statements as at and for the year ended December 31, 2018.

3. Significant accounting policies:

Except for the accounting policies described below, these condensed consolidated interim financial statements follow the same significant accounting policies as described and used in Pollard's consolidated financial statements for the year ended December 31, 2018 and should be read in conjunction with these statements.

(a) Leases:

Pollard has adopted International Financial Reporting Standards ("IFRS") 16 *Leases* with a date of initial application of January 1, 2019. The new standard introduces a statement of financial position recognition and measurement model for lessees, eliminating the distinction between operating and finance leases. As a result, most leases are recognized on the statement of financial position. Certain exemptions apply for short-term leases and leases for low-value assets. Lessors continue to classify leases as operating and finance leases. IFRS 16 replaces IAS 17 *Leases* and the related interpretations.

Pollard has applied IFRS 16 using the modified retrospective approach, and therefore the comparative information has not been restated and continues to be reported under IAS 17.

Impact on the 2019 Interim Condensed Consolidated Financial Statements

On initial application, Pollard has elected to record right-of-use assets based on the corresponding lease liability. Right-of-use assets (included in property, plant and equipment) of $18,665, current portion of lease liabilities of $4,348 and long-term portion of lease liabilities of $14,317 were recorded as of January 1, 2019, with no net impact on the deficit. When measuring lease liabilities, Pollard discounted lease payments using its incremental borrowing rate of 4.0% at January 1, 2019.

For leases with a lease term ending within 12 months of the date of initial application and leases for low-value assets, Pollard has elected to apply the practical expedient which allows the recognition of the lease payments associated with these leases as an expense on a straight-line basis over the lease term. The discounted value of the leases classified under the recognition exemption as at January 1, 2019 was $343.

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

3. Significant accounting policies (continued):

The following tables summarize the impact of adopting IFRS 16 on Pollard's condensed consolidated statement of financial position as at June 30, 2019 and its condensed consolidated statement of income for the six months ended June 30, 2019.

Impact on Pollard's condensed consolidated statement of financial position as at June 30, 2019:

	Amount without IFRS 16	IFRS 16 Adjustment	As Reported
Property, plant and equipment	$ 72,532	$ 16,789	$ 89,321
Current portion of lease liabilities	–	4,469	4,469
Lease liabilities	–	12,586	12,586
Retained earnings (deficit)	248	(266)	(18)

Impact on Pollard's condensed consolidated statement of income for the six months ended June 30, 2019:

	Amount without IFRS 16	IFRS 16 Adjustment	As Reported
Cost of sales	$ 150,247	$ (73)	$ 150,174
Finance costs	2,776	339	3,115

The following table presents a continuity schedule from the date of adoption of Pollard's right-of-use assets:

Opening balance, January 1, 2019	$ 18,665
Acquisition	402
Additions	–
Depreciation	(2,278)
Closing balance, June 30, 2019	$ 16,789

3. Significant accounting policies (continued):

Accounting policies

Pollard has updated its accounting policies upon adoption of IFRS 16 on January 1, 2019.

At inception of a contract, Pollard assesses whether a contract is, or contains, a lease. A contract is, or contains, a lease if the contract conveys the right to control the use of an identified asset for a period of time in exchange for consideration.

Pollard recognizes a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, less any lease incentives received. The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the earlier of the end of the useful life of the right-of-use asset or the end of the lease term. The estimated useful lives of right-of-use assets are determined on the same basis as those of property, plant and equipment. The lease liability is subsequently measured at cost less any accumulated depreciation and impairment losses.

The lease liability is initially measured at the present value of the lease payments that are not paid at the commencement date, discounted using the interest rate implicit in the lease or, if that rate cannot be readily determined, Pollard's incremental borrowing rate. Generally, Pollard uses its incremental borrowing rate as the discount rate.

The lease liability is measured at amortized cost using the effective interest method. It is remeasured when there is a change in future lease payments arising from a change in an index or rate, a change in Pollard's estimate of the amount expected to be payable under a residual value guarantee, or as appropriate, changes in the assessment of whether a purchase or extension option is reasonably certain to be exercised or a termination option is reasonably certain not to be exercised.

In comparative periods, operating leases were not recognized in Pollard's consolidated statement of financial position. Payments made were recognized in the statement of income on a straight-line basis over the term of the lease, while any lease incentive received was recognized as a reduction of the total lease expense over the term of the lease.

Pollard presents right-of-use assets in "property, plant and equipment" on the statement of financial position.

Pollard's leases are for offices, manufacturing facilities, production equipment and office equipment.

3. Significant accounting policies (continued):

Pollard has elected not to recognize right-of-use assets and lease liabilities for short-term leases that have a lease term of 12 months or less and leases of low-value assets. Pollard recognizes the lease payments associated with these leases as an expense on a straight-line basis over the lease term.

The adoption of IFRS 16 did not impact Pollard's accounting policies for lessors.

(b) Uncertainty over income tax treatments:

In June 2017, the International Financial Reporting Interpretations Committee ("IFRIC") issued Interpretation 23 *Uncertainty over Income Tax Treatments*, which aims to reduce diversity in how companies recognize and measure a tax liability or tax asset when there is uncertainty over income tax treatments. The Interpretation was implemented with retrospective application, effective January 1, 2019 and had no impact on the condensed consolidated interim financial statements.

(c) Investments in associates and joint ventures:

In October 2017, the International Accounting Standards Board ("IASB") issued amendments to IAS 28 *Investments in Associates and Joint Ventures.* The amendments clarify that long-term interests in associates and joint ventures, to which the equity method is not applied, are in the scope of both IFRS 9 *Financial Instruments*, including impairment testing, and IAS 28 in terms of the application of IFRS 9 loss absorption and the impairment requirements of IAS 28. The amendments were implemented with retrospective application, effective January 1, 2019 and had no impact on the condensed consolidated interim financial statements.

(d) Employee benefits:

In February 2018, amendments to IAS 19 *Employee Benefits* were issued to specify how an entity determines pension expenses when changes to a defined benefit plan occur. When a change to a plan takes place, including an amendment, curtailment or settlement, IAS 19 requires an entity to remeasure its employee benefit plan liability or asset. The amendments require an entity to use the updated assumptions from this remeasurement to determine current service cost and the net finance cost for the remainder of the reporting period after the change to the plan. The amendments were implemented with prospective application, effective January 1, 2019 and had no impact on the condensed consolidated interim financial statements.

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

4. Acquisitions:

(a) Schafer Systems Inc.:

On October 31, 2018, Pollard Systems Inc., a wholly-owned indirect subsidiary of Pollard, acquired substantially all of the operating assets and business of Schafer Systems Inc. ("Schafer"), the leading global provider of lottery ticket dispensers and play stations. Pollard Systems Inc. was renamed Schafer Systems (2018) Inc. upon completion of the transaction. The purchase price was funded by proceeds from Pollard's credit facility and cash on hand. The acquisition has been accounted for using the acquisition method. The fair values of the identifiable assets and liabilities have been based on management's best estimates and valuation techniques as at October 31, 2018, the acquisition date.

Total consideration transferred	$	30,447
Net tangible assets acquired:		
Accounts receivable	$	1,042
Inventories		2,566
Property, plant and equipment		5,409
Accounts payable and accrued liabilities		(374)
Net tangible assets acquired	$	8,643
Customer relationships	$	11,426
Brand		1,013
Patents		132
Identifiable intangible assets acquired	$	12,571
Goodwill acquired	$	9,233

The goodwill acquired is largely attributable to the assembled workforce, market share and the expected synergies and cost savings after integration of the combined businesses. This goodwill is expected to be deductible for tax purposes.

The fair values of identifiable assets and liabilities acquired are preliminary and are subject to change if new information becomes available.

(b) Fastrak Retail (UK) Limited:

On May 1, 2019, Pollard acquired 100% of the common shares of Fastrak, a leading provider of lottery ticket dispensers, lottery play points and other retail merchandising products based in the United Kingdom. The purchase price was funded by proceeds from Pollard's credit facility and cash on hand. The acquisition has been accounted for using the acquisition method. The fair values of the identifiable assets and liabilities have been based on management's best estimates and valuation techniques as at May 1, 2019, the acquisition date.

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

4. Acquisitions (continued):

Cash paid, net of cash acquired of $1,213	$	7,997
Contingent consideration		504
Total consideration transferred	$	8,501
Additional net tangible assets acquired:		
Accounts receivable	$	2,418
Inventories		885
Prepaid expenses and deposits		177
Property, plant and equipment		1,646
Income taxes receivable		128
Accounts payable and accrued liabilities		(2,121)
Lease liabilities		(402)
Deferred income tax liability		(951)
Net tangible assets acquired (excluding cash)	$	1,780
Customer relationships	$	3,770
Brand		457
Patents		342
Identifiable intangible assets acquired	$	4,569
Goodwill acquired	$	2,152

The goodwill acquired is largely attributable to the assembled workforce, market share and the expected synergies and cost savings after integration of Fastrak with Pollard. This goodwill is not expected to be deductible for tax purposes. The fair values of identifiable assets and liabilities acquired are preliminary and are subject to change if new information becomes available.

Acquisition costs related to the Fastrak purchase in the three months and six months ended June 30, 2019, were $434. These costs were included in administration expenses.

During the period between May 1, 2019 and June 30, 2019, Fastrak generated revenues of approximately $5,853 and net income of $1,239, after depreciation and amortization of the fair values of identifiable assets acquired, which have been recorded in the consolidated financial statements. Fastrak's revenues and net income during this period significantly exceeded historical levels due to the fulfillment of a one-time, non-recurring, customer contract.

If Fastrak had been acquired on January 1, 2019, incremental revenue of $3,203 and net loss of $441, after depreciation and amortization of the fair values of identifiable assets acquired, would have been recognized in the six months ended June 30, 2019.

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

4. Acquisitions (continued):

Contingent consideration, based on achievement of certain revenue and EBITDA targets, may be paid to the vendor. The revenue earn-out target is based on achievement of certain sales volumes to one customer during the period 2019 through 2023. The maximum potential payment under the revenue-based earn-out is £2,000. Pollard believes the likelihood of payment is low, and as such, has not accrued a liability for the revenue earn-out.

The EBITDA earn-out is based on Fastrak's achievement of certain EBITDA targets during the period 2019 through 2021. The potential payment under the EBTIDA earn-out is unlimited. Pollard has accrued $504 relating to this portion of the contingent consideration, included within accounts payable and accrued liabilities, which represents the present value of the liability. The accrual is based on management's best estimates and valuation techniques as at May 1, 2019, the acquisition date.

5. Inventories:

		June 30, 2019		December 31, 2018
Raw materials	$	17,141	$	18,537
Work-in-process		3,569		2,861
Finished goods		22,319		23,955
	$	43,029	$	45,353

During the second quarter of 2019, Pollard recorded inventory write-downs of $268, representing an increase in the obsolescence reserves, and inventory write-downs of $23 due to changes in foreign exchange rates. During the six months ended June 30, 2019, Pollard recorded inventory write-downs of $416 representing an increase in the obsolescence reserves, and inventory write-downs of $63 due to changes in foreign exchange rates.

During the second quarter of 2018, Pollard recorded inventory write-downs of $90, representing an increase in the obsolescence reserves, and an increase in write-downs of $5 due to changes in foreign exchange rates. During the six months ended June 30, 2018, Pollard recorded inventory write-downs of $227 representing an increase in the obsolescence reserves, and a reversal of previous write-downs of $22 due to changes in foreign exchange rates.

The cost of sales reflects the costs of inventory including direct material, direct labour and manufacturing overheads.

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

6. Equity investment:

Interest in joint venture	Six months ended June 30, 2019	Six months ended June 30, 2018
Balance, beginning of period	$ 1,164	$ 877
Investment	2,201	1,095
Equity loss	(1,993)	(1,185)
Effects of movements in exchange rates	(50)	47
Balance, end of period	$ 1,322	$ 834

Pollard has entered into an agreement with NeoGames US, LLP for the establishment of NeoPollard Interactive LLC. The entity was established to provide iLottery services in the United States and Canada, excluding the State of Michigan.

Pollard and Neogames S.à r.l. operate the iLottery operation for the Michigan Lottery under a separate joint operating agreement. Pollard recognizes its interest in the joint operation by including its assets, including its share of any assets held jointly, its liabilities, including its share of any liabilities incurred jointly and its share of revenue and expenses.

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

7. Revenue and contract balances:

In the following tables, revenue from contracts with customers is disaggregated by geographical segment and product line:

Revenue – geographical segment	Six months ended June 30, 2019		
	Lotteries and charitable gaming	Diamond Game	Total
Canada	$ 34,535	$ 5,279	$ 39,814
United States	109,164	8,937	118,101
International	36,754	–	36,754
	$ 180,453	$ 14,216	$ 194,669

Revenue – geographical segment	Six months ended June 30, 2018		
	Lotteries and charitable gaming	Diamond Game	Total
Canada	$ 37,551	$ 5,708	$ 43,259
United States	84,048	7,359	91,407
International	32,509	–	32,509
	$ 154,108	$ 13,067	$ 167,175

Revenue – product lines	Six months ended June 30, 2019		
	Lotteries and charitable gaming	Diamond Game	Total
Lottery	$ 149,225	$ –	$ 149,225
Charitable	31,228	–	31,228
Gaming systems	–	14,216	14,216
	$ 180,453	$ 14,216	$ 194,669

Revenue – product lines	Six months ended June 30, 2018		
	Lotteries and charitable gaming	Diamond Game	Total
Lottery	$ 128,706	$ –	$ 128,706
Charitable	25,402	–	25,402
Gaming systems	–	13,067	13,067
	$ 154,108	$ 13,067	$ 167,175

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

7. Revenue and contract balances (continued):

The following tables provide information about receivables, contract assets, and contract liabilities from contracts with customers:

Contract balances		June 30, 2019		December 31, 2018
Trade receivables, which are included in accounts receivable	$	48,113	$	27,061
Contract assets, which are included in accounts receivable		3,885		3,128
Contract liabilities		96		857

Contract liabilities		Six months ended June 30, 2019		Six months ended June 30, 2018
Balance, beginning of period	$	857	$	1,491
Increases due to cash received		–		951
Revenue recognized during the period		(761)		(441)
Balance, end of period		96		2,001
Less current portion		(96)		(1,766)
	$	–	$	235

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

8. Long-term debt:

		June 30, 2019		December 31, 2018
Credit facility, interest of 4.0% to 4.4%, payable monthly, maturing 2021	$	126,952	$	116,177
Equipment debt		–		4
Equipment lease		–		36
Deferred financing charges, net of amortization		(283)		(421)
		126,669		115,796
Less current portion		–		(40)
	$	126,669	$	115,756

Credit facility

Effective June 22, 2018, Pollard renewed its credit facility. The credit facility provides loans of up to $160,000 for its Canadian operations and US$12,000 for its U.S. subsidiaries. The credit facility also includes an accordion feature which can increase the facility by $25,000. The borrowings for the Canadian operations can be denominated in Canadian or U.S. dollars, to a maximum of $160,000 Canadian equivalent. Borrowings under the credit facility bear interest at fixed and floating rates based on Canadian and U.S. prime bank rates, banker's acceptances or LIBOR. At June 30, 2019, the outstanding letters of guarantee drawn under the credit facility were $2,386 (December 2018 – $1,337).

Included in the total credit facility balance is a U.S. dollar denominated balance of US$40,400 (December 2018 – US$43,600).

Under the terms and conditions of the credit facility agreement Pollard is required to maintain certain financial covenants including debt to income before interest, income taxes, amortization and depreciation ("Adjusted EBITDA") ratios and certain debt service coverage ratios. As at June 30, 2019, Pollard is in compliance with all financial covenants.

As of June 30, 2019, Pollard had unused credit facility available of $46,381 (December 2018 – $58,860).

Pollard's credit facility is secured by a first security interest in all of the present and after acquired property of Pollard. Under the terms of the agreement the facility is committed for a three-year period, renewable June 22, 2021. Principal payments are not required until maturity. The facility can be prepaid without penalties.

9. Pension liability:

During the three month period ended June 30, 2019, Pollard recorded a remeasurement loss of $3,052 (net of $1,080 of income tax) on its defined pension plans. The remeasurement loss resulted from a decrease in the discount rate, which was partially offset by a gain arising on plan asset investments.

During the three month period ended June 30, 2018, Pollard recorded a remeasurement gain of $2,352 (net of $850 of income tax) on its defined pension plans. The remeasurement gain resulted from an increase in the discount rate and a gain arising on plan asset investments.

During the six month period ended June 30, 2019, Pollard recorded a remeasurement loss of $7,364 (net of $2,652 of income tax) on its defined pension plans. The remeasurement loss resulted from a decrease in the discount rate, which was partially offset by a gain arising on plan asset investments.

During the six month period ended June 30, 2018, Pollard recorded a remeasurement gain of $3,326 (net of $1,181 of income tax) on its defined pension plans. The remeasurement gain resulted from an increase in the discount rate and a gain arising on plan asset investments.

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

10. Share capital:

	Shares		Amount $
Authorized			
Unlimited common shares			
Unlimited preferred shares			
Issued			
Balance at December 31, 2017	23,543,158	$	73,209
Issuance of common shares	2,070,000		35,351
Stock option exercise	12,500		45
Balance at December 31, 2018	25,625,658	$	108,605
Stock option exercise	10,000		37
Balance at June 30, 2019	25,635,658	$	108,642

Stock option exercise

On March 19, 2019, 5,000 common shares were issued in conjunction with the exercise of stock options. On May 24, 2019, 5,000 common shares were issued in conjunction with the exercise of stock options.

Dividends

Dividends are paid on the common shares within 15 days of the end of each quarter and are fully discretionary, as determined by the Board of Directors of Pollard.

On May 8, 2019, a dividend of $0.04 per share was declared, payable on July 15, 2019, to the shareholders of record on June 30, 2019.

11. Other (income) expenses:

		Three months ended June 30, 2019		Three months ended June 30, 2018		Six months ended June 30, 2019		Six months ended June 30, 2018
Loss on equity investment (note 6)	$	1,073	$	647	$	1,993	$	1,185
EBITDA support agreement		(500)		(500)		(1,000)		(1,000)
Other (income) expense		88		(46)		(69)		(87)
	$	661	$	101	$	924	$	98

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

11. Other (income) expenses (continued):

EBITDA support agreement

One of Pollard's subsidiaries, Diamond Game, previously entered into an EBITDA support agreement with Amaya Inc. pursuant to which, subject to certain terms and conditions, Amaya Inc. will pay Diamond Game each year for up to five years from July 1, 2015, an amount equal to the shortfall, if any, between (i) Diamond Game's EBITDA directly or indirectly derived from the deployment of Diamond Game's products at certain entertainment centers or in connection with Diamond Game's relationship with a certain customer, and (ii) $2,000. This agreement remains in effect after the acquisition of Diamond Game's common shares by Pollard.

12. Finance costs and finance income:

Finance costs	Three months ended June 30, 2019	Three months ended June 30, 2018	Six months ended June 30, 2019	Six months ended June 30, 2018
Foreign exchange loss	$ –	$ 1,354	$ –	$ 2,533
Interest	1,628	1,009	3,115	2,176
	$ 1,628	$ 2,363	$ 3,115	$ 4,709

Finance income	Three months ended June 30, 2019	Three months ended June 30, 2018	Six months ended June 30, 2019	Six months ended June 30, 2018
Foreign exchange gain	$ 1,393	$ –	$ 2,870	$ –
	$ 1,393	$ –	$ 2,870	$ –

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

13. Income taxes:

Reconciliation of effective tax rate		Three months ended June 30, 2019		Three months ended June 30, 2018
Net income for the period		$ 5,003		$ 5,033
Total income taxes		1,047		2,226
Income before income taxes		$ 6,050		$ 7,259
Income tax using Pollard's domestic tax rate	27.0%	$ 1,634	27.0%	$ 1,960
Effect of tax rates in foreign jurisdictions	(5.6%)	(340)	(0.6%)	(47)
Non-deductible amounts	0.0%	–	1.2%	86
Effect of non-taxable items related to foreign exchange	(4.1%)	(247)	3.1%	227
	17.3%	$ 1,047	30.7%	$ 2,226

Reconciliation of effective tax rate		Six months ended June 30, 2019		Six months ended June 30, 2018
Net income for the period		$ 13,043		$ 9,572
Total income taxes		3,492		3,925
Income before income taxes		$ 16,535		$ 13,497
Income tax using Pollard's domestic tax rate	27.0%	$ 4,464	27.0%	$ 3,644
Effect of tax rates in foreign jurisdictions	(3.3%)	(539)	(0.8%)	(113)
Non-deductible amounts	0.0%	–	0.6%	86
Effect of non-taxable items related to foreign exchange	(2.6%)	(433)	2.3%	308
	21.1%	$ 3,492	29.1%	$ 3,925

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

14. Net income per share:

	Three months ended June 30, 2019	Three months ended June 30, 2018
Net income attributable to shareholders for basic and diluted net income per share	$ 5,003	$ 5,033
Weighted average number of shares (basic)	25,632,714	25,613,158
Weighted average impact of share options on issue	230,445	250,000
Weighted average number of shares (diluted)	25,863,159	25,863,158
Net income per share (basic)	$ 0.20	$ 0.20
Net income per share (diluted)	$ 0.20	$ 0.20

	Six months ended June 30, 2019	Six months ended June 30, 2018
Net income attributable to shareholders for basic and diluted net income per share	$ 13,043	$ 9,572
Weighted average number of shares (basic)	25,629,547	25,258,628
Weighted average impact of share options on issue	233,611	250,000
Weighted average number of shares (diluted)	25,863,158	25,508,628
Net income per share (basic)	$ 0.51	$ 0.38
Net income per share (diluted)	$ 0.51	$ 0.38

On February 1, 2018, Pollard announced that it had entered into an agreement with a syndicate of underwriters led by Canaccord Genuity Corp. (together, the "Underwriters") to purchase on a bought deal basis 1,800,000 common shares of Pollard at a price of $18.45 per share. Pollard also granted the Underwriters an over-allotment option exercisable at any time up to 30 days following the closing of the offering, to purchase up to an additional 270,000 common shares. On February 21, 2018, Pollard issued 2,070,000 common shares.

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

15. Supplementary cash flow information:

	Six months ended June 30, 2019	Six months ended June 30, 2018
Change in non-cash operating working capital:		
Accounts receivable	$ (17,840)	$ 8,227
Inventories	2,078	2,291
Prepaid expenses and deposits	(1,656)	861
Income taxes payable	(572)	(238)
Accounts payable and accrued liabilities	(3,698)	(7,665)
Contract liabilities	(702)	1,003
	$ (22,390)	$ 4,479

16. Related party transactions:

Pollard Equities Limited and affiliates

During the quarter ended June 30, 2019, Pollard paid property rent of $809 (2018 - $795) and $118 (2018 - $95) in plane charter costs to an affiliate of Pollard Equities Limited. During the six months ended June 30, 2019, Pollard paid property rent of $1,618 (2018 - $1,588) and $236 (2018 - $190) in plane charter costs to an affiliate of Equities. In addition, during the quarter, Pollard paid Equities $nil (2018 – $158) interest on Pollard's subordinated debt and $nil (2018 – $421) for the six months ended June 30, 2019.

During the quarter, Equities paid Pollard $18 (2018 - $18) for accounting and administration fees and $36 (2018 - $36) during the six months ended June 30, 2019.

At June 30, 2019, included in accounts receivable is an amount owing from Equities and its affiliates for expenses and other items of $18. At December 31, 2018, included in accounts payable and accrued liabilities is an amount owing to Equities and its affiliates for rent, expenses and other items of $560.

Neogames S.à r.l. and affiliates

Pollard reimbursed operating costs and paid software royalties of $1,451 (2018 - $766) during the quarter ended June 30, 2019 and $2,604 (2018 - $1,561) during the six months ended June 30, 2019 to its iLottery joint venture partner, which are recorded in cost of sales.

At June 30, 2019, included in accounts payable and accrued liabilities is a net amount owing to Pollard's iLottery partner of $1,274 (December 31, 2018 – $940) for reimbursement of operating costs and capital expenditures, and its share of operating results.

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

16. Related party transactions (continued):

Key management personnel

Key management personnel are those having authority and responsibility for planning, directing and controlling the activities of the company. The Board of Directors and the Executive Committee are considered key management personnel.

Key management personnel compensation comprised:

	Three months ended June 30, 2019	Three months ended June 30, 2018	Six months ended June 30, 2019	Six months ended June 30, 2018
Wages, salaries and benefits	$ 697	$ 695	$ 1,389	$ 1,382
Profit share	2	6	6	11
Expenses related to defined benefit plans	154	152	308	304
	$ 853	$ 853	$ 1,703	$ 1,697

At June 30, 2019, the Directors and Named Executive Officers of Pollard, as a group, beneficially owned or exercised control or direction over 17,443,108 common shares of Pollard.

17. Segmented information:

Pollard has two reportable segments: Lotteries and charitable gaming, and Diamond Game, which are Pollard's strategic business units. The strategic business units offer different products and services, and are managed separately. For each of the strategic business units, Pollard's Co–CEO's review internal management reports on a monthly basis.

The Lotteries and charitable gaming segment derives its revenues from the manufacture of instant tickets and related products. The Diamond Game segment derives its revenues from the development of game systems.

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

17. Segmented information (continued):

Segment information about profits and assets is as follows:

	Three months ended June 30, 2019		
	Lotteries and charitable gaming	Diamond Game	Total
Revenues from external customers	$ 89,733	$ 7,389	$ 97,122
Operating costs and expenses	85,038	6,034	91,072
Earnings before income taxes	4,695	1,355	6,050
Total assets	277,647	59,570	337,217

	Three months ended June 30, 2018		
	Lotteries and charitable gaming	Diamond Game	Total
Revenues from external customers	$ 80,071	$ 6,760	$ 86,831
Operating costs and expenses	74,108	5,464	79,572
Earnings before income taxes	5,963	1,296	7,259
Total assets	193,976	58,679	252,655

	Six months ended June 30, 2019		
	Lotteries and charitable gaming	Diamond Game	Total
Revenues from external customers	$ 180,453	$ 14,216	$ 194,669
Operating costs and expenses	166,246	11,888	178,134
Earnings before income taxes	14,207	2,328	16,535
Total assets	277,647	59,570	337,217

	Six months ended June 30, 2018		
	Lotteries and charitable gaming	Diamond Game	Total
Revenues from external customers	$ 154,109	$ 13,066	$ 167,175
Operating costs and expenses	142,289	11,389	153,678
Earnings before income taxes	11,820	1,677	13,497
Total assets	193,976	58,679	252,655

(In thousands of Canadian dollars, except where otherwise noted and for share amounts)

18. Financial risk management:

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

Credit risk
Liquidity risk
Currency risk
Interest rate risk

Pollard's risk management policies are established to identify and analyze the risks, to set appropriate risk limits and controls and to monitor risks and adherence to limits. The Audit Committee oversees how management monitors compliance with Pollard's risk management policies and procedures. The Audit Committee is assisted in its oversight role by Internal Audit, who undertakes regular reviews of risk management controls and utilizes the annual risk assessment process as the basis for the annual internal audit plan.

Credit risk

The following table outlines the details of the aging of Pollard's receivables and the related allowance for losses:

		June 30, 2019		December 31, 2018
Current	$	49,462	$	30,929
Past due for 1 to 60 days		3,120		2,647
Past due for more than 60 days		1,243		1,289
Less: Allowance for losses		(196)		(190)
	$	53,629	$	34,675

Liquidity risk

Liquidity risk is the risk that Pollard will not be able to meet its financial obligations as they fall due. Pollard's approach is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due. The 2019 requirements for capital expenditures, working capital and dividends are expected to be financed from cash flow provided by operating activities and the unused credit facility. Pollard enters into contractual obligations in the normal course of business operations.

18. Financial risk management (continued):

Currency risk

Pollard sells a significant portion of its products and services to customers in the United States and to some international customers where sales are denominated in U.S. dollars. In addition, a significant portion of its cost inputs are denominated in U.S. dollars. Pollard also generates revenue in currencies other than the Canadian and U.S. dollar, primarily in Euros.

A 50 basis point strengthening/weakening in the foreign exchange rate between the Canadian and U.S. dollar would decrease/increase the income before income taxes due to changes in operating cashflow by approximately $8 for the second quarter of 2019 (2018 - $1) and approximately $30 for the six months ended June 30, 2019 (2018 - $8). A 50 basis point strengthening/weakening in the foreign exchange rate between the Canadian and Euro would decrease/increase the income before income taxes due to changes in operating cashflow by approximately $22 for the second quarter of 2019 (2018 - $16) and approximately $37 for the six months ended June 30, 2019 (2018 - $34).

In addition, translation differences arise when foreign currency monetary assets and liabilities are translated at foreign exchange rates that change over time. At June 30, 2019, the amount of financial liabilities denominated in U.S. dollars exceeds the amount of financial assets denominated in U.S. dollars by approximately $37,852 (December 31, 2018 - $36,147). A 50 basis point weakening/strengthening in the value of the Canadian dollar relative to the U.S. dollar would result in a decrease/increase in income before taxes of approximately $189 for the three and six months ended June 30, 2019 (2018 - $66).

Pollard utilizes a number of strategies to mitigate its exposure to currency risk. Five manufacturing facilities are located in the U.S. and a significant amount of cost inputs for all production facilities are denominated in U.S. dollars, offsetting a large portion of the U.S. dollar revenue in a natural hedge.

Pollard also uses financial hedges, including foreign currency contracts, to help manage foreign currency risk. At June 30, 2019, Pollard had no outstanding foreign currency contracts.

Interest rate risk

Pollard is exposed to interest rate risk relating to its fixed and floating rate instruments. Fluctuation in interest rates will have an effect on the valuation and repayment of these instruments.

A 50 basis point decrease/increase in interest rates would result in an increase/decrease in income before income taxes of approximately $159 for the three months ended June 30, 2019 (2018 - $122) and approximately $296 for the six months ended June 30, 2019 (2018 - $207).