POLLARD banknote limited

ANNUAL REPORT

2018

CONTENTS

LETTER TO SHAREHOLDERS

Enclosed please find our 2018 Annual Report. 2018 was a successful year on a number of fronts, including achieving record revenue of more than $331 million, generating almost $30 million in income from operations and over $39 million in cash flow from operating activities. We are very pleased with our accomplishments during 2018, both financially and operationally. Our vision is to be the partner of choice in the lottery and charitable gaming market by offering retail and digital games and solutions that attract and engage players and we believe this is being achieved through the development of industry leading innovative products and services.

Sales of our main product, instant tickets, were relatively flat compared to 2017 primarily due to the temporary reduction of order volumes in the fourth quarter. Notwithstanding this short-term dip, the long-term outlook in consumer demand for instant tickets remains very strong and provides the business foundation for future growth. We continue to develop our ancillary product portfolio to expand our revenue and earnings including areas such as loyalty clubs (PlayOn™), in-lane retail distribution (ScanActiv™), Lottery Management Systems (SureTrack®) and digital apps among others. Our proprietary print products such as Scratch FX® and ClearPlay™ are industry leaders and help position Pollard Banknote as a true innovative trailblazer.

Our acquisition strategy was very successful during this past year with the completion of two transactions: International Gamco, Inc. (“Gamco”) and the business of Schafer Systems, Inc (“Schafer”). These acquisitions meet our benchmarks of being financially accretive as well as strategically important in expanding our expertise and breadth of product offering.

Sales

2018 revenue reached a new record at over $331 million, an increase of $46 million or 16%, the second year in a row of 16% top line growth. Sales of instant tickets were relatively stable compared to the record volumes and average selling prices achieved in 2017, with higher revenue in the first three quarters of the year primarily being offset by lower order volumes in the fourth quarter. Our lower volumes in the fourth quarter were due to the timing of certain customer orders and does not reflect any systemic change in our underlying contracts or retail consumer demand. Sales of our key proprietary print products continue to play a critical role in our strategic sales objectives and ancillary sales increased revenue slightly from 2017, with higher digital revenue including iLottery being partially offset by a reduction in licensed games revenue.

The bulk of our increased revenue was due to our acquisitions, with the additions of Schafer (November 1) and Gamco (February 1) and a full 12 months of revenue from Diamond Game (versus five months in 2017) adding approximately $44 million in revenue to our top line. The Canadian dollar on average was steady in value relative to the U.S. dollar compared to 2017.

We received a number of contract renewals and extensions throughout 2018, retaining all of our instant ticket customers during the year. Key contract extensions include a ten-year extension with the British Columbia Lottery Corporation (one of our very first instant ticket customers), a four-year extension with the Michigan State Lottery and other important renewals with such lotteries as Texas, Iowa and many others. New lottery contract wins include the instant ticket contract to provide exclusive products for the lottery of Norway. After factoring in existing renewal options, the weighted average life of our existing instant ticket contract portfolio is in excess of 4 years, providing the foundation for solid recurring revenue and organic growth.

Our iLottery operations continued to produce very positive results, driven by our industry leading Michigan operation. At the same time as growing this digital distribution channel, Michigan's growth in sales of instant tickets at traditional retail outlets is outpacing other lotteries in the Untied States, highlighting the importance of iLottery to grow the player base and benefit overall lottery sales. In addition to Michigan, our iLottery joint venture is now operating in Virginia, won a new contract in 2018 for the New Hampshire iLottery and was awarded the contract to operate the North Carolina iLottery, which we expect to go live in late 2019.

Our charitable games revenue was significantly higher in 2018, exceeding $55 million, reflecting our acquisition of Gamco, but also as a result of moderate growth in the overall industry. Key jurisdictions have shown growth at the retail level and with the addition of the valuable Gamco branded pull-tab tickets, we are in a unique position to develop a stronger presence in this market.

During 2018 North Dakota opened its market for eGaming pull-tab machines which provided an opportunity for our Diamond Game and Gamco operations to provide an effective solution. Utilizing the Gamco Oasis branded machine, our teams worked together to develop and successfully deploy approximately 250 machines into this market, illustrating the revenue synergies available to our organization. As this new market continues to grow, we look forward to the placement of more machines and bringing the market exciting new games.

Operations

Our gross margin increased by $10.0 million or 15.2% primarily due to the impact of our acquisitions of Gamco and Schafer and the full year effect of Diamond Game. Our instant ticket gross margin was relatively flat compared to 2017 due to the temporary shortfall in orders in the fourth quarter. Our gross margin percentage declined slightly year over year, 22.8% compared to 23%, due primarily to the impact of the lower orders in the fourth quarter.

Administration expenses increased $3.5 million, or approximately 12%, partially due to the inclusion of a full year of Diamond Game operations and our acquisitions of Gamco and Schafer. In addition, increased personnel costs were incurred relating to our growth strategies and product development of our digital innovations and increased investment in our technology infrastructure. These increases were partially offset by a decline in acquisition costs and lower severance costs associated with our acquisitions relative to 2017. Selling expenses increased $3.8 million over 2017 primarily due to the inclusion of a full year of Diamond Game, our acquisitions of Gamco and Schafer and ongoing investments in additional personnel to support our expanded portfolio of products and services offered to the lottery market.

During 2018 we recommissioned our original press line in Ypsilanti to provide extra capacity and scheduling flexibility for our instant ticket product line. We are currently adding additional equipment to this press line to increase its efficiencies and capacity, which will provide us with more than sufficient capacity to produce expected volumes while ensuring additional room for growth.

A number of important capital projects were undertaken during the year in addition to the press recommissioning including the expansion of our in-house plate making operations, additional investments in finishing equipment including folding and packaging equipment and upgrades in a number of technical infrastructure areas. These investments will improve the efficiencies of our operations while at the same time continuing our cost reduction initiatives.

Acquisitions

Acquisitions are a key objective in our strategic plan by ensuring the quality and breadth of our products and services are industry leading. Over the last 18 months we have successfully made three important additions to the Pollard Banknote family.

Diamond Game completed its first full year within Pollard Banknote and continues to exceed our expectations. In addition to developing the North Dakota market, Diamond Game is actively working on a number of new jurisdictions for their electronic gaming machines and to expand the machine count in existing market places. We expect additional machines to be installed during the year in pilot programs which is often the first step in further expansion.

Our Gamco purchase on February 1, 2018, has proceeded very well and the integration of the business with our existing American Games operation has gone smoothly. The market reception of the combined businesses has been very positive and we believe the portfolio of multiple branded pull-tabs provides us a unique opportunity for future revenue synergies.

On November 1, 2018, we completed the acquisition of the Schafer Systems operating business. Schafer is the market leader in instant ticket lottery dispensing and related merchandising products and has significant relationships with the leading lotteries in the United States. While still early, we are very pleased with the management team and employees of Schafer and see great potential to combine Schafer's merchandising expertise with our unique portfolio of innovative instant tickets to provide unparalleled growth opportunities for lotteries. Further expansion into Canada and internationally are other areas of potential growth for the Schafer business.

We continue to actively search for additional opportunities to acquire strategic and financially accretive businesses that can further our goal of being the partner of choice for lotteries around the world.

Capital

We work to ensure an appropriate capital structure that will provide the funds to meet our strategic objectives and during this past year we achieved some important objectives in that regard.

In June we renewed our credit facility for a three-year term, significantly increasing the amount of capital available, lowering costs and increasing the flexibility of our relationship with our senior banking group. At December 31, 2018, we had approximately $60 million of unused availability in our credit facility.

In February 2018, we completed a very successful common share offering raising approximately $36 million before costs. This was our first return to the equity capital markets since our initial public offering more than 10 years ago and we remain committed to expanding our equity base to support our long-term growth.

The nature of our operations generates significant organic cash flow which is a key building block in our liquidity and funding strategy. In 2018 our cash flow from operating activities was $39.7 million, a significant 77% conversion rate of cash relative to Adjusted EBITDA. These funds are used to finance our investments in capital improvements, product development and the ongoing operations of Pollard as well as providing capital to assist in our acquisitions.

Outlook for 2019

Our outlook for 2019 remains very positive. The lottery and charitable gaming industries remain healthy with continued growing demand for instant tickets and other regulated gaming products. Lotteries and charitable organizations are looking for additional products and services to generate proceeds for the good causes they support and this in turn provides opportunities for Pollard Banknote. We believe our growth and development over 2018 and the past few years has positioned us to be the partner of choice and we will continue to pursue this strategy.

Our investments in innovative products and services to meet these growing customer demands will continue, both through the internal development of unique state-of-the art solutions and leading-edge print products as well as enhancing our offerings through strategic acquisitions.

We anticipate our businesses will continue to generate strong cash flow in 2019 which will provide the funding for our key initiatives including critical capital investments, working capital growth and ongoing debt repayment. On March 13, 2019, our Board of Directors increased our dividend by 33%, recognizing the strength of our underlying businesses and strong cash flow.

2018 was another successful year for Pollard Banknote and we owe this success to many people: over 1,700 enthusiastic employees work diligently to achieve our vision; numerous lottery and charitable gaming organizations partner with us to help generate proceeds for various good causes; many industry leading suppliers help us develop innovative solutions; our Board of Directors provide insightful leadership and encouragement; and shareholders entrust us with their confidence to grow Pollard Banknote and ensure we are the partner of choice in the lottery and charitable gaming industry for years to come. We thank you for your support and look forward to another year of growth in 2019.

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On January 4, 2019, Lawrie Pollard, our past President and Chairman Emeritus, passed away peacefully at age 90 after 71 years of devoted service to our company. Lawrie was a true visionary who led our organization into the lottery business and without his foresight, drive and passion, Pollard Banknote would not be the organization it is today. Lawrie always enjoyed engaging with people he met through Pollard Banknote, including his employees, his business partners and his shareholders. He will be sorely missed.

Douglas Pollard
Co-Chief Executive Officer

John Pollard
Co-Chief Executive Officer

DIRECTORS OF POLLARD BANKNOTE LIMITED

Gordon Pollard

Executive Chair

Gordon Pollard joined Pollard Banknote in 1989 as Vice President, Marketing. He became Co-Chief Executive Officer in 1997 and on May 1, 2011, was appointed Executive Chair of the Board of Directors. Prior to 1989, he practiced law with a major Manitoba firm specializing in corporate and securities law. Mr. Pollard has an LL.B. from the University of Manitoba and a B.A. from the University of Winnipeg.

Dave Brown

Dave Brown is President and CEO of Richardson Capital and Managing Director of RBM Capital Limited. Previously, he was Corporate Secretary of James Richardson & Sons, Limited, and a partner in the independent law and accounting firm of Gray & Brown. He also serves on the Board of Directors of GMP Capital, Inc. and Richardson Financial Group, and on the Board of Trustees of The Boyd Group Income Fund. He graduated from the University of Manitoba law school and is a Chartered Professional Accountant and member of the Manitoba Bar.

Jerry Gray

Jerry Gray is Dean Emeritus of the I. H. Asper School of Business at the University of Manitoba where he also held the CA Manitoba Endowed Chair in Business Leadership. He is a Past Chair of the Winnipeg Regional Health Authority and is a director and Chairman of the Board of Gendis, Inc. He has consulted with many major corporations in the United States and Canada in the areas of motivation, organizational design, manpower planning, managing change, management development, incentive system design, customer service and strategic planning.

Garry Leach

Garry Leach is the Chief Executive Officer of Mandak Capital Limited (an investment corporation). From 1988 to 2004, Mr. Leach was President and Chief Executive Officer of Gerdau MRM Steel (Manitoba Rolling Mills) and its predecessors. Mr. Leach has previously served on the Board of Directors for Gerdau Ameristeel, GLM Industries, Manitoba Hydro, the Canadian Steel Producers Association, (Ottawa), the Steel Manufacturers Association, (Washington), as well as the Business Council of Manitoba. Mr. Leach also served as Regent for the University of Winnipeg.

Douglas Pollard

Douglas Pollard is Co-Chief Executive Officer of Pollard Banknote. He joined Pollard Banknote in 1997 as Vice President, Lottery Management Services and on May 1, 2011, he was appointed Co-Chief Executive Officer. From 1997 to 1999 he was a director and the General Manager of Imprimerie Spéciale de Banque, a subsidiary of Pollard Banknote based in Paris, France. Prior to 1997, Mr. Pollard was a Senior Consultant with PricewaterhouseCoopers. Mr. Pollard has an M.B.A. from The Richard Ivey School of Business at the University of Western Ontario and a B.A. from the University of Manitoba.

John Pollard

John Pollard is Co-Chief Executive Officer of Pollard Banknote. He joined Pollard Banknote in 1986 as Vice President, Finance and became Co-Chief Executive Officer in 1997. Prior to 1986, he was an associate with the accounting firm Deloitte & Touche LLP. Mr. Pollard has a B.Comm. (Honours) from the University of Manitoba and is a former member of the Institute of Chartered Accountants of Manitoba.

December 31, 2018

MANAGEMENT'S DISCUSSION AND ANALYSIS OF FINANCIAL CONDITION AND RESULTS OF OPERATIONS

FOR THE YEAR ENDED DECEMBER 31, 2018

March 13, 2019

This management's discussion and analysis ("MD&A") of Pollard Banknote Limited ("Pollard") for the year ended December 31, 2018, is prepared as at March 13, 2019, and should be read in conjunction with the accompanying audited financial statements of Pollard and the notes therein as at December 31, 2018. Results are reported in Canadian dollars and have been prepared in accordance with International Financial Reporting Standards ("GAAP" or "IFRS").

Forward-Looking Statements

Certain statements in this report may constitute "forward-looking" statements which involve known and unknown risks, uncertainties and other factors which may cause actual results, performance or achievements to be materially different from any future results, performance or achievements expressed or implied by such forward looking statements. When used in this document, such statements include such words as "may," "will," "expect," "believe," "plan" and other similar terminology. These statements reflect management's current expectations regarding future events and operating performance and speak only as of the date of this document. There should not be an expectation that such information will in all circumstances be updated, supplemented or revised whether as a result of new information, changing circumstances, future events or otherwise.

Use of Non-GAAP Financial Measures

Reference to "Adjusted EBITDA" is to earnings before interest, income taxes, depreciation and amortization, purchase accounting amortization, unrealized foreign exchange gains and losses and certain non-recurring items including severance costs and acquisition costs. Adjusted EBITDA is an important metric used by many investors to compare issuers on the basis of the ability to generate cash from operations and management believes that, in addition to net income, Adjusted EBITDA is a useful supplementary measure.

Adjusted EBITDA is a measure not recognized under GAAP and does not have a standardized meaning prescribed by GAAP. Therefore, this measure may not be comparable to similar measures presented by other entities. Investors are cautioned that Adjusted EBITDA should not be construed as an alternative to net income determined in accordance with GAAP as an indicator of Pollard's performance or to cash flows from operating, investing and financing activities as measures of liquidity and cash flows.

Basis of Presentation

The results of operations in the following discussions encompass the consolidated results of Pollard for the year ended December 31, 2018. All figures are in millions except for per share amounts.

POLLARD BANKNOTE LIMITED

Overview

Pollard Banknote Limited ("Pollard") is one of the leading providers of products and services to lottery and charitable gaming industries throughout the world. Management believes Pollard is the largest provider of instant-win scratch tickets ("instant tickets") based in Canada and the second largest producer of instant tickets in the world. With the acquisition of International Gamco, Inc. ("Gamco"), on February 1, 2018, management believes Pollard has also become the second largest bingo paper and pull-tab supplier to the charitable gaming industry in North America.

Pollard produces and provides a comprehensive line of instant tickets and lottery services including: licensed products, distribution, SureTrack® lottery management system, retail telephone selling ("tel-sell"), marketing, iLottery, interactive digital gaming, Playon™ VIP lottery program, Social Instants™, retail management services, ScanACTIV™ and vending machines including charitable game systems marketed under the Diamond Game and Oasis trade names. In addition, Pollard's charitable gaming product line includes pull-tab (or break-open) tickets, bingo paper, pull-tab vending machines and ancillary products such as pull-tab counting machines. Pollard also markets products to the commercial gaming and security sector including such items as promotional scratch and win tickets, transit tickets and parking passes.

Pollard's lottery products are sold extensively throughout Canada, the United States and the rest of the world, wherever applicable laws and regulations authorize their use. Pollard serves over 60 instant ticket lotteries including a number of the largest lotteries throughout the world. Charitable gaming products are mostly sold in the United States and Canada where permitted by gaming regulatory authorities. Pollard serves a highly diversified customer base in the charitable gaming market of over 275 independent distributors with the majority of revenue generated from repeat business.

Product line breakdown of revenue

	Year ended December 31, 2018	Year ended December 31, 2017
Lottery[1]	75.5%	86.7%
Charitable [2]	16.6%	9.7%
Gaming systems [3]	7.9%	3.6%

(1) Includes the business of Schafer Systems Inc. which was acquired on October 31, 2018.

(2) Includes International Gamco, Inc. which was acquired on February 1, 2018.

(3) INNOVA Gaming Group Inc. ("INNOVA", "Diamond Game") was acquired on August 3, 2017.

Geographic breakdown of revenue

	Year ended December 31, 2018	Year ended December 31, 2017
United States	56%	56%
Canada	23%	22%
International	21%	22%

Acquisition of International Gamco, Inc.

On February 1, 2018, Pollard Holdings Inc., a wholly-owned subsidiary of Pollard, acquired 100% of the common shares of International Gamco, Inc.. 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 February 1, 2018, the acquisition date. As per the sales agreement, the purchase price was decreased by the amount of other current liabilities assumed, which were specified in the agreement. The majority of these other current liabilities were paid in March 2018.

During the period between February 1, 2018 and December 31, 2018, Gamco generated revenues of $27.1 million and net income of $1.1 million, after depreciation and amortization of the fair values of identifiable assets acquired, which have been recorded in the consolidated financial statements. If Gamco had been acquired on January 1, 2018, incremental revenue of $2.2 million and net loss of $4.8 million (which includes $4.8 million of transaction related expenditures, net of income tax) would have been recognized in the year ended December 31, 2018.

Share offering

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.

The offering, including the full over-allotment, closed on February 21, 2018. The total gross proceeds, prior to any commissions and offering expenses, from the sale of 2,070,000 common shares was approximately $38.2 million.

Pollard used the net proceeds to repay indebtedness under the Company's credit facility and subordinated debt.

Acquisition of Schafer Systems

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"), a leading global provider of lottery ticket dispensers and play stations, for a purchase price of approximately US$23.2 million. 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. Pollard Systems Inc. was renamed Schafer Systems (2018) Inc. upon completion of the transaction.

During the period between October 31, 2018 and December 31, 2018, Schafer generated revenues of $2.2 million and net income of $0.2 million, after depreciation and amortization of the fair values of identifiable assets acquired, which have been recorded in the consolidated financial statements. If Schafer had been acquired on January 1, 2018, incremental revenue of $11.8 million and net income of $1.9 million would have been recognized in the year ended December 31, 2018.

The following financial information should be read in conjunction with the accompanying financial statements of Pollard and the notes therein as at and for the year ended December 31, 2018.

SELECTED FINANCIAL INFORMATION

(millions of dollars, except per share information)

	Year ended December 31, 2018	Year ended December 31, 2017	Year ended December 31, 2016
Sales	**$331.9**	$285.6	$246.4
Cost of sales	**256.2**	219.9	197.2
Gross profit	**75.7**	65.7	49.2
Gross profit as a % of sales	***22.8%***	*23.0%*	*20.0%*
Administration expenses	**32.2**	28.6	20.9
Expenses as a % of sales	***9.7%***	*10.0%*	*8.5%*
Selling expenses	**13.4**	9.4	8.0
Expenses as a % of sales	***4.0%***	*3.3%*	*3.2%*
Net income	**14.9**	16.8	12.3
Net income as a % of sales	***4.5%***	*5.9%*	*5.0%*
Adjusted EBITDA	**48.8**	44.0	29.7
Adjusted EBITDA as a % of sales	***14.7%***	*15.4%*	*12.1%*
Earnings per share (basic and diluted)	**$0.58**	$0.71	$0.52

	December 31, 2018	December 31, 2017	December 31, 2016
Total Assets	**$305.6**	$228.3	$176.8
Total Non-Current Liabilities	**$142.9**	$124.8	$94.4

RECONCILIATION OF NET INCOME TO ADJUSTED EBITDA

(millions of dollars)

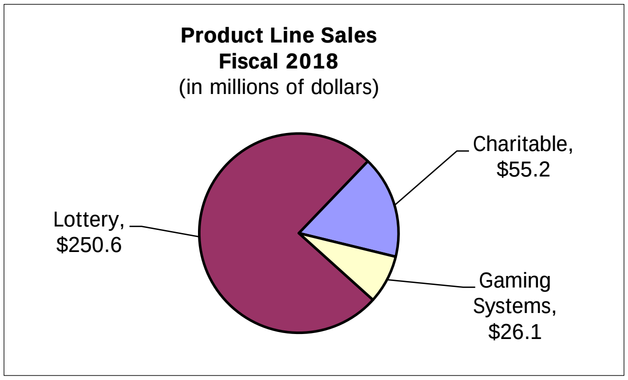
	Year ended December 31, 2018	Year ended December 31, 2017	Year ended December 31, 2016
Net income	**$14.9**	$16.8	$12.3
Adjustments:			
Amortization and depreciation	**18.0**	13.1	10.6
Interest	**4.2**	3.9	3.6
Unrealized foreign exchange (gain) loss	**4.6**	(1.4)	(1.6)
Acquisition costs	**0.8**	2.7	-
Severance costs	**0.4**	1.7	-
Income taxes	**5.9**	7.2	4.8
Adjusted EBITDA	**$48.8**	$44.0	$29.7
Lotteries and charitable gaming	**$38.4**	$40.0	$29.7
Diamond Game	**10.4**	4.0	-
Total Adjusted EBITDA	**$48.8**	$44.0	$29.7

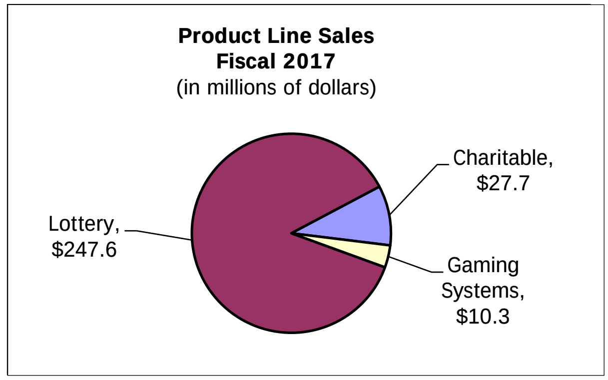
REVIEW OF OPERATIONS

Financial and operating information has been derived from, and should be read in conjunction with, the consolidated financial statements of Pollard and the selected financial information disclosed in this MD&A.

ANALYSIS OF RESULTS FOR THE YEAR ENDED DECEMBER 31, 2018

Sales



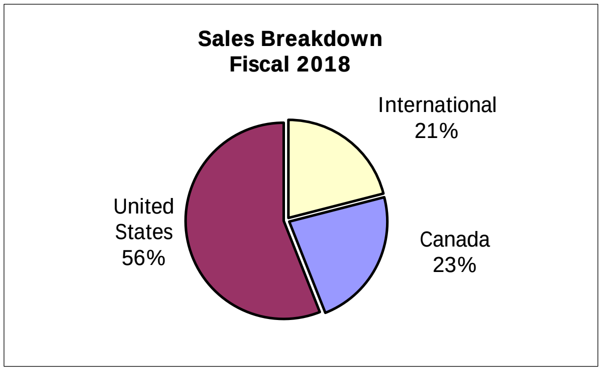


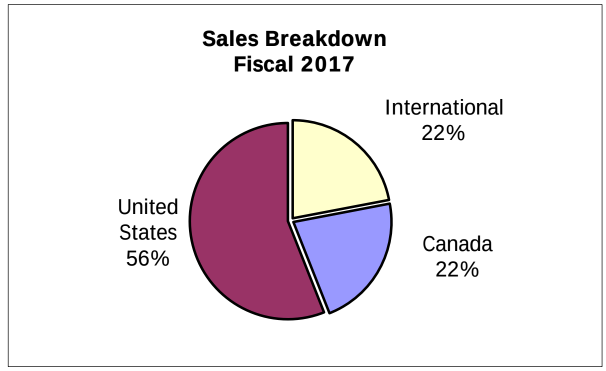
During the year ended December 31, 2018 ("Fiscal 2018" or "2018"), Pollard achieved sales of $331.9 million, compared to $285.6 million in the year ended December 31, 2017 ("Fiscal 2017" or "2017"). Factors impacting the $46.3 million sales increase were:

Higher instant ticket sales volumes in the first three quarters of 2018, which were substantially offset by lower sales volumes in the fourth quarter of 2018, increased sales slightly by $1.3 million compared to Fiscal 2017. Additionally, higher instant ticket average selling price increased sales by $1.8 million when compared to 2017. An increase in ancillary instant ticket products and services volumes grew revenue by $0.5 million. This increase primarily resulted from sales due to the addition of Schafer, beginning November 1, 2018, and higher iLottery revenues, partially offset by lower licensed product sales in 2018.

After the first nine months of 2018 our instant ticket volumes were on track to be significantly higher than Fiscal 2017. However, a temporary reduction in orders from our customers in the fourth quarter resulted in Fiscal 2018 sales and production volumes roughly equaling 2017. Our order volumes for the first quarter of 2019 have returned to similar levels of the first three quarters of 2018. In addition, approximately 15% of the instant tickets produced in the fourth quarter 2018 were not recognized in sales due to the timing of shipments but are anticipated to be recognized in the first quarter of 2019.

The addition of Diamond Game in August 2017 added $15.5 million in sales to Fiscal 2018 when compared to 2017. An increase in charitable gaming volumes, primarily as a result of the acquisition of Gamco, including its Oasis division's sale of electronic pull-tab machines into the North Dakota market, increased sales by $26.7 million from 2017. A higher average selling price for charitable games in 2018 further increased sales by $1.1 million.





During Fiscal 2018, Pollard generated approximately 69.8% (2017 – 69.4%) of its revenue in U.S. dollars including a portion of international sales which are priced in U.S. dollars. During Fiscal 2018 the actual U.S. dollar value was converted to Canadian dollars at an average rate of $1.292 compared to an average rate of $1.304 during Fiscal 2017. This 1.0% decrease in the U.S. dollar value resulted in an approximate decrease of $1.5 million in revenue relative to Fiscal 2017. Also during 2018 the value of the Canadian dollar weakened against the Euro resulting in an approximate increase of $0.9 million in revenue relative to 2017.

Cost of sales and gross profit

Cost of sales was $256.2 million in Fiscal 2018 compared to $219.9 million in Fiscal 2017. Cost of sales was higher in Fiscal 2018 primarily as a result of the inclusion of Gamco and Schafer, and a full year of Diamond Game, as well as the slight increase in instant ticket sales volumes.

Gross profit was $75.7 million (22.8% of sales) in Fiscal 2018 compared to $65.7 million (23.0% of sales) in Fiscal 2017. This increase of $10.0 million in gross profit was primarily the result of the addition of Gamco and Schafer, and a full year of Diamond Game, which increased gross margin by approximately $11 million. Gross profit generated from the lotteries and charitable gaming business (excluding acquisitions) declined approximately $1 million due to lower licensed games sales and lower gross margin on slightly lower instant ticket production volumes year over year. The significant reduction in the fourth quarter instant ticket production volumes resulted in the total production volume for Fiscal 2018 being slightly lower than Fiscal 2017. The gross profit percentage was slightly lower due to the small decrease in instant ticket production volumes and a reduction in license product sales, partially offset by higher iLottery sales.

Administration expenses

Administration expenses increased to $32.2 million in Fiscal 2018 from $28.6 million in Fiscal 2017. The increase of $3.6 million was partially a result of the inclusion of Gamco and Schafer, and a full year of Diamond Game. Additional reasons for the increase were higher compensation expenses to support Pollard's growth strategies of acquisition and digital innovation, as well as increased professional fees and IT infrastructure related expenses totaling approximately $2 million. These increases were partially offset by the $1.9 million reduction in acquisition costs and $1.3 million reduction in severance costs as compared to 2017.

Selling expenses

Selling expenses increased to $13.4 million in Fiscal 2018 from $9.4 million in Fiscal 2017 primarily due to the addition of Gamco and Diamond Game for an entire year in 2018, as well as higher compensation costs. These increases were partially offset by a decrease in contract support costs.

Other expenses

Other expenses decreased to $0.4 million in Fiscal 2018 from $0.7 million in 2017, primarily due to the increase in the income from the EBITDA support agreement with a full year of Diamond Game, partially offset by the increased loss on equity investment.

Foreign exchange

The net foreign exchange loss was $4.7 million in Fiscal 2018 compared to a net gain of $0.9 million in Fiscal 2017. The 2018 net foreign exchange loss consisted of a $4.6 million unrealized loss primarily as a result of the increased Canadian equivalent value of U.S. dollar denominated accounts payable and long-term debt with the weakening of the Canadian dollar relative to the U.S. dollar. In 2018 Pollard added almost $29 million of U.S. dollar denominated debt, with the acquisitions of Gamco and Schafer, which is subject to revaluation through the income statement. At December 31, 2018, the Canadian dollar had weakened relative to the U.S. dollar, resulting in the substantial unrealized foreign exchange loss.

In addition to the unrealized foreign exchange loss in 2018, Pollard incurred a realized foreign exchange loss of $0.1 million as a result of foreign currency denominated accounts receivable collected being converted into Canadian dollars at unfavorable foreign exchange rates.

The 2017 net foreign exchange gain consisted of a $1.4 million unrealized gain primarily as a result of the decreased Canadian equivalent value of U.S. dollar denominated accounts payable and long-term debt with the strengthening of the Canadian dollar relative to the U.S. dollar. This gain was partially offset by the realized foreign exchange loss of $0.5 million as a result of foreign currency denominated account receivables collected being converted into Canadian dollars at unfavorable foreign exchange rates.

Adjusted EBITDA

Adjusted EBITDA was $48.8 million in Fiscal 2018 compared to $44.0 million in Fiscal 2017. The primary reasons for the increase in Adjusted EBITDA of $4.8 million were the increase in gross profit of $14.9 million (net of amortization and depreciation), a decrease in other expenses of $0.3 million and a decrease in realized foreign exchange loss of $0.4 million. These increases to Adjusted EBITDA were partially offset by higher administration expenses (net of acquisition and severance costs) of $6.8 million and an increase in selling expenses of $4.0 million.

Our lotteries and charitable gaming business, excluding our 2018 acquisition of Gamco, generated approximately $5.0 million lower Adjusted EBITDA compared to Fiscal 2017. Gross profit decreased by approximately $3.0 million (excluding depreciation and amortization) due to lower licensed games sales and higher costs of goods sold despite slightly lower instant ticket production volumes. Higher administration costs (excluding acquisition costs) increased by approximately $2.0 million primarily due to higher compensation expenses to support Pollard's growth strategies of acquisition and digital innovation, as well as increased professional fees and IT infrastructure related expenses.

These decreases in lotteries and charitable gaming Adjusted EBITDA were partially offset by acquisitions of Gamco and Schafer, and the full year impact of Diamond Game, totaling approximately $9.8 million.

Interest expense

Interest expense increased to $4.2 million in Fiscal 2018 from $3.9 million in Fiscal 2017 primarily as a result of the additional interest expense related to increased long-term debt incurred with the acquisitions of Gamco and Schafer.

Amortization and depreciation

Amortization and depreciation, including depreciation of property and equipment and the amortization of intangible assets, totaled $18.0 million during Fiscal 2018 which increased from $13.1 million during Fiscal 2017. The increase was a result of the addition of Diamond Game, Gamco and Schafer including the amortization and depreciation relating to the purchase price allocations to tangible and intangible assets acquired.

Income taxes

Income tax expense was $5.9 million in Fiscal 2018, an effective rate of 28.5%, which was higher than our domestic rate of 27.0% due primarily to non-deductible amounts relating to expenses incurred in the acquisitions and the effect of foreign exchange. Partially offsetting these increases was the lower federal income tax rates in the United States.

Income tax expense was $7.2 million in Fiscal 2017, an effective rate of 30.0%, which was higher than our domestic rate of 27.0% due primarily to adjustments relating to the acquisition of Diamond Game, the effect of higher tax rates in the United States in 2017 on current taxes and non-deductible amounts primarily relating to expenses incurred in the acquisition of Diamond Game. Partially offsetting these increases was the reduction in the future federal income tax rates in the United States which reduced related deferred taxes.

Net income

Net income was $14.9 million in Fiscal 2018 compared to net income of $16.8 million in Fiscal 2017. Our lotteries and charitable gaming business generated lower net income compared to 2017 due to the lower instant ticket production and sales volumes combined with the large unrealized foreign exchange loss. Partially offsetting these decreases were the net income associated with the 2018 acquisitions and the inclusion of a full year of Diamond Game.

Specifically the reasons for the decrease in net income were the increase in net foreign exchange loss of $5.6 million, the increase in administration expenses of $3.6 million, the increase in selling expenses of $4.0 million and the increase in interest expense of $0.3 million. Partially offsetting these decreases in net income were the increase in gross profit of $10.0 million, the decrease in other expenses of $0.3 million and the decrease in income taxes of $1.3 million.

Earnings per share (basic and diluted) decreased to $0.58 per share in Fiscal 2018 from $0.71 per share in Fiscal 2017.

Liquidity and Capital Resources

Cash provided by operating activities

For the year ended December 31, 2018, cash flow provided by operating activities was $39.7 million compared to $28.4 million in Fiscal 2017. Higher net income before income taxes and after non-cash adjustments in Fiscal 2018 contributed an additional $9.5 million to the increase in cash provided by operating activities compared to Fiscal 2017.

For the fiscal year 2018, changes in the non-cash component of working capital increased cash flow from operations by $4.0 million. The increase was due primarily to a decrease in accounts receivables, partially offset by an increase in inventory and a decrease in accounts payable and accrued liabilities. For the fiscal year 2017, changes in the non-cash component of working capital decreased cash flow from operations by $2.9 million. The decrease was due primarily to increases in inventory and prepaid expenses and deposits, partially offset by an increase in accounts payable and accrued liabilities.

Cash used for interest payments increased to $4.5 million in 2018 as compared to $3.7 million in 2017. Cash used for pension plan contributions increased to $5.5 million in 2018 as compared to $5.3 million in 2017. Cash used for income taxes paid was $10.2 million in 2018 compared to $6.1 million in 2017. Income tax payments in 2018 included the final installments for the 2017 tax year and initial installments for 2018. Increasing taxable income in 2017 resulted in a higher installment requirement.

Cash used for investing activities

In the year ended December 31, 2018, cash used for investing activities was $77.1 million compared to $51.2 million in the year ended December 31, 2017. In Fiscal 2018, Pollard used $21.6 million, net of cash acquired, to purchase Gamco and $30.4 million to purchase Schafer. In addition, Pollard expended $15.1 million in capital expenditures, $2.8 million on its investment in its iLottery joint venture and $7.1 million on additions to intangible assets.

In Fiscal 2017, Pollard used $39.3 million, net of cash acquired, to purchase Diamond Game. In addition, Pollard invested $6.9 million in capital expenditures, $2.2 million in its iLottery joint venture and $2.2 million on additions to intangible assets.

Cash provided by financing activities

Cash provided by financing activities was $42.6 million in the year ended December 31, 2018, compared to $21.3 million in the year ended December 31, 2017.

During Fiscal 2018, Pollard raised $35.4 million, net of expenses, from the issuance of common shares, which was used, in part, to repay $16.7 million of subordinated debt. In addition, Pollard received net proceeds from long-term debt of $27.9 million, partially to fund the acquisitions of Gamco and Schafer. These cash receipts were partially offset by $0.6 million of financing costs and dividends paid of $3.1 million.

During Fiscal 2017, Pollard received net proceeds from long-term debt of $13.5 million and $10.6 million from subordinated debt, which partially funded the acquisition of Diamond Game. These cash receipts were partially offset by $0.3 million of financing costs and dividends paid of $2.8 million.

As at December 31, 2018, Pollard had unused committed credit facility of $58.9 million, in addition to $11.2 million in available cash resources. These amounts, in addition to cash flow provided by operating activities, are available to be used for future working capital requirements, contractual obligations, capital expenditures, dividends and to assist in financing future acquisitions.

ANALYSIS OF RESULTS FOR THE PERIOD OCTOBER 1, 2018 TO DECEMBER 31, 2018 FOURTH QUARTER OF 2018

SELECTED FINANCIAL INFORMATION

(millions of dollars)

	Three months ended December 31, 2018	Three months ended December 31, 2017
	(unaudited)	(unaudited)
Sales	$70.2	$79.6
Cost of sales	56.9	62.1
Gross profit	13.3	17.5
Administration	7.9	7.5
Selling	3.6	2.6
Other income	(0.1)	-
Income from operations	1.9	7.4
Finance costs	4.2	1.3
Income (loss) before income taxes	(2.3)	6.1
Income taxes:		
Current (recovery)	(0.4)	1.5
Future	-	0.3
	(0.4)	1.8
Net income (loss)	($1.9)	$4.3
Adjustments:		
Amortization and depreciation	5.3	4.5
Interest	1.2	1.3
Unrealized foreign exchange loss	3.1	0.5
Acquisition costs	0.2	0.3
Severance costs	-	0.3
Income taxes (recovery)	(0.4)	1.8
Adjusted EBITDA	$7.5	$13.0
Lotteries and charitable gaming	$4.9	$10.1
Diamond Game	2.6	2.9
Adjusted EBITDA	$7.5	$13.0

Sales

During the three months ended December 31, 2018, Pollard achieved sales of $70.2 million, compared to $79.6 million in the three months ended December 31, 2017. Factors impacting the $9.4 million sales decrease were:

Instant ticket sales volumes for the fourth quarter of 2018 were significantly lower, 31.9%, than the fourth quarter of 2017, which decreased sales by $19.4 million. The reduction in instant ticket volumes was two-fold. Production orders were down almost 15% from the fourth quarter of 2017 due to a temporary decline in orders from our customer portfolio as a number of our larger customers had lower orders during the quarter. The reduction in order volumes was temporary and reflects the variability of order patterns and the nature of our sales mix with relatively few orders of a large dollar amount. With the start of the first quarter of 2019 our production volumes and order levels have returned to similar levels experienced in the first three quarters of 2018.

Secondly, approximately 14% of the tickets produced in the quarter did not meet the revenue recognition standards primarily because shipments to the lotteries were not required until early 2019. This is similar to the situation that occurred in the first quarter of 2017 when timing of customer receipts delayed the revenue recognition of produced tickets until the next quarter. We anticipate a majority of these deferred sales volumes to be shipped and recognized in the first quarter of 2019. The impact of these factors resulted in an approximate reduction in Adjusted EBITDA of $6.0 million. A decrease in the average selling prices of instant tickets further reduced sales by $0.4 million.

Partially offsetting these decreases was an increase in our ancillary instant ticket products and services volumes, primarily sales from the addition of Schafer, increased iLottery revenues, and partially offset by lower licensed product sales. The net of these increased revenue by $1.5 million.

The increase in charitable gaming volumes, primarily as a result of the addition of Gamco, increased sales by $7.1 million from 2017, including its Oasis division's sale of electronic pull-tab machines into the North Dakota market. Also the higher average selling price for charitable games in 2018 further increased sales by $0.4 million.

During the three months ended December 31, 2018, Pollard generated approximately 80.5% (2017 – 67.1%) of its revenue in U.S. dollars including a portion of international sales which were priced in U.S. dollars. During the fourth quarter of 2018 the actual U.S. dollar value was converted to Canadian dollars at an average rate of $1.311, compared to an average rate of $1.275 during the fourth quarter of 2017. This 2.9% increase in the value of the U.S. dollar resulted in an approximate increase of $1.4 million in revenue relative to 2017.

Cost of sales and gross profit

Cost of sales was $56.9 million in the fourth quarter of 2018 compared to $62.1 million in the fourth quarter of 2017. Cost of sales was lower in the quarter as a result of the decrease in instant ticket volumes discussed above. Partially offsetting the decrease was increases in cost of goods sold incurred with the inclusion of Gamco and Schafer as compared to the fourth quarter of 2017.

Gross profit was $13.3 million (18.9% of sales) in the fourth quarter of 2018 compared to $17.5 million (22.0% of sales) in the fourth quarter of 2017. This decrease in gross profit was primarily the result of the decrease in instant ticket production and sales volumes. The decrease in our order volumes was temporary and reflects the variability of our order patterns and the nature of our sales mix with relatively few orders of a large dollar amount. With the start of the first quarter of 2019 our production volumes and order levels have returned similar to the levels experienced in the first three quarters of 2018.

Partially offsetting this reduction in gross profit was the gross profit earned by Gamco and Schafer and increased iLottery gross profits. The gross profit percentage was lower due to the decrease in instant tickets volumes, partially offset by increased sales of ancillary instant ticket products and services, including higher iLottery sales, and the inclusion of Gamco and Schafer.

Administration expenses

Administration expenses increased to $7.9 million in the fourth quarter of 2018 compared to $7.5 million in the fourth quarter of 2017. The increase was partially a result of the inclusion of Schafer and Gamco in 2018. Additional reasons for the increase were higher compensation expenses to support Pollard's growth strategies of digital innovation, as well as increased professional fees. These increases were partially offset by a reduction in Diamond Game compensation and severance costs compared to 2017.

Selling expenses

Selling expenses increased to $3.6 million in the fourth quarter of 2018 from $2.6 million in the fourth quarter of 2017. The increase was primarily as a result of the inclusion of Schafer and Gamco, in addition to higher selling related costs in Diamond Game when compared to 2017. Partially offsetting these increases was a decrease in contract support costs.

Foreign exchange

The net foreign exchange loss was $3.0 million in the fourth quarter of 2018 compared to a net loss of $nil in the fourth quarter of 2017. The 2018 net foreign exchange loss consisted of a $3.1 million unrealized loss primarily as a result of the increased Canadian equivalent value of U.S. dollar denominated accounts payable and long-term debt due to the weakening of the Canadian dollar relative to the U.S. dollar. The Canadian dollar weakened approximately 5.5% since the beginning of the fourth quarter of 2018 and this movement, combined with higher U.S. dollar denominated debt relating to the acquisitions, generated a substantial unrealized foreign exchange loss. The unrealized foreign exchange loss was partially offset by the realized foreign exchange gain of $0.1 million, as a result of foreign currency denominated account receivables collected being converted into Canadian dollars at favorable foreign exchanges rates.

The 2017 net foreign exchange loss consisted of a $0.5 million unrealized loss which was primarily as a result of the decreased Canadian equivalent value of U.S. denominated accounts receivables with the weakening of the Canadian dollar relative to the U.S. dollar. This loss was fully offset by the realized foreign exchange gain of $0.5 million, as a result of foreign currency denominated account receivables collected being converted into Canadian dollars at favorable foreign exchanges rates.

Adjusted EBITDA

Adjusted EBITDA was $7.5 million in the fourth quarter of 2018 compared to $13.0 million in the fourth quarter of 2017. The primary reason for the reduction were the lower sales and production volumes of instant tickets noted above which negatively impacted Adjusted EBITDA by approximately $6.0 million. In addition, the increase in administration expenses (net of severance and acquisition costs) of $0.8 million, an increase in selling expenses of $1.0 million and the decrease in the realized foreign exchange gain of $0.4 million further lowered Adjusted EBITDA. The 2018 acquisitions increased Adjusted EBITDA by approximately $3.0 million.

Interest expense

Interest expense was $1.2 million in the fourth quarter of 2018 consistent with $1.3 million in the fourth quarter of 2017.

Amortization and depreciation

Amortization and depreciation, including depreciation of property, plant and equipment and the amortization of intangible assets, increased to $5.3 million during the fourth quarter of 2018 as compared to $4.5 million during the fourth quarter of 2017. The increase was a result of the additions of Diamond Game, Gamco and Schafer including the amortization and depreciation relating to the purchase price allocations to tangible and intangible assets acquired.

Income taxes (recovery)

Income tax recovery was $0.4 million in the fourth quarter of 2018, an effective rate of 16.3% which was lower than our domestic rate of 27.0% due primarily to non-deductible amounts relating to expenses incurred in the acquisitions and the effect of foreign exchange. Partially offsetting these decreases were the lower federal income tax rates in the United States.

Income tax expense was $1.8 million in the fourth quarter of 2017, an effective rate of 28.8% which was higher than our domestic rate of 27.0% due primarily to adjustments relating to the acquisition of Diamond Game, the effect of higher tax rates in the United States in 2017 on current taxes, the effect of foreign exchange and non-deductible amounts primarily relating to expenses incurred in the acquisition of Diamond Game. Partially offsetting these increases was the reduction in the future federal income tax rates in the United States which reduced related deferred taxes.

Net income (loss)

Net loss was $1.9 million in the fourth quarter of 2018 compared to net income of $4.3 million in the fourth quarter of 2017. The primary reasons for the decrease in net income were the lower gross profit of $4.2 million, due to the reduction in instant ticket sales and production volumes partially offset by the impact of the 2018 acquisitions, the increase in foreign exchange loss of $3.0 million, the increase in administration expenses of $0.4 million and the increase in selling expenses of $1.0 million. Partially offsetting these decreases was the reduction in income taxes of $2.2 million.

Earnings (loss) per share (basic and diluted) decreased to ($0.08) per share in the fourth quarter of 2018 from $0.18 per share in the fourth quarter of 2017.

Quarterly Information
(unaudited)
(millions of dollars)

	Q4 2018	Q3 2018	Q2 2018	Q1 2018	Q4 2017	Q3 2017	Q2 2017	Q1 2017
Sales	$70.2	$94.5	$86.8	$80.4	$79.6	$70.6	$77.9	$57.5
Adjusted EBITDA	7.5	14.2	14.1	13.0	13.0	11.6	13.1	6.3
Net income (loss)	(1.9)	7.2	5.0	4.6	4.3	4.7	6.0	1.8

The significant decrease in instant ticket volumes in the fourth quarter of 2018 reduced sales, Adjusted EBITDA and net income. Net income was further reduced by the large unrealized foreign exchange loss in the quarter.

The trend of increased sales, Adjusted EBITDA and net income, starting the fourth quarter of 2017 through to the third quarter of 2018, was primarily as a result of higher instant ticket volumes and the additions of Diamond Game and Gamco.

Working Capital

Net non-cash working capital varies throughout the year based on the timing of individual sales transactions and other investments. The nature of the lottery industry is few individual customers who generally order large dollar value transactions. As such, the change in timing of a few individual orders can significantly impact the amount required to be invested in inventory or receivables at a particular period end. The high value, low volume of transactions results in some significant volatility in non-cash working capital, particularly during a period of rising volumes. Similarly, the timing of the completion of the sales cycle through collection can significantly impact non-cash working capital.

Instant tickets are produced specifically for individual clients resulting in a limited investment in finished goods inventory. Customers are predominantly government agencies, which result in regular payments. There are a limited number of individual customers, and therefore net investment in working capital is managed on an individual customer by customer basis, without the need for company-wide benchmarks.

The overall impact of seasonality does not have a material impact on the carrying amounts in working capital.

As at December 31, 2018, Pollard's investment in non-cash working capital decreased $4.0 million compared to December 31, 2017, primarily as a result of the decreased investment in accounts receivables, partially offset by an increase in inventory and a decrease in accounts payable and accrued liabilities.

	December 31, 2018	December 31, 2017
Working Capital	$65.5	$44.6
Total Assets	$305.6	$228.3
Total Non-Current Liabilities	$142.9	$124.8

Credit Facility

Pollard's credit facility was renewed effective June 22, 2018. The credit facility provides loans of up to $160.0 million for its Canadian operations and US$12.0 million for its U.S. subsidiaries. The borrowings for the Canadian operations can be denominated in Canadian or U.S. dollars, to a maximum of $160.0 million Canadian equivalent. The credit facility also includes an accordion feature which can increase the facility by $25.0 million. 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 December 31, 2018, the outstanding letters of guarantee were $1.3 million. The remaining balance available for drawdown under the credit facility was $58.9 million.

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 December 31, 2018, Pollard is in compliance with all financial covenants.

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.

Pollard believes that its credit facility and ongoing cash flow from operations will be sufficient to allow it to meet ongoing requirements for investment in capital expenditures, working capital, dividends and acquisitions.

Subordinated Debt

On June 23, 2017, Pollard entered into a loan agreement with Pollard Equities Limited for a subordinated term loan with a seven year term, repayable at any time (subject to meeting certain financial covenants under the secured credit facility). The loan was provided to assist with the purchase of Diamond Game. A total of $25.1 million was drawn in the third quarter of 2017. Interest on the subordinated debt commenced with the first draw at a rate of 8%. Quarterly principal payments on the loan facility commenced the month following the first draw, which occurred August 4, 2017.

In addition to the mandatory quarterly payments, Pollard has made three lump sum prepayments. On September 20, 2017, Pollard repaid $7.5 million in outstanding principal and on February 23, 2018, Pollard repaid an additional $7.5 million in outstanding principal. On June 29, 2018, Pollard repaid in full the remainder of the outstanding principal in the amount of $7.5 million.

Outstanding Share Data

As at December 31, 2018 outstanding share data was as follows:

Common shares	25,625,658

In February 2018, 2,070,000 common shares were issued through a share offering.

In October 2018, 12,500 common shares were issued through the exercise of stock options.

As at March 13, 2019, outstanding share data was as follows:

Common shares	25,625,658

Share Options

Under the Pollard Banknote Limited Stock Option Plan the Board of Directors has the authority to grant options to purchase common shares to eligible persons and to determine the applicable terms. The aggregate maximum number of common shares available for issuance from Pollard's treasury under the Option Plan is 2,354,315 common shares. On October 17, 2018, 12,500 stock options were exercised. As at December 31, 2018, the total share options issued and outstanding were 237,500.

Dividends

On March 13, 2019, the Board of Directors increased the rate of dividend from $0.03 per quarter per common share to $0.04 per quarter per common share, declaring a dividend of $0.04 per common share payable on April 15, 2019, for the quarter ending March 31, 2019.

Contractual Obligations

Pollard rents premises and equipment under long-term operating leases. The following is a schedule by year of commitments and contractual obligations outstanding, including related interest payments:

(millions of dollars)	Total	2019	2020	2021	2022	2023
Long-term debt	$129.4	$4.8	$5.6	$119.0	-	-
Operating leases	$20.0	$5.7	$4.9	$3.8	$3.2	$2.4
Total	$149.4	$10.5	$10.5	$122.8	$3.2	$2.4

Pension Obligations

Pollard sponsors four non-contributory defined benefit pension plans, of which three are final pay plans and one is a flat benefit plan. As of December 31, 2018, the aggregate fair value of the assets of Pollard's defined benefit pension plans was $52.9 million and the accrued benefit plan obligations were $73.3 million. Pollard's total annual funding contribution for its defined pension plans in 2019 is expected to be approximately $4.7 million, compared to $4.7 million in 2018, including $1.2 million in additional solvency payments.

One of Pollard's Canadian pension plans was subject to a solvency valuation beginning with its December 31, 2016, valuation. The solvency valuation is required to be updated annually. As at the December 31, 2017, valuation there was a deficit of $9.4 million, due to the low current levels of the mandated interest rate used to discount the future liabilities. As a result, Pollard is subject to additional special pension plan payments of approximately $1.2 million per year through to 2026. These additional solvency payments do not impact pension expense and therefore will not affect our net income or Adjusted EBITDA and will be funded from operating cash flows.

Off-Balance Sheet Arrangements

Other than the operating leases described previously, Pollard has no other off-balance sheet arrangements.

Related Party Transactions

Pollard Equities Limited and affiliates

During the year ended December 31, 2018, Pollard paid property rent of $3.2 million (2017 - $3.2 million) and $0.5 million (2017 - $0.4 million) in plane charter costs to affiliates of Equities. In addition, Pollard paid Equities $0.4 million (2017 - $1.0 million) of interest on Pollard's subordinated debt.

During the year ended December 31, 2018, Equities paid Pollard $0.07 million (2017 - $0.07 million) for accounting and administration fees.

At December 31, 2018, Pollard owed Equities and its affiliates $0.6 million (2017 - $1.9 million) for rent, interest, expenses and other items.

Neogames S.à r.l. and affiliates

During the year ended December 31, 2018, Pollard reimbursed operating costs and paid software royalties of $3.3 million (2017 - $2.9 million) to its iLottery partner, which are recorded in cost of sales.

At December 31, 2018, included in accounts payable and accrued liabilities is a net amount owing to Pollard's iLottery partner of $0.9 million (2017 - $0.7 million) for reimbursement of operating costs and capital expenditures, and its share of operating profits.

Critical Accounting Policies and Estimates

Described in the notes to Pollard's 2018 audited consolidated financial statements are the accounting policies and estimates that Pollard believes are critical to its business. Please refer to note 2 (c) to the audited consolidated financial statements for the year ended December 31, 2018, for a discussion of the significant accounting estimates and judgements.

Future Changes in Accounting Policies

In January 2016, the International Accounting Standards Board ("IASB") issued IFRS 16 *Leases* which replaces IAS 17 *Leases*. This standard introduces a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognize a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. This standard substantially carries forward the lessor accounting requirements of IAS 17, while requiring enhanced disclosures to be provided by lessors. Other areas of the lease accounting model have been impacted, including the definition of a lease. Transitional provisions have been provided. The new standard is effective for annual periods beginning on or after January 1, 2019.

Pollard has undertaken a preliminary review of all lease contracts and has applied the new measurement model for lessees. Pollard leases a number of manufacturing facilities in Canada and the United States. The present value of the remaining lease payments will be recognized on the balance sheet as right to use assets and related lease liabilities upon adoption. The nature of expenses related to those leases will now change because Pollard will recognize a depreciation charge on the right to use assets and an interest expense on the related lease liabilities. Pollard intends to adopt the standard using the modified retrospective approach, using the practical expedient of setting the initial right to use asset and the corresponding lease liability equal. No restatement is required under this approach. Pollard has preliminarily estimated that the transitional impact on the consolidated statements of financial position will result in recognizing right to use assets and corresponding lease liabilities of $18.7 million.

In June 2017, the IASB issued IFRIC Interpretation 23 *Uncertainty over Income Tax Treatments.* The Interpretation 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 is effective for annual periods beginning on or after January 1, 2019 and is to be applied retrospectively. Pollard does not expect the Interpretation to have a significant impact on the consolidated financial statements upon adoption.

In October 2017, the 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. These amendments are effective for annual periods beginning on or after January 1, 2019. Pollard does not expect the amendments to have a significant impact on the consolidated financial statements upon adoption.

In February 2018, the IASB issued amendments to IAS 19 *Employee Benefits*. The amendments 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 are for annual and interim reporting periods beginning on or after January 1, 2019 and are to be applied prospectively. Pollard does not expect the amendments to have a significant impact on the consolidated financial statements upon adoption.

Industry Risks and Uncertainties

Pollard is exposed to numerous risks and uncertainties which are described in this MD&A and Pollard's most recent Annual Information Form dated March 13, 2019, which is available under Pollard's profile on SEDAR (www.sedar.com).

Financial Instruments

Pollard is exposed to financial risks that arise from fluctuations in interest rates and foreign exchange rates and the degree of volatility of these rates, liquidity risk and credit risk. Pollard uses financial instruments, from time to time, to manage these risks.

Pollard's risk management policies are established to identify and analyze the risks, to set appropriate risk limits and controls 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.

Risk Exposure

Currency risk

Pollard sells a significant portion of its products and services to customers in the United States and to 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 Canadian and U.S. dollars, primarily in Euros.

In addition, translation differences arise when foreign currency monetary assets and liabilities are translated at foreign exchange rates that change over time.

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.

Credit risk

Credit risk is the risk of financial loss if a customer or counterpart to a financial instrument fails to meet its financial obligations.

Liquidity risk

Liquidity risk is the risk that Pollard will not be able to meet its financial obligations as they fall due.

Risk Management

Currency risk

Pollard utilizes a number of tools to manage its foreign currency risk including sourcing its manufacturing facilities in the U.S. and sourcing other cost of sales in U.S. dollars.

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 by approximately $0.02 million for year ended December 31, 2018 (2017 - $0.15 million). A 50 basis point strengthening/weakening in the foreign exchange rate between the Canadian dollar and Euro would decrease/increase the income before income taxes due to changes in operating cashflow by approximately $0.08 million for year ended December 31, 2018 (2017 - $0.07 million).

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.

As at December 31, 2018, the amount of financial liabilities denominated in U.S. dollars exceeded the amount of financial assets denominated in U.S. dollars by approximately $36.1 million (2017 - $1.3 million). 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 income taxes of approximately $0.2 million (2017 - $0.01 million).

Pollard also uses financial hedges, including foreign currency contracts, to help manage foreign currency risk. At December 31, 2018, Pollard had no outstanding foreign currency contracts.

<u>Interest rate risk</u>

A 50 basis point decrease/increase in interest rates would result in an increase/decrease in income before income taxes of $0.6 million for the year ended December 31, 2018 (2017 - $0.4 million).

<u>Credit risk</u>

Credit risk on Pollard's accounts receivable is minimized since they are mainly from governments and their agencies and are collected in a relatively short period of time. Credit risk on foreign currency contracts is minimized since the counterparties are restricted to Schedule 1 Canadian financial institutions.

In accordance with IFRS 9, Pollard has applied the expected credit loss model in evaluating the credit risk associated with its accounts receivable. As part of this analysis, Pollard groups its customers into two tranches: government lottery organizations and charitable gaming distribution networks. For sales to government lottery organizations, Pollard has assessed the loss allowance at zero based on the nature of the customer organizations, and no history of losses, collection issues, or significantly overdue receivables, as well as other customer-specific and forward-looking macroeconomic factors. Pollard has performed the same assessment for charitable gaming distribution network customers, resulting in the provision of a loss allowance of $0.2 million, which is netted against accounts receivables.

<u>Liquidity risk</u>

Pollard's approach is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due. Pollard maintains a committed credit facility including up to $160.0 million for its Canadian operations and up to US$12.0 million for its U.S. subsidiaries. At December 31, 2018, the unused balance available for drawdown was $58.9 million (2017 - $34.2 million).

The 2019 requirements for capital expenditures, working capital and dividends are expected to be financed from cash flow provided by operating activities and unused credit facility. Pollard enters into contractual obligations in the normal course of business operations.

Outlook

The lottery industry remains very robust, with continued consumer demand presenting lotteries with the foundation for growing their revenue and proceeds raised for good causes. Showing particularly strong growth is the instant ticket product line. Higher price points, greater prize payouts, varying ticket sizes and play mechanics, all continue to drive higher retail sales and ultimately greater demand for our instant tickets over the long term. We also believe our ancillary and support products for instant tickets will see increased demand. These items, such as iLottery and digital games, loyalty solutions and other related services, also help expand sales of instant tickets creating more opportunities for Pollard.

We believe our first quarter 2019 Adjusted EBITDA will return to expected levels and we anticipate this trend to continue. Orders can vary in the short-term and on a quarter to quarter basis can impact our results. We believe growing our volumes and market share will help mitigate this variability.

Revenue recognition standards and delivery terms can impact when we are able to recognize our instant ticket production in revenue. Over a longer period of time these variations are lessened but over the short term it can have an impact on our financial results. We anticipate the majority of the instant ticket volumes that were deferred at the end of 2018 to be recognized in the first quarter of 2019.

Much of our revenue is based on long term contracts and our current contract portfolio is well positioned with no large contracts up for expiry in 2019. We renewed or extended all our major contracts that came due in 2018. Many of our contracts allow the lottery to choose from multiple suppliers, which provides Pollard the opportunity to win market share from other suppliers by providing successful products for the lottery. Over the past few years this has been one of the keystones of our growth and we will continue to focus on this strategy in 2019. We have previously disclosed that there were a number of large instant ticket contracts that came up for bid in 2018 where Pollard was not a major supplier. These contract bid processes remain underway as we enter 2019.

The ability to develop and sell proprietary products and services is a key success factor for Pollard. Our specialty instant tickets such as Scratch FX® and laminated products such as PlayBooks® have been very important in supporting lotteries in their growth initiatives and we are planning to continue to invest in the resources to develop more innovative products and services. Ticket features such as Clear Play™ and the development and roll out of our PlayOn™ player engagement solution are examples of the development necessary to remain partner of choice.

We expect our first quarter 2019 revenue to be boosted due to the deferral of completed tickets from 2018 being delivered in the first three months of 2019. This additional sales volume will supplement the revenue from sales of tickets produced in the first quarter.

We anticipate our 2019 CAPEX to be at similar levels expended in 2018 once adjusted for the full year of ownership of our recent acquisitions. Included in our planned capital expenditures are new eGaming machines for our Diamond Game and Oasis operations. These expenditures can vary depending on timing of new machine placements and new contract wins. We expect our operations to generate strong free cash flow after consideration of CAPEX and expect to use these funds to pay down bank debt and to contribute to any additional acquisitions.

Charitable gaming remains steady, with ongoing orders from private distributors supporting pull-tab and bingo paper sales. Third party data has indicated some retail sales growth of these products which is a positive sign. The charitable gaming business generates strong cash flow, as it requires minimal capital investment.

In early 2018 we increased our instant ticket capacity by recommissioning our original press line in Ypsilanti. We are in the process of adding supplementary equipment to this original press line which will add incremental capacity in 2019 to help ensure we will have the capability to effectively and efficiently handle future sales growth.

In January 2019, the United States Department of Justice ("DOJ") issued a new interpretation of its previous 2011 interpretation relating to the applicability of the Wire Act to internet gaming including operations conducted by state lotteries. The 2011 interpretation had determined that the Wire Act, which prohibited gambling or associated gambling activity from utilizing interstate wire communication facilities, including the internet, only applied to sports betting. As a result, a number of state lotteries initiated iLottery businesses to sell their lottery products over the internet within each of their own states to local residents. The new January 2019 interpretation reverses this view and, in effect, indicates the Wire Act is not restricted to just sports gambling. The DOJ granted an initial 90-day grace period from the date of release of their ruling (January 14, 2019) for various organizations to assess the impact. Subsequently the DOJ granted an additional 60-day grace period for a total of 150 days. This new interpretation reverses the 2011 ruling and raises uncertainty as to how the Wire Act will be applied to existing and future gaming activities including those run by state sponsored lotteries.

On February 15, 2019, Pollard Banknote Limited and NeoPollard Interactive LLC. filed a motion with the United States District Court for the District of New Hampshire ("District Court") requesting a formal declatory judgement clarifying that the Wire Act only applies to sports betting. Simultaneously, the State of New Hampshire also filed a motion with the District Court requesting the same definitive clarification.

We believe the January 2019 DOJ interpretation is incorrect on a number of key issues relating to existing and long-time legacy lottery gaming products and we are confident a definitive ruling from the District Court will reconfirm that iLottery and other gaming operations conducted by state lotteries are not subject to the Wire Act and can therefore continue to operate as they have for many years. Notwithstanding the uncertainty brought on with the Department of Justice reinterpretation, interest in iLottery operations continues to rise among many lottery organizations. We expect opportunities to provide these services to lotteries will continue to grow and are actively pursuing a number of them in 2019.

The integration of our recently acquired Schafer retail merchandising business is proceeding as expected and we are looking for opportunities to maximize instant ticket sales through innovative use of point of sale dispensers. The integration of our International Gamco business with our American Games business is also progressing well. At the same time, Diamond Game is pursuing a number of new market opportunities for its eGaming machines and will be increasing the number of machines in developing markets.

Our strategic vision includes pursuing acquisitions to expand our product offerings and we are actively looking at a number of tactical additions that would further enhance Pollard's position as partner of choice for the lottery and charitable gaming industries.

Disclosure Controls and Procedures

Under National Instrument 52-109, "Certification of Disclosure in Issuers' Annual and Interim Filings," issuers are required to document the conclusions of the Chief Executive Officer and Chief Financial Officer (the "Certifying Officers") regarding the design and effectiveness of the disclosure controls and procedures. Pollard's management, with the participation of the Certifying Officers of Pollard, has concluded that the disclosure controls and procedures as defined in National Instrument 52-109 are designed appropriately and are effective at providing reasonable assurance of achieving the disclosure objectives.

Pollard has limited its design of disclosure controls and procedures to exclude controls, policies and procedures of Schafer, as it was acquired not more than 365 days before the end of the financial period to which this MD&A relates.

Internal Controls over Financial Reporting

Under National Instrument 52-109, "Certification of Disclosure in Issuers' Annual and Interim Filings," issuers are required to document the conclusions of the Certifying Officers regarding the design and effectiveness of the internal controls over financial reporting. Management used the Internal Control – Integrated Framework published by the Committee of Sponsoring Organizations of the Treadway Commission (COSO 2013) as the control framework in designing its internal controls over financial reporting. Pollard's management, with the participation of the Certifying Officers of Pollard, has concluded that the internal controls over financial reporting as defined in National Instrument 52-109 are designed appropriately and are effective at providing reasonable assurance of achieving the financial reporting objectives.

Pollard has limited its design of ICFR to exclude controls, policies and procedures of Schafer, as it was acquired not more than 365 days before the end of the financial period to which this MD&A relates.

No changes were made in Pollard's internal control over financial reporting during the year ended December 31, 2018, that have materially affected, or are reasonably likely to materially affect, Pollard's internal control over financial reporting.

Additional Information

Shares of Pollard Banknote Limited are traded on the Toronto Stock Exchange under the symbol PBL.

Additional information relating to Pollard, including the Audited Consolidated Financial Statements and the Annual Information Form for the year ended December 31, 2018, is available on SEDAR at www.sedar.com.

Pollard Banknote Limited
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Management's Report

The accompanying consolidated financial statements and all the information contained in the annual report of Pollard Banknote Limited ("Pollard") are the responsibility of management and have been approved by the Board of Directors of Pollard. Financial and operating data elsewhere in the annual report is consistent with the information contained in the financial statements. The financial statements and all other information have been prepared by management in accordance with Canadian generally accepted accounting principles. The financial statements include some amounts and assumptions based on management's best estimates which have been derived with careful judgment.

In fulfilling its responsibilities, management of Pollard has developed and maintains a system of internal accounting controls. These controls are designed to ensure that the financial records are reliable for preparing the financial statements. The Board of Directors of Pollard carries out its responsibility for the financial statements through the Audit Committee. The Audit Committee reviews Pollard's annual consolidated financial statements and recommends their approval by the Board of Directors. The auditors have full access to the Audit Committee with and without management present.

The consolidated financial statements have been audited by KPMG LLP Chartered Accountants, whose opinion is contained in this annual report.

"John Pollard"	*"Robert Rose"*
JOHN POLLARD Co-Chief Executive Officer	ROBERT ROSE Chief Financial Officer

March 13, 2019

Consolidated Financial Statements of

POLLARD BANKNOTE LIMITED

Years ended December 31, 2018 and 2017

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INDEPENDENT AUDITORS' REPORT

To the Shareholders of Pollard Banknote Limited

Opinion

We have audited the consolidated financial statements of Pollard Banknote Limited (the Entity), which comprise the consolidated statements of financial position as at December 31, 2018 and December 31, 2017, the consolidated statements of income, comprehensive income, changes in equity and cash flows for the years then ended, and notes to the financial statements, including a summary of significant accounting policies (hereinafter referred to as the "financial statements").

In our opinion, the accompanying financial statements present fairly, in all material respects, the consolidated financial position of the Entity as at December 31, 2018 and December 31, 2017, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for Opinion

We conducted our audit in accordance with Canadian generally accepted auditing standards. Our responsibilities under those standards are further described in the "Auditors' Responsibilities for the Audit of the Financial Statements" section of our auditors' report.

We are independent of the Entity in accordance with the ethical requirements that are relevant to our audit of the financial statements in Canada and we have fulfilled our other ethical responsibilities in accordance with these requirements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our opinion.

Other Information

Management is responsible for the other information. Other information comprises:

- the information included in Management's Discussion and Analysis filed with the relevant Canadian Securities Commissions.
- the information, other than the financial statements and the auditors' report thereon, included in a document likely to be entitled "Annual Report 2018".

Our opinion on the financial statements does not cover the other information and we do not and will not express any form of assurance conclusion thereon.

In connection with our audit of the financial statements, our responsibility is to read the other information identified above and, in doing so, consider whether the other information is materially inconsistent with the financial statements or our knowledge obtained in the audit, and remain alert for indications that the other information appears to be materially misstated.

We obtained the information included in Management's Discussion and Analysis filed with the relevant Canadian Securities Commissions, as at the date of this auditors' report. If, based on the work we have performed on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact in the auditors' report.

We have nothing to report in this regard.

The information, other than the financial statements and the auditors' report thereon, included in a document likely to be entitled "Annual Report 2018" is expected to be made available to us after the date of this auditors' report. If, based on the work we will perform on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact to those charged with governance.

Responsibilities of Management and Those Charged with Governance for the Financial Statements

Management is responsible for the preparation and fair presentation of the financial statements in accordance with IFRS, and for such internal control as management determines is necessary to enable the preparation of financial statements that are free from material misstatement, whether due to fraud or error.

In preparing the financial statements, management is responsible for assessing the Entity's ability to continue as a going concern, disclosing as applicable, matters related to going concern and using the going concern basis of accounting unless management either intends to liquidate the Entity or to cease operations, or has no realistic alternative but to do so.

Those charged with governance are responsible for overseeing the Entity's financial reporting process.

Auditors' Responsibilities for the Audit of the Financial Statements

Our objectives are to obtain reasonable assurance about whether the financial statements as a whole are free from material misstatement, whether due to fraud or error, and to issue an auditors' report that includes our opinion.

Reasonable assurance is a high level of assurance, but is not a guarantee that an audit conducted in accordance with Canadian generally accepted auditing standards will always detect a material misstatement when it exists.

Misstatements can arise from fraud or error and are considered material if, individually or in the aggregate, they could reasonably be expected to influence the economic decisions of users taken on the basis of the financial statements.

As part of an audit in accordance with Canadian generally accepted auditing standards, we exercise professional judgment and maintain professional skepticism throughout the audit.

We also:

- Identify and assess the risks of material misstatement of the financial statements, whether due to fraud or error, design and perform audit procedures responsive to those risks, and obtain audit evidence that is sufficient and appropriate to provide a basis for our opinion.

  The risk of not detecting a material misstatement resulting from fraud is higher than for one resulting from error, as fraud may involve collusion, forgery, intentional omissions, misrepresentations, or the override of internal control.

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Entity's internal control.

- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.

- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Entity to cease to continue as a going concern.

- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.

- Communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.

- Provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.

- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group Entity to express an opinion on the financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

KPMG LLP

Chartered Professional Accountants

The engagement partner on the audit resulting in this auditors' report is Robert Kowalchuk.

Winnipeg, Canada

March 13, 2019

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

	December 31, 2018	December 31, 2017*
Assets		
Current assets		
Cash	$ 11,174	$ 5,603
Restricted cash	10,158	5,780
Accounts receivable	34,675	40,749
Inventories (note 7)	45,353	32,008
Prepaid expenses and deposits	6,943	6,331
Income tax receivable	2,279	–
Total current assets	110,582	90,471
Non-current assets		
Property, plant and equipment (note 8)	71,606	54,319
Equity investment (note 9)	1,164	877
Goodwill (note 10)	69,667	51,768
Intangible assets (note 11)	50,086	27,746
Deferred income taxes (note 12)	2,495	3,093
Total non-current assets	195,018	137,803
Total assets	$ 305,600	$ 228,274

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

	December 31, 2018	December 31, 2017*
Liabilities and Shareholders' Equity		
Current liabilities		
Accounts payable and accrued liabilities	$ 43,058	$ 36,766
Dividends payable	768	706
Income taxes payable	408	3,373
Contract liabilities (note 18)	814	702
Current portion long-term debt (note 13)	40	784
Current portion subordinated debt (note 14)	–	3,585
Total current liabilities	45,088	45,916
Non-current liabilities		
Long-term debt (note 13)	115,756	83,771
Subordinated debt (note 14)	–	13,149
Contract liabilities (note 18)	43	789
Other non-current liabilities	466	753
Pension liability (note 15)	20,357	22,959
Deferred income taxes (note 12)	6,252	3,368
Total non-current liabilities	142,874	124,789
Shareholders' equity		
Share capital (note 16)	108,605	73,209
Reserves	12,698	2,965
Deficit	(3,665)	(18,605)
Total shareholders' equity	117,638	57,569
Commitments and contingencies (note 17)		
Total liabilities and shareholders' equity	$ 305,600	$ 228,274

* Pollard has initially applied IFRS 15 *Revenue from Contracts with Customers* and IFRS 9 *Financial Instruments* at January 1, 2018. Under the transition methods chosen, comparative information has not been restated. See note 3.

See accompanying notes to consolidated financial statements.

On behalf of the Board:

"Dave Brown" Director

"John Pollard" Director

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

Years ended December 31

		2018		2017*
Sales (note 18)	$	331,868	$	285,654
Cost of sales		256,131		219,916
Gross profit		75,737		65,738
Administration		32,154		28,609
Selling		13,395		9,412
Other expenses (note 19)		464		675
Income from operations		29,724		27,042
Finance costs (note 20)		9,836		4,172
Finance income (note 20)		(881)		(1,104)
Income before income taxes		20,769		23,974
Income taxes (note 12)				
Current		5,175		7,902
Deferred (reduction)		742		(712)
		5,917		7,190
Net income	$	14,852	$	16,784
Net income per share (basic) (note 21)	$	0.58	$	0.71
Net income per share (diluted) (note 21)	$	0.58	$	0.71

* Pollard has initially applied IFRS 15 *Revenue from Contracts with Customers* and IFRS 9 *Financial Instruments* at January 1, 2018. Under the transition methods chosen, comparative information has not been restated. See note 3.

See accompanying notes to consolidated financial statements.

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

Years ended December 31

		2018		2017*
Net income	$	14,852	$	16,784
Other comprehensive income (loss)				
Items that are or may be reclassified to profit and loss				
Foreign currency translation differences – foreign operations		9,733		(952)
Items that will never be reclassified to profit and loss				
Defined benefit plans remeasurements, net of income tax (reduction) (note 12 & note 15)		2,720		(7,397)
Other comprehensive income (loss)		12,453		(8,349)
Comprehensive income	$	27,305	$	8,435

* Pollard has initially applied IFRS 15 *Revenue from Contracts with Customers* and IFRS 9 *Financial Instruments* at January 1, 2018. Under the transition methods chosen, comparative information has not been restated. See note 3.

See accompanying notes to consolidated financial statements.

Pollard Banknote Limited

Consolidated Statements of Changes in Equity

(*In thousands of Canadian dollars*)

Year ended December 31, 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 (note 3)		–	–	332	332
Adjusted balance at January 1, 2018		73,209	2,965	(18,273)	57,901
Net income		–	–	14,852	14,852
Other comprehensive income					
Foreign currency translation differences – foreign operations		–	9,733	–	9,733
Defined benefit plans remeasurements, net of income tax (note 12 & note 15)		–	–	2,720	2,720
Total other comprehensive income	$	–	9,733	2,720	12,453
Total comprehensive income	$	–	9,733	17,572	27,305
Issue of common shares (note 16)		35,396	–	–	35,396
Share based compensation		–	–	110	110
Dividends to owners of Pollard Banknote Limited		–	–	(3,074)	(3,074)
Balance at December 31, 2018	$	108,605	12,698	(3,665)	117,638

Year ended December 31, 2017

		Share capital	Translation reserve	Deficit	Total equity
Balance at January 1, 2017	$	73,209	3,917	(25,289)	51,837
Net income		–	–	16,784	16,784
Other comprehensive loss					
Foreign currency translation differences – foreign operations		–	(952)	–	(952)
Defined benefit plans remeasurements, net of income tax reduction		–	–	(7,397)	(7,397)
Total other comprehensive loss	$	–	(952)	(7,397)	(8,349)
Total comprehensive income (loss)	$	–	(952)	9,387	8,435
Share based compensation		–	–	122	122
Dividends to owners of Pollard Banknote Limited		–	–	(2,825)	(2,825)
Balance at December 31, 2017	$	73,209	2,965	(18,605)	57,569

See accompanying notes to consolidated financial statements.

Pollard Banknote Limited
Consolidated Statements of Cash Flows
(*In thousands of Canadian dollars*)

Years ended December 31

	2018	2017*
Cash increase (decrease)		
Operating activities		
Net income	$ 14,852	$ 16,784
Adjustments		
Income taxes	5,917	7,190
Amortization and depreciation	18,017	13,155
Interest expense	4,243	3,962
Unrealized foreign exchange loss (gain)	4,533	(1,436)
Loss on sale of property, plant and equipment	–	74
Loss on equity investment (note 9)	2,631	1,727
Pension expense (note 15)	6,449	5,082
Contract liabilities (note 18)	(773)	(163)
Interest paid	(4,484)	(3,699)
Income tax paid	(10,187)	(6,127)
Pension contribution	(5,534)	(5,312)
Change in non-cash operating working capital (note 23)	3,997	(2,879)
	39,661	28,358
Investing activities		
Additions to property, plant and equipment (note 8)	(15,090)	(6,948)
Acquisition of Integrity Bingo	–	(502)
Acquisition of INNOVA Gaming Group, Inc. (note 6)	–	(39,318)
Acquisition of International Gamco, Inc. (note 6)	(21,558)	–
Acquisition of Schafer (note 6)	(30,447)	–
Equity investment (note 9)	(2,842)	(2,204)
Additions to intangible assets (note 11)	(7,145)	(2,246)
	(77,082)	(51,218)
Financing activities		
Proceeds from issue of share capital (note 16)	35,396	–
Net proceeds from long-term debt (note 13)	27,878	13,520
Net proceeds from (repayments of) subordinated debt	(16,734)	10,602
Change in other non-current liabilities	(328)	383
Deferred financing charges paid (note 13)	(561)	(342)
Change in dividend payable	62	–
Dividends paid	(3,074)	(2,825)
	42,639	21,338
Foreign exchange gain (loss) on cash held in foreign currency	353	(375)
Change in cash position	5,571	(1,897)
Cash position, beginning of year	5,603	7,500
Cash position, end of year	$ 11,174	$ 5,603

* Pollard has initially applied IFRS 15 *Revenue from Contracts with Customers* and IFRS 9 *Financial Instruments* at January 1, 2018. Under the transition methods chosen, comparative information has not been restated. See note 3.

See accompanying notes to consolidated 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 consolidated financial statements of Pollard as at and for the year ended December 31, 2018, 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. On February 1, 2018, Pollard completed a share offering, which reduced Equities' ownership to approximately 67.5% of Pollard's increased outstanding share amount. Further details are provided in note 16.

The operations of International Gamco, Inc. ("Gamco"), acquired during the first quarter of 2018, are included in the consolidated financial statements from February 1, 2018. Further details are provided in note 6.

The operations of Schafer Systems (2018) Inc., acquired during the fourth quarter of 2018, are included in the consolidated financial statements from October 31, 2018. Further details are provided in note 6.

2. Basis of preparation:

(a) Statement of compliance:

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards ("IFRS").

On March 13, 2019, Pollard's Board of Directors approved these consolidated financial statements.

(b) Basis of preparation:

These consolidated financial statements have been prepared on a historical cost basis, except for the following material items in the statement of financial position:

- The pension liability is recognized as the net total of the fair value of plan assets less the present value of the defined benefit obligation.

2. Basis of preparation (continued):

These statements are presented in Canadian dollars, Pollard's functional currency, and all values are rounded to the nearest thousand (except share and per share amounts) unless otherwise indicated.

(c) Use of estimates and judgments:

The preparation of the consolidated 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. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognized prospectively. Actual results may differ from these estimates.

Information about judgments, assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment within the next period are as follows:

Impairment of goodwill:

Pollard determines whether goodwill is impaired at least on an annual basis. This requires an estimation of the "value in use" or "fair value less costs to sell" of the cash-generating units ("CGUs") to which goodwill is allocated. Estimating a value in use requires Pollard to make an estimate of the expected future cash flows from the CGUs. Pollard also chooses a suitable discount rate in order to calculate the present value of those cash flows. Judgment is required in determining the level at which to test goodwill, including the grouping of assets that generate cash inflows. Further details are provided in note 10.

Employee future benefits:

Accounting for defined benefit plans requires Pollard to use actuarial assumptions. These assumptions include the discount rate and the rate of compensation increases. These assumptions depend on underlying factors such as economic conditions, government regulations, investment performance, employee demographics and mortality rates. Further details are provided in note 15.

Income taxes:

Pollard is required to evaluate the recoverability of deferred income tax assets. This requires an estimate of Pollard's ability to utilize the underlying future income tax deductions against future taxable income before they expire. In order to evaluate the recoverability of these deferred income tax assets, Pollard must estimate future taxable income. Further details are provided in note 12.

2. Basis of preparation (continued):

Acquisition accounting:

For acquisition accounting purposes, all identifiable assets and liabilities acquired in a business combination are recognized at fair value at the date of acquisition. Estimates are used to calculate the fair value of these assets and liabilities.

3. Accounting standards implemented in 2018:

(a) Revenue from contracts with customers:

In May 2014, the International Accounting Standards Board ("IASB") issued IFRS 15 *Revenue from Contracts with Customers.* The new standard specifies a single, five-step revenue recognition model that requires entities to recognize revenue when control of the promised goods or services is transferred to customers at an amount that reflects the consideration to which the entity expects to be entitled to in exchange for those goods or services. The standard also requires more informative, relevant disclosures. IFRS 15 supersedes IAS 11 *Construction Contracts* and IAS 18 *Revenue*.

Under certain contracts, Pollard is compensated for its products based on its customers' sales of those products at retail. Prior to IFRS 15, Pollard recognized sales under these contracts at the time the product was sold at retail. Under IFRS 15 Pollard has concluded that control transfers to its customers at delivery of the product to the customer. This will accelerate the recognition of sales under these contracts to the time of receipt of shipment. Pollard's sales under these contracts could vary year over year depending on the timing of shipments.

Pollard adopted the new standard retrospectively, with the cumulative effect of initially applying the standard recognized at January 1, 2018, in opening deficit. The impact of transition to IFRS 15 on opening deficit at January 1, 2018, was a reduction of $332, net of $123 of income taxes. The impact on the statement of financial position included an increase in accounts receivable of $3,260, a decrease in inventories of $2,805 and an increase in the deferred income tax liability of $123.

For the year ended December 31, 2018, Pollard's revenue increased by $3,052 and cost of sales increased by $2,104 as a result of the accelerated revenue recognition point on contracts where Pollard is compensated for its products based on its customers' sales at retail. As a result of the transitional adjustment, Pollard's sales in the year ended December 31, 2018, decreased by $3,184 and cost of sales decreased by $2,789, as these sales were previously recorded in opening deficit upon adoption at January 1, 2018.

As a result of the adoption of IFRS 15, Pollard's accounting policies for *Revenue from Contracts with Customers* have been updated in note 4 and applied from January 1, 2018. Additional revenue disclosures are presented in note 18.

(In thousands of Canadian dollars, except for share amounts)

3. Accounting standards implemented in 2018 (continued):

(b) Financial instruments:

In July 2014, the IASB issued IFRS 9 *Financial Instruments*, which replaced IAS 39 *Financial Instruments: Recognition and Measurement.* IFRS 9 includes revised guidance on the classification and measurement of financial instruments, a new expected credit loss model for calculating impairment on financial assets and new general hedge accounting requirements. It also carries forward the guidance on recognition and derecognition of financial instruments from IAS 39.

Pollard adopted the new standard retrospectively. The adoption of IFRS 9 did not result in any transition adjustments being recognized as at January 1, 2018. The adoption of the new standard had no material impact on Pollard's consolidated financial statements.

The standard contains three classification categories for financial assets: measured at amortized cost, fair value through other comprehensive income ("FVOCI") and fair value through profit or loss ("FVTPL"). The classification of financial assets under IFRS 9 is based on the business model in which a financial asset is managed and its contractual cash flow characteristics. The standard eliminates the previous IAS 39 categories of held to maturity, loans and receivables, and available for sale. Most of the requirements in IAS 39 for classification and measurement of financial liabilities were carried forward in IFRS 9; as a result, the adoption did not change Pollard's accounting policies for financial liabilities. The classification changes for each class of Pollard's financial assets and financial liabilities upon adoption at January 1, 2018 are summarized in the following table:

Financial assets and liabilities	IAS 39	IFRS 9		IAS 39/IFRS 9 carrying value
Cash	Loans and receivables	Amortized cost	$	5,603
Restricted cash	Loans and receivables	Amortized cost		5,780
Accounts receivable*	Loans and receivables	Amortized cost		44,009
Accounts payable and accrued liabilities	Other financial liabilities	Amortized cost		(36,766)
Other non-current liabilities	Other financial liabilities	Amortized cost		(753)
Dividends payable	Other financial liabilities	Amortized cost		(706)
Long-term debt	Other financial liabilities	Amortized cost		(83,771)
Subordinated debt	Other financial liabilities	Amortized cost		(13,149)

*January 1, 2018 figure includes the impact of the transitional adjustment booked to opening deficit upon adoption of IFRS 15 of $3,260. Further details are provided in note 3(a).

As a result of the adoption of IFRS 9, Pollard's accounting policies for *Financial Instruments* have been updated in note 4 and applied from January 1, 2018. Additional IFRS 9 disclosures are presented in note 27 and note 28.

(In thousands of Canadian dollars, except for share amounts)

3. Accounting standards implemented in 2018 (continued):

(c) Share-based payments:

In June 2016, the IASB issued amendments to IAS 2 *Share-Based Payments.* The amendments clarify how to account for certain types of share-based payment transactions. These amendments had no material impact on the consolidated financial statements.

(d) Foreign currency transactions and advance consideration:

In December 2016, the IASB issued IFRIC Interpretation 22 *Foreign Currency Transactions and Advance Consideration.* The Interpretation clarifies the date of the transaction for the purposes of determining the exchange rate to use on initial recognition of the related asset, expense or income is the date on which an entity initially recognizes the non-monetary asset or non-monetary liability arising from the payment or receipt of advance consideration. The Interpretation had no material impact on the consolidated financial statements.

4. Significant accounting policies:

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements, except as described in note 3.

(a) Principles of consolidation:

These consolidated financial statements include the accounts of Pollard and all its subsidiaries. Subsidiaries are entities which are under Pollard's control, where control is defined as the power to govern financial and operating policies of an entity so as to obtain benefits from its activities. Pollard holds 100% of the voting rights in, and therefore controls, its subsidiaries.

Significant subsidiaries:	Percent Ownership Interest	
	December 31, 2018	December 31, 2017
Pollard Holdings, Inc.	100	100
Pollard (U.S.) Ltd.	100	100
Pollard Games, Inc.	100	100
Pollard iLottery Inc.	100	100
Diamond Game Enterprises	100	100
Diamond Game Enterprises Canada ULC	100	100
International Gamco, Inc.	100	–
Schafer Systems (2018) Inc.	100	–

4. Significant accounting policies (continued):

Pollard has entered into a contractual joint agreement with Neogames S.à r.l. for the operation of iLottery gaming for the Michigan Lottery. As such Pollard has recognized in relation to its interest in the joint operation: 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.

Pollard, in conjunction with NeoGames US, LLP, established NeoPollard Interactive LLC ("NPI"). Pollard accounts for its investment in NPI as a joint venture. Under the equity method of accounting, Pollard recognizes its share of the income, expenses and equity movements of NPI.

All inter-company balances and transactions, and any unrealized income and expenses arising from inter-company transactions, have been eliminated.

(b) Business combinations:

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the fair value of the assets given, equity instruments and liabilities incurred or assumed at the date of exchange. Acquisition costs for business combinations are expensed as incurred and included in administration expenses. Identifiable assets acquired and liabilities assumed are measured at their fair value at the acquisition date. The excess of the fair value of consideration transferred over the fair value of the identifiable net assets acquired is recorded as goodwill.

(c) Restricted cash:

Pollard, under certain contractual arrangements, controls cash that is not available for use. Pollard records an equal, offsetting liability classified within accounts payable and accrued liabilities. Restricted cash includes player deposits held for the benefit of Pollard's iLottery customer, in addition to funds held for security purposes and certain contractual liabilities. Pollard has excluded changes in the restricted cash and related liability from its calculation of the change in cash position in the statements of cash flows.

(d) Revenue recognition:

Pollard previously recognized revenue under IAS 18 when persuasive evidence of an arrangement existed, significant risk and benefits of ownership were transferred, the sales price to the customer was fixed or was determined, and collection of the resulting receivable was reasonably assured. The significant risks of ownership and benefits of ownership were normally transferred in accordance with the shipping terms agreed to with the customer.

4. Significant accounting policies (continued):

Under IFRS 15 *Revenue from Contracts with Customers*, revenue is recognized when a customer obtains control of the goods or services. Pollard determines revenue recognition through the following steps: a) identification of the contract with a customer, b) identification of the performance obligations in the contract, c) determination of the transaction price, d) allocation of the transaction price to the performance obligations in the contract and e) recognition of revenue when Pollard satisfies a performance obligation.

Many of Pollard's contracts have a single performance obligation, including the sale of instant tickets and related products, pull-tab (or break-open) tickets, bingo paper, pull-tab vending machines, ancillary products such as pull-tab counting machines and gaming machines. The single performance obligation in these contracts is the promise to transfer the individual goods. Revenue is recognized at a point in time when the customer obtains control of a product, which typically takes place when legal title and physical possession of the product is transferred to the customer. These conditions are usually fulfilled upon delivery. However, under certain contracts, Pollard is compensated for its products based on its customers' sales of those products at retail. Prior to IFRS 15, Pollard recognized sales under these contracts at the time the product was sold at retail. Under IFRS 15, Pollard has concluded that control transfers to its customers at delivery of the product to the customer. This accelerates the recognition of sales under these contracts to the time of receipt of shipment. Pollard's sales under these contracts could vary year over year depending on the timing of shipments.

Certain Pollard contracts include multiple performance obligations, including license and royalty sales, iLottery services, loyalty programs, digital and lottery management services, training and consulting. Where such arrangements exist, the transaction price is allocated to the performance obligations based upon the relative fair value of the various elements. The fair values of each element are determined based on the current market price of each of the elements when sold separately. Revenue is then recognized upon satisfaction of each performance obligation. Where Pollard provides software and related infrastructure, revenue is recognized over time based on the relevant measure of progress of the asset being transferred to the customer.

Pollard earns revenue from leasing gaming machines and other equipment, and capitalizes the costs of installing gaming equipment. Revenue from the provision of gaming services is generally recognized as a daily fee or as a percentage of revenue generated by the gaming machines. Product support services, maintenance and periodic upgrades revenue is recognized over time as the related services are performed.

Contract liabilities consist of customer advances for services to be rendered in the future and is recognized as income in future periods. Labour costs associated with performing routine maintenance on participating gaming machines is expensed as incurred and included in cost of sales.

4. Significant accounting policies (continued):

Volume rebates are accrued and recorded as a reduction to sales based on historical experience and management's expectations regarding sales volume.

(e) Inventories:

Raw materials, work-in-process and finished goods are valued at the lower of cost and net realizable value. The cost of raw material inventory is based on its weighted average cost and includes all costs incurred to acquire the materials. In addition to the direct costs of conversion, the cost of work-in-process and finished goods, which Pollard manufactures, also includes an appropriate share of production overheads based on operating capacity.

Net realizable value is the estimated selling price in the ordinary course of business, less the estimated costs of completion.

(f) Goodwill:

Goodwill is comprised of the excess sale price over the underlying carrying amount of the net assets sold as at August 5, 2005, as part of the 26.7% of Pollard sold in conjunction with the Initial Public Offering ("IPO") and the excess fair value of the consideration transferred over the fair value of the identifiable net assets acquired of Pollard's subsidiaries. Goodwill is not amortized but is subject to an annual impairment test to ensure its recoverable value remains greater than, or equal to, book value.

(g) Intangible assets:

Deferred development

Development expenditures are recognized as an intangible asset only if Pollard can demonstrate that the development costs can be measured reliably, the product is technically and commercially feasible, future economic benefits are probable and Pollard has sufficient resources to complete development and to use or sell the asset. The expenditures capitalized include the cost of materials, direct labour and related fringes that are directly attributable to preparing the asset for its intended use and borrowing costs incurred in respect of qualifying assets. Other development expenditures are expensed as incurred.

Capitalized development expenditures are measured at cost less accumulated amortization and accumulated impairment losses.

4. Significant accounting policies (continued):

Computer software and licenses

Computer software consists of the cost of acquiring, developing and implementing these systems. Cost of implementation include third party costs as well as direct labour and related fringes attributable to the asset. Minimum license fees incurred in connection with our licensing agreements for our use of third-party brands are capitalized and amortized over the estimated life of the asset.

Capitalized computer software costs and licenses are measured at cost less accumulated amortization and accumulated impairment losses.

Customer assets and patents

Customer assets and patents that have finite useful lives are measured at cost less accumulated amortization and accumulated impairment losses.

Intangible assets, with finite useful lives, are amortized, on a straight-line basis, over their estimated useful lives as follows:

Asset	Rate
Customer assets	7 to 16 years
Patents	Term of patent
Computer software and licenses	3 to 10 years or term of license
Deferred development	3 to 9 years

Amortization methods, estimated useful lives and residual value are reviewed each annual reporting date and adjusted prospectively if appropriate.

Trademarks, trade names and brands

Trademarks, trade names and brands have been deemed to have an indefinite life and are not amortized. For purposes of impairment testing, the fair value of the trademarks, trade names and brands are determined using the relief from royalty method.

4. Significant accounting policies (continued):

(h) Property, plant and equipment:

Property, plant and equipment ("PP&E") are stated at cost less investment tax credits (including SR&ED credits), accumulated depreciation and accumulated impairment losses. Cost includes expenditures that are directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials, direct labour and related fringes, other costs directly attributable to bringing the assets to working condition for their intended use and borrowing costs incurred in respect to qualifying assets. Major spare parts are treated as PP&E when they have a useful life greater than a year. Once major spare parts are put in service, they are transferred into equipment and amortized accordingly.

An item of PP&E is derecognized upon disposal or when no future economic benefits are expected from its use or disposal. The gain or loss on disposal of an item of PP&E is determined by comparing the proceeds from disposal with the carrying value of the PP&E and is recognized in the statement of income on a net basis.

The cost of each component of an item of PP&E is depreciated over its estimated useful life on a straight-line basis, commencing the date it is ready for use. Land is not depreciated. The estimated useful lives for the current and comparative periods are as follows:

Asset	Rate
Buildings	10 to 39 years
Leasehold improvements	Term of lease
Equipment	2 to 11 years
Charitable gaming machines	3 to 8 years
Furniture, fixtures and computers	3 to 9 years

Depreciation methods, useful lives and residual values are reviewed each annual reporting date and adjusted prospectively if appropriate.

The carrying value of property, plant and equipment are reviewed for impairment whenever events or changes in circumstances indicate that the carrying amount of an asset may not be recoverable.

4. Significant accounting policies (continued):

(i) Investment in joint venture:

A joint venture is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the net assets of the arrangement, rather than rights to the assets and obligations for the liabilities. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require consent of both parties.

The consolidated financial statements include Pollard's share of the income and expenses and equity movements of the entity accounted for under the equity method of accounting.

(j) Investment in joint operation:

A joint operation is a joint arrangement whereby the parties that have joint control of the arrangement have rights to the assets, and obligations for the liabilities, relating to the arrangement. Joint control is the contractually agreed sharing of control of an arrangement, which exists only when decisions about the relevant activities require consent of both parties.

The consolidated financial statements include Pollard's interest in the Michigan Lottery iLottery joint operations: 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.

(k) Financial instruments:

IFRS 9 *Financial Instruments*, replaced the previous guidance in IAS 39 *Financial Instruments: Recognition and Measurement.* IFRS 9 includes revised guidance on the classification and measurement of financial instruments, a new expected credit loss model for calculating impairment on financial assets and new general hedge accounting requirements.

Financial assets are initially measured at fair value. On initial recognition, Pollard classifies its financial assets at either amortized cost, FVOCI or FVTPL, depending on its business model for managing the financial assets and the contractual cash flow characteristics of the financial assets. Financial assets are not reclassified subsequent to their initial recognition, unless Pollard changes its business model for managing financial assets. Financial liabilities are classified at amortized cost.

A financial asset is classified as measured at amortized cost if it meets both of the following conditions: a) the asset is held within a business model whose objective is to hold assets to collect contractual cash flows and b) the contractual terms of the financial asset give rise on specified dates to cash flows that are solely payments of principal and interest on the principal outstanding.

4. Significant accounting policies (continued):

A financial asset is classified as measured at FVOCI if it meets both of the following conditions: a) it is held within a business model whose objective is achieved by both collecting contractual cash flows and selling financial assets and b) its contractual terms give rise on specified dates to cash flows that are solely payments of principal and interest on the principal amount outstanding.

All financial assets not classified as measured at amortized cost or FVOCI are measured at FVTPL. This includes all derivative financial assets. On initial recognition, Pollard may irrevocably designate a financial asset that otherwise meets the requirements to be measured at amortized cost or at FVOCI as FVTPL, if doing so eliminates or significantly reduces an accounting mismatch that would otherwise arise.

Hedge accounting

Pollard has adopted the new general hedging accounting model in IFRS 9. 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.

From time to time, Pollard enters into hedging arrangements in order to mitigate this exposure to foreign exchange fluctuations. Pollard determines the existence of an economic relationship between the hedging instrument and hedged item based on the currency, amount and timing of their respective cash flows. An assessment is made whether the derivative designated in each hedging relationship is expected to be and has been effective in offsetting changes in cash flows of the hedged item using the hypothetical derivative method.

The fair value of each contract is included on the consolidated balance sheet as either a financial asset or liability. Changes in fair value are recorded in either other comprehensive income or the consolidated statement of income, depending on the nature of the hedged item.

If the hedge no longer meets the criteria for hedge accounting or the hedging instrument is sold, expires, is terminated or is exercised, then hedge accounting is discontinued prospectively. When hedge accounting for cash flow hedges is discontinued, the amount that has been accumulated in the hedging reserve remains in equity until, for a hedge of a transaction resulting in recognition of a non-financial item, it is included in the non-financial item's cost on its initial recognition or, for other cash flow hedges, it is reclassified to the consolidated statement of income in the same period or periods as the hedged expected future cash flows affects income or loss. If the hedged future cash flows are no longer expected to occur, the amounts that have been accumulated in the hedging reserve are immediately reclassified to the consolidated statement of income.

4. Significant accounting policies (continued):

(l) Impairment:

Financial assets

IFRS 9 replaces the incurred loss model in IAS 39 with an expected credit loss ("ECL") model. The new impairment model applies to financial assets measured at amortized cost, contract assets and debt investments at FVOCI, but not to investments in equity instruments.

Pollard applies the simplified approach to providing for expected credit losses, which requires the use of the lifetime expected credit loss provision for all accounts receivable. Expected credit losses are measured as the difference in the present value of the contractual cash flows that are due under the contract and the cash flows that Pollard expects to receive. The expected cash flows reflect all available information, including Pollard's historical experience, the past due status, and forward-looking macroeconomic factors. Further details are provided in note 27 and note 28.

Non-financial assets

The carrying amount of Pollard's non-financial assets, other than inventories and deferred income tax assets, are reviewed at each reporting date to determine whether there is an indication that an asset may be impaired. If any such indication exists, or when the annual impairment testing for an asset is required, Pollard estimates the asset's recoverable amount. For goodwill the recoverable amount is estimated as of December 31 each year. An impairment loss is recognized if the carrying amount of an asset or its related CGU exceeds its estimated recoverable amount.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset of CGU. For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of cash inflows of other assets or CGUs.

Impairment losses are recognized in net income. Impairment losses recognized in respect to CGUs are allocated first to reduce the carrying amount of any goodwill allocated to the CGU and then to reduce the carrying amounts of the other assets in the CGU on a pro rata basis. An impairment loss in respect to goodwill is not reversed. In respect to other assets, impairment losses recognized in prior periods are assessed at each reporting date for any indications that the loss has decreased or no longer exists. An impairment loss is reversed if there has been a change in the estimates used to determine the recoverable amount. An impairment loss can only

4. Significant accounting policies (continued):

be reversed to the extent that the asset's carrying value that would have been determined, net of amortization, if no impairment had been recognized.

(m) Share capital:

Common stock is classified as equity. Incremental costs directly attributable to the issue of common stock are recognized as a deduction from equity, net of any tax effects.

(n) Translation of foreign currencies:

The functional currency for each of Pollard's subsidiaries is the currency of the primary economic environment in which the entity operates. Transactions in foreign currencies are translated to the respective functional currencies of each entity within the consolidated group using the exchange rates in effect at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rates prevailing at the end of the reporting period. Non-monetary items measured at historical cost in a foreign currency are translated to the functional currency using the exchange rate prevalent at the date of acquisition. Non-monetary items denominated in foreign currencies that are measured at fair value are translated to the functional currency at the exchange rate prevalent at the date that the fair value was determined. Foreign currency differences arising from translation are recognized in net income, except for exchange differences arising on the translation of financial instruments qualifying as a cash flow hedge, which are recognized directly in other comprehensive income ("OCI").

The results and financial position of entities within the consolidated group that have a functional currency different from the presentation currency are translated into Canadian dollars as follows: assets and liabilities are translated at the exchange rate prevailing at the end of the reporting period; income and expenses are translated at the average rate for the reporting period; all resulting exchange differences are recognized in OCI. On disposal of a foreign operation, the deferred cumulative amount recognized in OCI relating to that particular foreign operation is recognized in net income.

(o) Employee benefits:

Share based compensation

The grant date fair value of stock options granted to employees is recognized as an expense, with a corresponding increase in equity, over the vesting period of the awards.

4. Significant accounting policies (continued):

Defined contribution plans

Pollard's U.S. subsidiaries maintain four defined contribution plans in the United States. The obligation to contribute to these plans is recognized as an employee benefit expense as incurred.

Defined benefit plans

Pollard maintains four non-contributory defined benefit pension plans in Canada and the United States, three being final pay plans and one being a flat benefit plan. None of the plans have indexation features.

The costs of Pollard's defined benefit plans are recognized over the period in which employees render service to Pollard in return for the benefits. The defined benefit obligations associated with the plans are actuarially determined using the projected unit credit method pro-rated on service and management's best estimate of salary escalation and retirement ages of employees. The present value of the defined benefit obligations are determined by discounting the estimated future cash outflows using interest rates of high quality corporate bonds that have maturity terms approximating the maturity terms of the related obligation and that are denominated in the currency in which the benefits will be paid. The expected return on pension plan assets is calculated utilizing the discount rate used to measure the defined benefit obligation at the beginning of the annual period.

Past service costs are recognized as an expense on a straight line basis over the average period until the benefits becomes vested. If the benefits have vested, past service costs are recognized in net income immediately.

Remeasurements that arise in calculating the present value of the defined benefit obligation and the fair value of plan assets are recognized immediately in OCI.

Pollard's pension asset is limited to the total of any unrecognized past services costs and the present value of economic benefits available in the form of any future refunds from the plan or reductions in future contributions to the plan. In order to calculate the present value of economic benefits, consideration is given to any minimum funding requirements that apply to Pollard's plans. An economic benefit is available to Pollard if it is realizable during the life of the plan, or on settlement of the plan liabilities.

4. Significant accounting policies (continued):

(p) Income taxes:

Current income tax and deferred income tax are recognized in the statement of income except to the extent that the tax relates to items recognized directly in equity or in OCI. Current income tax is the expected tax payable or receivable on the taxable income or loss for the period and any adjustment to tax payable in respect to previous years. Current income tax expense includes withholding taxes and U.S. state franchise taxes.

Deferred income tax is recorded to reflect the expected future tax consequences of temporary differences between the carrying amounts of assets and liabilities and their tax basis. Deferred income tax assets and liabilities are determined based on the enacted or substantively enacted tax rates, which are expected to be in effect when the underlying items of income and expense are expected to be realized.

Deferred income tax is not recognized for: temporary differences related to investments in subsidiaries to the extent that it is probable that they will not reverse in the foreseeable future, taxable temporary differences arising on the initial recognition of goodwill or temporary differences on the initial recognition of assets or liabilities in a transaction that is not a business combination and that affects neither accounting nor taxable profit or loss.

Deferred income tax assets are reviewed at each reporting date and are reduced to the extent that it is no longer probable that the related tax benefit will be realized.

The effect on deferred income tax assets and liabilities of a change in tax rates is recognized in income in the period that includes the date of enactment or substantive enactment, except if it relates to an item previously recognized in equity, in which case the adjustment is made to equity.

Deferred income tax assets and liabilities are offset when there is a legally enforceable right to offset current income tax liabilities and assets, and they are levied by the same taxation authority on the same taxable entity, or on different tax entities which intend to settle their current income tax assets and liabilities on a net basis.

(q) Provisions:

Provisions are recognized when Pollard has a present legal or constructive obligation as a result of a past event that can be estimated reliably, and it is probable that an outflow of economic benefits will be required to settle the obligation. If the effect of the time value of money is material, provisions are discounted using a current pre-tax rate that reflects, where appropriate, the risks specific to the liability. Where discounting is used, the increase in the provision due to the passage of time is recognized as a finance cost.

4. Significant accounting policies (continued):

(r) Finance costs and finance income:

Finance costs comprise interest expense on borrowings including amortization of deferred financing costs, mark-to-market losses on foreign exchange contracts and net foreign exchange losses.

Borrowing costs that are not directly attributable to the acquisition, construction or production of an asset that necessarily takes a substantial period of time to get ready for its intended use or sale are expensed in the period incurred using the effective interest method.

Finance income comprises mark-to-market gains on foreign exchange contracts and net foreign exchange gains.

(s) Leases:

The determination of whether an arrangement is or contains a lease is based on the substance of the arrangement and requires an assessment of whether the arrangement conveys a right to use the asset. When substantially all risk and rewards of ownership are transferred from the lessor to the lessee, lease transactions are accounted for as finance leases. All other leases are accounted for as operating leases.

Certain Pollard subsidiaries, as lessees, have entered into leases which are classified as finance leases. These leases are presented in the consolidated financial statements according to their nature. The interest element of the lease payment is recognized over the term of the lease based on the effective interest rate method and is included in finance expenses.

5. Future accounting standards:

(a) Leases:

In January 2016, the IASB issued IFRS 16 *Leases* which replaces IAS 17 *Leases*. This standard introduces a single lessee accounting model and requires a lessee to recognize assets and liabilities for all leases with a term of more than 12 months, unless the underlying asset is of low value. A lessee is required to recognize a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. This standard substantially carries forward the lessor accounting requirements of IAS 17, while requiring enhanced disclosures to be provided by lessors. Other areas of the lease accounting model have been impacted, including the definition of a lease. Transitional provisions have been provided. The new standard is effective for annual periods beginning on or after January 1, 2019.

5. Future accounting standards (continued):

Pollard has undertaken a preliminary review of all lease contracts and has applied the new measurement model for lessees. Pollard leases a number of manufacturing facilities in Canada and the United States. The present value of the remaining lease payments will be recognized on the balance sheet as right to use assets and related lease liabilities upon adoption. The nature of expenses related to those leases will now change because Pollard will recognize a depreciation charge on the right to use assets and an interest expense on the related lease liabilities. Pollard intends to adopt the standard using the modified retrospective approach, using the practical expedient of setting the initial right to use asset equal to the corresponding lease liability. No restatement is required under this approach. Pollard has preliminarily estimated that the transitional impact on the consolidated statements of financial position will result in recognizing right to use assets and corresponding lease liabilities of $18,721.

(b) Uncertainty over income tax treatments:

In June 2017, the IASB issued IFRIC Interpretation 23 *Uncertainty over Income Tax Treatments.* The Interpretation 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 is effective for annual periods beginning on or after January 1, 2019 and is to be applied retrospectively. Pollard does not expect the Interpretation to have a significant impact on the consolidated financial statements upon adoption.

(c) Investments in associates and joint ventures:

In October 2017, the 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. These amendments are effective for annual periods beginning on or after January 1, 2019. Pollard does not expect the amendments to have a significant impact on the consolidated financial statements upon adoption.

5. Future accounting standards (continued):

(d) Employee benefits:

In February 2018, the IASB issued amendments to IAS 19 *Employee Benefits*. The amendments 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 are for annual and interim reporting periods beginning on or after January 1, 2019 and are to be applied prospectively. Pollard does not expect the amendments to have a significant impact on the consolidated financial statements upon adoption.

6. Acquisitions:

(a) INNOVA Gaming Group Inc.:

On August 3, 2017, 10188557 Canada Inc. (the "Offeror"), a wholly-owned subsidiary of Pollard, acquired 17,929,021 common shares of INNOVA Gaming Group Inc. ("INNOVA" or "Diamond Game") which had been validly tendered under the offer to acquire all of the outstanding common shares (the "Offer") for $2.50 in cash per common share. The Offer was extended until August 15, 2017.

On August 15, 2017, an additional 1,167,946 common shares were acquired under the extension of the Offer for $2.50 in cash per common share. A total of 19,096,967 common shares or 95.13% of the issued and outstanding common shares were acquired under the Offer. On August 18, 2017, Pollard mailed to all remaining holders of common shares a Notice of Compulsory Acquisition pursuant to the provisions of Section 206 of the Canada Business Corporations Act to complete the acquisition of 100% of the common shares. On September 18, 2017, the Compulsory Acquisition was completed and the Offeror acquired the remaining 976,932 common shares not already held by the Offeror, thereby becoming the holder of 100% of the common shares. On September 19, 2017, INNOVA was formally delisted from the Toronto Stock Exchange. The acquisition was completed for aggregate consideration of $50,185.

The purchase price was funded by proceeds from Pollard's credit facility and additional subordinated debt. 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 August 3, 2017, the acquisition date.

(In thousands of Canadian dollars, except for share amounts)

6. Acquisitions (continued):

Purchase price	$	50,185
Cash acquired		(10,867)
Net consideration paid	$	39,318
Additional net tangible assets acquired		
Accounts receivable	$	3,702
Inventories		1,739
Prepaid expenses and deposits		2,255
Property and equipment		10,288
Deferred income tax asset		5,912
Accounts payable and accrued liabilities		(5,915)
Income tax payable		(189)
Deferred revenue		(2,505)
Long-term debt		(1,467)
Deferred income tax liability		(4,892)
Net tangible assets acquired (excluding cash)	$	8,928
Trademarks	$	2,616
Software		2,733
Patents		436
Customer contracts		10,247
Identifiable intangible assets acquired	$	16,032
Goodwill acquired	$	14,358

Subsequent to the preliminary assignment of fair values to identifiable assets and liabilities acquired, Pollard assessed there to be a high degree of uncertainty that it will be able to recognize value from a portion of the deferred tax asset initially valued. As a result, in the year ended December 31, 2017, Pollard reduced the deferred income tax asset by $3,128, from $9,040 to $5,912 and increased the goodwill from $11,230 to $14,358.

The goodwill acquired is largely attributable to the assembled workforce and the expected synergies from the combined businesses. This goodwill is not expected to be deductible for tax purposes.

During the period ended June 30, 2018, the acquisition accounting was finalized.

(In thousands of Canadian dollars, except for share amounts)

6. Acquisitions (continued):

(b) International Gamco, Inc.:

On February 1, 2018, Pollard Holdings Inc., a wholly-owned subsidiary of Pollard, acquired 100% of the common shares of International Gamco, Inc. ("Gamco"). 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 February 1, 2018, the acquisition date. As per the sales agreement, the net purchase price was decreased by the amount of other current liabilities assumed, which were specified in the agreement. The majority of these other current liabilities were paid in March 2018.

Purchase price	$	21,648
Cash acquired		(90)
Net consideration paid	$	21,558
Additional net tangible assets acquired		
Restricted cash - other current liabilities	$	5,999
Accounts receivable		1,554
Inventories		4,831
Prepaid expenses and deposits		244
Property, plant and equipment		7,025
Patents		36
Deferred income tax asset		1,362
Accounts payable and accrued liabilities		(1,853)
Income taxes payable		(156)
Other current liabilities		(5,999)
Deferred income tax liability		(2,532)
Net tangible assets acquired (excluding cash)	$	10,511
Trade name	$	526
Game library		579
Customer relationships		4,058
Identifiable intangible assets acquired	$	5,163
Goodwill acquired	$	5,884

During the measurement period, the fair value of acquired accounts payable and accrued liabilities was increased by $601 with an offsetting increase to goodwill in the year ended December 31, 2018.

During the measurement period, the fair value of acquired prepaid expenses and deposits was decreased by $85 with an offsetting increase to goodwill in the year ended December 31, 2018.

During the measurement period, the fair value of acquired inventories was increased by $320 with an offsetting decrease to goodwill in the year ended December 31, 2018.

6. Acquisitions (continued):

During the measurement period, the fair value of the acquired deferred income tax liability was increased by $160 with an offsetting increase to goodwill in the year ended December 31, 2018.

Acquisition costs related to the Gamco purchase in the year ended December 31, 2018, were $227. These costs were included in administration expenses.

During the period between February 1, 2018 and December 31, 2018, Gamco generated revenues of approximately $27,114 and net income of $1,081, after depreciation and amortization of the fair values of identifiable assets acquired, which have been recorded in the consolidated financial statements. If Gamco had been acquired on January 1, 2018, incremental revenue of $2,217 and net loss of $4,755 (which includes $4,826 of transaction related expenditures, net of income tax) would have been recognized in the year ended December 31, 2018.

The goodwill acquired is largely attributable to the assembled workforce and the expected synergies from the combined businesses, including a greater share of the charitable gaming market. This goodwill is not expected to be deductible for tax purposes.

During the period ended December 31, 2018, the acquisition accounting was finalized.

(c) 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.

(In thousands of Canadian dollars, except for share amounts)

6. Acquisitions (continued):

Consideration paid	$	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

Acquisition costs related to the Schafer purchase in the year ended December 31, 2018, were $374. These costs were included in administration expenses.

During the period between October 31, 2018 and December 31, 2018, Schafer generated revenues of approximately $2,153 and net income of $152, after depreciation and amortization of the fair values of identifiable assets acquired, which have been recorded in the consolidated financial statements. If Schafer had been acquired on January 1, 2018, incremental revenue of $11,831 and net income of $1,897 would have been recognized in the year ended December 31, 2018.

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.

(In thousands of Canadian dollars, except for share amounts)

7. Inventories:

		December 31, 2018		December 31, 2017
Raw materials	$	18,537	$	11,755
Work-in-process		2,861		930
Finished goods		23,955		19,323
	$	45,353	$	32,008

During 2018, Pollard recorded inventory write-downs of $302 representing an increase in the obsolescence reserves and reversal of previous write-downs of $53 due to changes in foreign exchange rates.

During 2017, Pollard recorded inventory write-downs of $457 representing an increase in the obsolescence reserves and reversal of previous write-downs of $26 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 for share amounts)

8. Property, plant and equipment:

Cost		Land	Buildings	Leasehold improve-ments	Equipment	Furniture, fixture and computers	Assets in progress & spare parts	Total
Balance at January 1, 2017	$	803	12,068	3,306	154,054	4,879	1,579	176,689
Acquisitions		–	–	–	8,468	1,527	293	10,288
Additions/net transfers		–	88	284	5,674	422	480	6,948
Disposals		–	–	–	(10,087)	(6)	–	(10,093)
Effect of movements in exchange rates		–	–	(63)	(309)	8	–	(364)
Balance at December 31, 2017	$	803	12,156	3,527	157,800	6,830	2,352	183,468
Acquisitions		881	7,496	–	3,832	–	225	12,434
Additions/net transfers		–	195	1,460	6,549	510	6,376	15,090
Disposals		–	–	–	(65)	–	–	(65)
Effect of movements in exchange rates		47	145	74	2,269	26	44	2,605
Balance at December 31, 2018	$	1,731	19,992	5,061	170,385	7,366	8,997	213,532

Accumulated depreciation		Land	Buildings	Leasehold improve-ments	Equipment	Furniture, fixture and computers	Assets in progress & spare parts	Total
Balance at January 1, 2017	$	–	4,912	1,915	119,085	3,871	–	129,783
Depreciation for the year		–	369	424	8,469	522	–	9,784
Disposals		–	–	–	(10,013)	(6)	–	(10,019)
Effect of movements in exchange rates		–	–	(189)	(206)	(4)	–	(399)
Balance at December 31, 2017	$	–	5,281	2,150	117,335	4,383	–	129,149
Depreciation for the year		–	444	242	11,129	233	–	12,048
Disposals		–	–	–	(47)	–	–	(47)
Effect of movements in exchange rates		–	2	74	691	9	–	776
Balance at December 31, 2018	$	–	5,727	2,466	129,108	4,625	–	141,926

Carrying amounts		Land	Buildings	Leasehold improve-ments	Equipment	Furniture, fixture and computers	Assets in progress & spare parts	Total
At December 31, 2017	$	803	6,875	1,377	40,465	2,447	2,352	54,319
At December 31, 2018	$	1,731	14,265	2,595	41,277	2,741	8,997	71,606

(In thousands of Canadian dollars, except for share amounts)

9. Equity investment:

Interest in joint venture	December 31, 2018	December 31, 2017
Balance, beginning of year	$ 877	$ 468
Investment	2,842	2,204
Equity loss	(2,631)	(1,727)
Effects of movements in exchange rates	76	(68)
Balance, end of year	$ 1,164	$ 877

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.

10. Goodwill:

	December 31, 2018	December 31, 2017
Balance, beginning of year	$ 51,768	$ 37,513
Acquisition of Diamond Game (note 6)	–	14,358
Acquisition of Integrity	–	189
Acquisition of Gamco (note 6)	5,884	–
Acquisition of Schafer (note 6)	9,233	–
Effects of movements in exchange rates	2,782	(292)
Balance, end of year	$ 69,667	$ 51,768

(In thousands of Canadian dollars, except for share amounts)

10. Goodwill (continued):

Impairment assessment methodology

Pollard performs its annual goodwill impairment test as at December 31. Goodwill has been allocated as follows to Pollard's CGUs:

		December 31, 2018		December 31, 2017
Lotteries	$	30,816	$	30,816
American Games		7,012		6,457
Diamond Game		15,741		14,495
Gamco		6,513		–
Schafer		9,585		–
Total	$	69,667	$	51,768

Goodwill allocated to the American Games, Diamond Game, Gamco and Schafer CGUs are subject to foreign exchange revaluation.

For each CGU, the recoverable amounts have been determined based on a value in use calculation using cash flow projections from financial forecasts approved by senior management. These forecasts cover a period of five years and reflect an estimate of a terminal value. Included in these forecasts is an assumption of certain growth rates which was based on historical trend and expected future performance.

The calculation of value in use for the CGUs described above are most sensitive to the following key assumptions on which management has based its cash flow projections to undertake impairment testing of goodwill:

- Revenue and related gross profit
- Foreign exchange rates
- Discount rates
- Growth rates

Revenue and related gross profit

Projected cash flows from revenue assumes the continuation of recent historical trends adjusted for expected new contract wins, anticipated contract renewal pricing pressures and the expected impact of sales initiatives in conjunction with certain production efficiencies that are being developed or are expected to be developed.

10. Goodwill (continued):

Foreign exchange rates

A significant portion of revenue is denominated in U.S. dollars and Euros, partially offset by U.S. dollar denominated costs. In addition, certain financial assets and liabilities are denominated in U.S. currency. Projected cash flows assume an estimated exchange rate between Canadian dollars to U.S. dollars and Euros based on expected exchange rates during the forecast period.

Discount rates

Discount rates were calculated based on the estimated cost of equity capital and debt capital considering data and factors relevant to the economy, the industry and the CGUs. These costs were then weighted in terms of a typical industry capital structure to arrive at an estimated weighted average cost of capital. The after-tax discount rates applied to the cash flow projections for the CGUs described above were as follows:

Lotteries	12.0%
American Games	11.0%
Diamond Game	15.0%
Gamco	12.0%
Schafer	14.7%

Growth rates

Growth rates are based on estimated sustainable long-term growth rates of the CGUs. A terminal value of 2% was applied in the value in use calculations for all of the above CGUs.

Management believes that any reasonable possible change in any of the key assumptions on which the cash generating unit’s recoverable amounts are based would not cause the unit’s carrying amounts to exceed its recoverable amount.

(In thousands of Canadian dollars, except for share amounts)

11. Intangible assets:

Cost		Customer assets	Patents	Trademarks	Deferred development	Computer software and licenses	Total
Balance at January 1, 2017	$	18,645	5,187	–	1,148	7,139	32,119
Acquisitions		10,247	436	2,616	–	2,733	16,032
Additions (net of investment tax credits)		–	69	–	–	867	936
Additions – internally developed (net of investment tax credits)		–	–	–	62	1,248	1,310
Effect of movements in exchange rates		99	4	25	–	17	145
Balance at December 31, 2017	$	28,991	5,696	2,641	1,210	12,004	50,542
Acquisitions		15,484	167	1,539	–	579	17,769
Additions (net of investment tax credits)		–	742	–	429	678	1,849
Additions – internally developed (net of investment tax credits)		–	–	–	–	5,296	5,296
Effect of movements in exchange rates		1,769	46	323	–	460	2,598
Balance at December 31, 2018	$	46,244	6,651	4,503	1,639	19,017	78,054

(In thousands of Canadian dollars, except for share amounts)

11. Intangible assets (continued):

Accumulated amortization		Customer assets	Patents	Trademarks	Deferred development	Computer software and licenses	Total
Balance at January 1, 2017	$	13,297	4,781	–	1,106	1,019	20,203
Amortization for the year		1,789	128	–	104	595	2,616
Effect of movements in exchange rates		(16)	(1)	–	–	(6)	(23)
Balance at December 31, 2017	$	15,070	4,908	–	1,210	1,608	22,796
Amortization for the year		3,152	204	–	36	1,555	4,947
Effect of movements in exchange rates		120	6	–	–	99	225
Balance at December 31, 2018	$	18,342	5,118	–	1,246	3,262	27,968

Carrying amounts		Customer assets	Patents	Trademarks	Deferred development	Computer software and licenses	Total
At December 31, 2017	$	13,921	788	2,641	–	10,396	27,746
At December 31, 2018	$	27,902	1,533	4,503	333	15,815	50,086

Amortization of intangible assets in 2018 of $4,947 (2017 – $2,616), was included in cost of sales.

(In thousands of Canadian dollars, except for share amounts)

12. Income taxes:

Income tax expense

		2018		2017
Current	$	5,175	$	7,902
Deferred (reduction)		742		(712)
Total	$	5,917	$	7,190

Income tax recognized in other comprehensive income (loss)

		Amount before tax	Tax expense	2018 Amount net of tax		Amount before tax	Tax benefit	2017 Amount net of tax
Defined benefit plans remeasurement gain (loss)	$	3,695	(975)	2,720	$	(9,875)	2,478	(7,397)

Reconciliation of effective tax rate

	2018		2018	2017		2017
Net income for the year		$	14,852		$	16,784
Total income tax expense			5,917			7,190
Income before income taxes		$	20,769		$	23,974
Income tax using Pollard's domestic tax rate	27.0%		5,608	27.0%		6,473
Effect of tax rates in foreign jurisdictions	(2.5%)		(508)	4.1%		996
Non-deductible amounts	2.7%		553	3.7%		887
Changes in enacted United States federal income tax rates	0.0%		–	(9.4%)		(2,261)
Adjustments for tax of prior periods related to Diamond Game acquisition	0.0%		–	5.1%		1,217
Other items	(2.4%)		(500)	1.4%		331
Effect of non-taxable items related to foreign exchange	3.7%		764	(1.9%)		(453)
	28.5%	$	5,917	30.0%	$	7,190

(In thousands of Canadian dollars, except for share amounts)

12. Income taxes (continued):

Deferred income tax assets and liabilities

Recognized deferred income tax assets and liabilities

Deferred income tax assets and liabilities are attributable to the following:

	Assets		Liabilities		Net	
	2018	2017	2018	2017	2018	2017
Property, plant and equipment	$ 23	48	$ (9,319)	(7,762)	$ (9,296)	(7,714)
Intangible assets	2,954	685	(6,067)	(2,082)	(3,113)	(1,397)
Inventories	259	432	(57)	–	202	432
Employee benefits	7,409	7,738	(1,227)	(1,488)	6,182	6,250
Unrealized foreign exchange (gains) and losses	1,126	393	(874)	(303)	252	90
Unused tax losses	2,153	1,855	–	–	2,153	1,855
Contract liabilities	56	182	(272)	–	(216)	182
Other	101	98	(22)	(71)	79	27
Tax assets (liabilities)	$ 14,081	11,431	$ (17,838)	(11,706)	$ (3,757)	(275)

Movement in temporary differences during the year

	January 1, 2017	Recognized in profit or loss	Acquisitions	Recognized in other comprehensive income	Balance December 31, 2017
Property, plant and equipment	$ (6,907)	2,104	(2,911)	–	(7,714)
Intangible assets	(3,157)	911	849	–	(1,397)
Inventories	364	52	16	–	432
Employee benefits	4,300	(1,506)	978	2,478	6,250
Unrealized foreign exchange (gains) and losses	419	(329)	–	–	90
Unused tax losses	–	193	1,662	–	1,855
Contract liabilities	–	(159)	341	–	182
Other	72	(127)	82	–	27
Tax assets (liabilities)	$ (4,909)	1,139	1,017	2,478	(275)

(In thousands of Canadian dollars, except for share amounts)

12. Income taxes (continued):

		January 1, 2018	Recognized in profit or loss	Acquisitions	Recognized in other comprehensive income	Balance December 31, 2018
Property, plant and equipment	$	(7,714)	(406)	(1,176)	–	(9,296)
Intangible assets		(1,397)	(477)	(1,239)	–	(3,113)
Inventories		432	(71)	(159)	–	202
Employee benefits		6,250	(536)	1,443	(975)	6,182
Unrealized foreign exchange (gains) and losses		90	162	–	–	252
Unused tax losses		1,855	239	–	–	2,094
Contract liabilities		182	(125)	–	–	57
Other*		(96)	–	(39)	–	(135)
Tax assets (liabilities)	$	(398)	(1,214)	(1,170)	(975)	(3,757)

* January 1, 2018 figure includes the impact of the transitional adjustment booked to opening deficit upon adoption of IFRS 15 of $123. Further details are provided in note 3(a).

Recognized in the consolidated statements of comprehensive income as follows:

		2018		2017
Deferred income tax expense (reduction)	$	742	$	(712)
Finance income (loss)		472		(427)
	$	1,214	$	(1,139)

Amounts included in finance income relate to unrealized foreign exchange.

Unrecognized deferred tax assets

Deferred tax assets have not been recognized in respect to certain tax losses because it is not probable that future taxable profit will be available against which Pollard can use the benefits therefrom. The amount of tax losses not recognized at December 31, 2018 was $9,965 (2017 – $8,426), with an estimated tax effect of $2,690 (2017 – $2,332). These tax losses, related to the acquisition of Diamond Game in 2017, will expire between 2034 and 2038.

(In thousands of Canadian dollars, except for share amounts)

13. Long-term debt:

		December 31, 2018		December 31, 2017
Credit facility, interest of 4.0% to 4.3%, payable monthly, maturing 2021	$	116,177	$	83,972
Equipment debt, interest of 6.72%, payable monthly, maturing 2019		4		189
Equipment lease, interest of 3.89% to 5.55% payable monthly, maturing 2019		36		647
Deferred financing charges, net of amortization		(421)		(253)
		115,796		84,555
Less current portion		(40)		(784)
	$	115,756	$	83,771

		Credit facility	Deferred financing	Equipment debt	Equipment lease	Total
Balance at January 1, 2018	$	83,972	(253)	189	647	84,555
Net proceeds (payments)		28,705	–	(187)	(640)	27,878
Payment of deferred financing charges		–	(561)	–	–	(561)
Total changes from financing cash flows		28,705	(561)	(187)	(640)	27,317
Effect of movements in exchange rates		3,500	–	2	29	3,531
Amortization of deferred financing charges		–	393	–	–	393
Total other changes		3,500	393	2	29	3,924
Balance at December 31, 2018	$	116,177	(421)	4	36	115,796

(In thousands of Canadian dollars, except for share amounts)

13. Long-term debt (continued):

		Credit facility	Deferred financing	Equipment debt	Equipment lease	Total
Balance at January 1, 2017	$	71,003	(151)	–	–	70,852
Net proceeds (payments)		14,164	–	(193)	(451)	13,520
Payment of deferred financing charges		–	(342)	–	–	(342)
Total changes from financing cash flows		14,164	(342)	(193)	(451)	13,178
Effect of movements in exchange rates		(1,195)	–	3	10	(1,182)
Acquisitions		–	–	379	1,088	1,467
Amortization of deferred financing charges		–	240	–	–	240
Total other changes		(1,195)	240	382	1,098	525
Balance at December 31, 2017	$	83,972	(253)	189	647	84,555

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 December 31, 2018, the outstanding letters of guarantee drawn under the credit facility were $1,337 (2017 – $1,909).

Included in the total credit facility balance is a U.S. dollar denominated balance of US$43,600 (2017 – US$14,700).

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 December 31, 2018, Pollard is in compliance with all financial covenants.

As of December 31, 2018, Pollard had unused credit facility available of $58,860 (2017 – $34,202).

(In thousands of Canadian dollars, except for share amounts)

13. Long-term debt (continued):

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.

Equipment debt and leasing

Pollard's subsidiary, Diamond Game, entered into agreements to purchase equipment payable in monthly installments including interest. The equipment purchased includes charitable gaming machines, machinery and equipment, and computer equipment all relating to the operations of Diamond Game.

14. Subordinated debt:

	December 31, 2018	December 31, 2017
Subordinated debt, interest of 8.00% payable quarterly, maturing 2024	$ –	$ 16,734
	$ –	$ 16,734
Less current portion	–	(3,585)
	$ –	$ 13,149

On June 23, 2017, Pollard entered into a loan agreement with Equities for a subordinated term loan with a seven year term, repayable at any time (subject to meeting certain financial covenants under the secured credit facility). The loan was provided to assist with the purchase of Diamond Game. A total of $25,092 was drawn in the third quarter of 2017. Interest on the subordinated debt commenced with the first draw at a rate of 8%. Quarterly principal payments on the loan facility commenced the month following the first draw, which occurred August 4, 2017.

In addition to the mandatory quarterly payments, Pollard has made three lump sum prepayments. On September 20, 2017, Pollard repaid $7,462 in outstanding principal and on February 23, 2018, Pollard repaid an additional $7,471 in outstanding principal. On June 29, 2018, Pollard repaid in full the remainder of the outstanding principal in the amount of $7,471.

(In thousands of Canadian dollars, except for share amounts)

15. Pension liability:

	December 31, 2018	December 31, 2017
Fair value of benefit plan assets	$ 52,946	$ 50,506
Present value of benefit plan obligations	(73,303)	(73,465)
Net pension liability	$ (20,357)	$ (22,959)

Pollard sponsors non-contributory defined benefit plans providing pension benefits to its employees. Pollard has four defined benefit pension plans of which three are final pay plans and one is a flat benefit plan. None of the plans have indexation features. The measurement date for all the plans is December 31. Two of the plans of the U.S. subsidiaries require valuations annually with the last valuations being as of January 1, 2018. One of the Canadian plans of Pollard currently requires valuation every year with the last valuation as of December 31, 2017. Pollard's other Canadian plan's valuation was as of January 1, 2017. Pollard's U.S. subsidiaries also maintain four defined contribution plans. The pension expense for these defined contribution plans is the annual funding contribution by the subsidiaries.

Pollard expects to contribute approximately $4,706 to its defined benefit plans in 2019. Included in the 2019 estimated contributions is $1,212 in additional solvency payments.

The benefit plan assets are held in trust and are invested as follows:

	December 31, 2018	December 31, 2017
Equities	62.0%	60.8%
Bonds	35.8%	36.2%
Cash and cash equivalents	2.2%	3.0%
	100.0%	100.0%

(In thousands of Canadian dollars, except for share amounts)

15. Pension liability (continued):

Information about Pollard's defined benefit plans, in aggregate, is as follows:

		2018		2017
Benefit plan assets				
Fair value, beginning of year	$	50,506	$	44,372
Expected return on plan assets		1,788		1,834
Employer contributions		4,720		4,623
Benefits paid		(1,548)		(1,773)
Remeasurement gains (losses)		(3,024)		1,825
Effect of movements in exchange rates		504		(375)
Fair value, end of year	$	52,946	$	50,506

		2018		2017
Accrued benefit plan obligations				
Balance, beginning of year	$	73,465	$	57,896
Current service cost		4,839		3,934
Interest cost		2,512		2,294
Benefits paid		(1,548)		(1,773)
Remeasurement (gains) losses		(6,790)		11,671
Effect of movements in exchange rates		825		(557)
Balance, end of year	$	73,303	$	73,465
Net pension liability	$	(20,357)	$	(22,959)

(In thousands of Canadian dollars, except for share amounts)

15. Pension liability (continued):

The total net cost for Pollard's defined benefit and defined contribution pension plans recognized in cost of sales is as follows:

	2018	2017
Net defined benefit plans cost		
Current service cost	$ 4,839	$ 3,934
Interest on plan obligations	2,512	2,294
Actual return on plan assets	1,236	(3,659)
Difference between expected return and actual return on plan assets	(2,655)	2,190
Net defined benefit plans cost	5,932	4,759
Defined contribution plans cost	517	323
Net pension plans cost	$ 6,449	$ 5,082

Actuarial assumptions

The principal actuarial assumptions used in measuring at the reporting date are as follows:

	2018	2017
Discount rate	3.9% to 4.6%	3.4% to 3.8%
Rate of compensation increase	0% to 3.0%	0% to 3.0%

Assumptions regarding future mortality have been based on published statistics and mortality tables. As of December 31, 2018, Pollard used CPM2014 Private Sector projected CPM-B mortality table for its Canadian subsidiary's pension plans and the RP-2018 healthy mortality tables for its U.S. subsidiary's pension plans. As of December 31, 2017, Pollard used CPM2014 Private Sector projected CPM-B mortality table for its Canadian subsidiary's pension plans and the RP-2017 healthy mortality tables for its U.S. subsidiary's pension plans.

(In thousands of Canadian dollars, except for share amounts)

15. Pension liability (continued):

Sensitivity analysis

Reasonably possible changes at the reporting date to one of the relevant actuarial assumptions, holding other assumptions constant, would have affected the defined benefit obligation by the amounts show below:

		Increase		Decrease
Discount rate (1% movement)	$	(13,112)	$	17,390
Rate of compensation (1% movement)	$	1,906	$	(1,745)
Future mortality (one year)	$	933	$	(944)

Remeasurements

		2018		2017
Remeasurement gains (losses) arising on plan assets	$	(3,024)	$	1,825
Remeasurement (gains) losses arising on plan liabilities from:				
Demographic assumptions	$	23	$	589
Financial assumptions		(8,601)		8,698
Experience adjustments		1,788		2,384
Remeasurement (gains) losses arising on plan liabilities	$	(6,790)	$	11,671

Remeasurements recognized in other comprehensive income

		2018		2017
Amount accumulated in deficit, beginning of year	$	(19,393)	$	(11,996)
Recognized during the year, net of income tax		2,720		(7,397)
Amount accumulated in deficit, end of year	$	(16,673)	$	(19,393)

(In thousands of Canadian dollars, except for share amounts)

16. Share capital:

	Shares		Amount $
Authorized			
Unlimited common shares			
Unlimited preferred shares			
Issued			
Balance at January 1, 2017 and 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

Ownership restrictions:

The holders of the common shares are entitled to one vote in respect to each common share held, subject to the Board of Directors ability to take constraint actions when a person, or group of persons acting in concert acquires, agrees to acquire, holds, beneficially owns or controls, either directly or indirectly, a number of shares equal to or in excess of 5% of the common shares (on a non-diluted basis) issued and outstanding ("Ownership Threshold"). The Board of Directors, in its sole discretion, can take the following constraint actions:

- place a stop transfer on all or any of the common shares believed to be in excess of the Ownership Threshold;
- suspend all voting and/or dividend rights on all or any of common share held believed to be in excess of the Ownership Threshold;
- apply to a court seeking an injunction to prevent a person from acquiring, holding, owning, controlling and/or directing, directly or indirectly, common shares in excess of the Ownership Threshold; and/or
- make application to the relevant securities commission to effect a cease trading order or such similar restriction, until the person no longer controls common shares equal to or in excess of the Ownership Threshold.

In addition, if a Gaming Regulatory Authority has determined that ownership by a holder of common shares is inconsistent with its declared policies, the Board of Directors is entitled to take constraint action against such shareholder. Any person who controls common shares equal to or in excess of the Ownership Threshold, may be required to file an application, be investigated and have suitability as a shareholder determined by a Gaming Regulatory Authority, if such Gaming Regulatory Authority has reason to believe such ownership would otherwise be inconsistent with its declared policies.

16. Share capital (continued):

The shareholder must pay all the costs of the investigation incurred by any such Gaming Regulatory Authority.

Capital management:

Pollard's objectives in managing capital are to maintain a strong capital base so as to maintain investor, creditor and market confidence and to sustain future development of the business. Pollard also strives to maintain an optimal capital structure to reduce the overall cost of capital.

In the management of capital, Pollard includes long-term debt, share capital and deficit, but excludes reserves. The Board of Directors regularly monitors the levels of debt, equity and dividends.

Pollard monitors capital on the basis of funded debt to Adjusted EBITDA, working capital ratio and debt service coverage. Pollard has externally imposed capital requirements as determined through its bank credit facility. As at December 31, 2018, Pollard is in compliance with all financial covenants.

There were no other changes in Pollard's approach to capital management during the current period.

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 November 6, 2018, a dividend of $0.03 per share was declared, payable on January 15, 2019, to the shareholders of record on December 31, 2018.

Issue of common shares:

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. The proceeds, net of commissions and offering expenses, was $35,351.

On October 17, 2018, 12,500 common shares were issued in conjunction with the exercise of stock options. The proceeds were $45.

(In thousands of Canadian dollars, except for share amounts)

16. Share capital (continued):

Share based compensation:

Under the Pollard Banknote Limited Stock Option Plan the Board of Directors has the authority to grant options to purchase common shares to eligible persons and to determine the applicable terms. The aggregate maximum number of common shares available for issuance from Pollard's treasury under the Option Plan is 2,354,315 common shares.

The Board of Directors previously approved awards of 250,000 options in total to purchase common shares of Pollard for certain key management personnel. Options were granted on three grant dates, with the exercise price being the common share price on the exercise price determination date. All of the outstanding options have seven year terms, vesting 25% per year over the first four years.

The grant date fair value of these options was determined based on the Black-Scholes formula. Expected volatility is estimated by considering historic average share price volatility. The inputs used in the measurement of the fair values of the share based compensation granted are the following:

Option grant date		April 24, 2017		October 3, 2016		March 10, 2014
Fair value at grant date	$	2.27	$	1.87	$	0.82
Number of options granted		125,000		25,000		100,000
Share price	$	10.00	$	8.12	$	3.63
Exercise price	$	10.00	$	8.12	$	3.63
Exercise price determination date		April 21, 2017		September 30, 2017		March 7, 2014
Expected volatility		29.3%		30.7%		33.7%
Option life (expected weighted average life)		4.75 years		4.75 years		4.75 years
Risk-free interest rate (based on Canadian government bonds)		0.6% to 0.7%		0.6% to 0.7%		1.7% to 2.1%

	2018			2017		
	Number		Weighted average exercise price	Number		Weighted average exercise price
Balance, beginning of year	250,000	$	7.26	125,000	$	4.53
Granted during the year	–	$	–	125,000	$	10.00
Exercised during the year	(12,500)		3.63	–		–
Balance, end of year	237,500	$	7.46	250,000	$	7.26

(In thousands of Canadian dollars, except for share amounts)

16. Share capital (continued):

On October 17, 2018, 12,500 stock options were exercised by a member of Pollard's key management at an exercise price of $3.63 per share. As a result, 12,500 common shares were issued.

As of December 31, 2018, no share options had expired. Of the 237,500 options outstanding at December 31, 2018, 68,750 were exercisable.

17. Commitments and contingencies:

Pollard and certain subsidiaries rent premises and equipment under long-term operating leases. The following is a schedule by fiscal year of rental payment commitments under operating leases outstanding:

2019	$	5,704
2020		4,888
2021		3,832
2022		3,205
2023		2,353

Pollard is contingently liable for outstanding letters of guarantee in the amount of $1,337 at December 31, 2018 (2017 – $1,909). These letters of guarantee are part of Pollard's credit facility and are secured as disclosed in note 13.

During 2008, Pollard entered into a sale leaseback with an affiliate of Equities for land and building in Council Bluffs, Iowa. The property was sold for $4,081 and leased back for ten years at an annual lease rate of approximately US$260. During 2019, Pollard entered into a new lease. The base rental rate is approximately US$375, which is based on the current market value as determined through independent appraisal.

Also in 2008, Pollard entered into a lease with an affiliate of Equities for a manufacturing facility in Winnipeg, Manitoba. The lease was for a 12 year 6 month period, ending March 31, 2021, at an annual base rate of approximately $2,453. In 2015, Pollard agreed to exercise its renewal clause. The renewal covers the period from April 2021 to September 2023 with an approximate annual lease rate of $2,400, including an annual amortization of a leasehold improvement allowance of approximately $1,000. The total leasehold allowance is $2,500. The base rental rate was based on current market value as determined through independent appraisal.

(In thousands of Canadian dollars, except for share amounts)

17. Commitments and contingencies (continued):

During 2011, Pollard entered into a sale leaseback with an affiliate of Equities for land and building in Winnipeg, Manitoba. The property was sold for $3,473 and leased back for five years (with an option to renew its lease for an additional five year term) for annual rent of $313 per year. The rental rate was based on current market value as determined through independent appraisal. The sale value was determined through independent appraisal. During 2016, Pollard exercised its option to renew its lease for an additional five year term for annual rent of $363 per year. The rental rate was based on current market value as determined through independent appraisal.

Pollard is involved in litigation and claims associated with operations, the aggregate amounts of which are not determinable. While it is not possible to estimate the outcome of the proceedings, management is of the opinion that any resulting settlements would not materially affect the financial position of Pollard. Should a loss occur on resolution of these claims, such loss would be accounted for as a charge to income in the period in which the settlement occurs.

Pollard has agreed to indemnify Pollard's current and former directors and officers from and against liability and costs in respect of any action or suit against them in connection with the execution of their duties of office, subject to certain usual limitations. No claims with respect to such occurrences have been made and, as such, no amount has been recorded in these financial statements with respect to these indemnifications.

18. Revenue and contract balances:

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

Revenue – geographical segment	Year ended December 31, 2018		
	Lotteries and charitable gaming	Diamond Game	Total
Canada	$ 65,750	$ 11,343	$ 77,093
United States	170,643	14,763	185,406
International	69,369	–	69,369
Total	$ 305,762	$ 26,106	$ 331,868

(In thousands of Canadian dollars, except for share amounts)

18. Revenue and contract balances (continued):

Revenue – geographical segment	Year ended December 31, 2017		
	Lotteries and charitable gaming	Diamond Game	Total
Canada	$ 59,176	$ 5,126	$ 64,302
United States	154,442	5,141	159,583
International	61,769	–	61,769
Total	$ 275,387	$ 10,267	$ 285,654

Revenue – product line	Year ended December 31, 2018		
	Lotteries and charitable gaming	Diamond Game	Total
Lottery	$ 250,580	$ –	$ 250,580
Charitable	55,182	–	55,182
Gaming systems	–	26,106	26,106
Total	$ 305,762	$ 26,106	$ 331,868

Revenue – product line	Year ended December 31, 2017		
	Lotteries and charitable gaming	Diamond Game	Total
Lottery	$ 247,649	$ –	$ 247,649
Charitable	27,738	–	27,738
Gaming systems	–	10,267	10,267
Total	$ 275,387	$ 10,267	$ 285,654

(In thousands of Canadian dollars, except for share amounts)

18. Revenue and contract balances (continued):

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

Contract balances		December 31, 2018		January 1, 2018
Trade receivables, which are included in accounts receivable	$	27,061	$	36,263
Contract assets, which are included in accounts receivable (1)		3,128		3,260
Contract liabilities (2)		857		1,491

(1) Pollard recognized contract assets upon adoption IFRS 15 as an adjustment to the opening balance at January 1, 2018.
(2) Contract liabilities were previously classified as deferred revenue.

Contract liabilities		Year ended December 31, 2018
Balance, beginning of year	$	1,491
Increases due to cash received		982
Revenue recognized during the year		(1,616)
Balance, end of year		857
Less current portion		(814)
	$	43

19. Other expenses:

		2018		2017
Loss on equity investment (note 9)	$	2,631	$	1,727
EBITDA support agreement income		(2,000)		(825)
Loss on sale of property, plant and equipment		–		74
Other income		(167)		(301)
	$	464	$	675

(In thousands of Canadian dollars, except for share amounts)

19. Other 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.

20. Finance costs and finance income:

Finance costs		2018		2017
Foreign exchange loss	$	5,593	$	210
Interest		4,243		3,962
	$	9,836	$	4,172

Finance income		2018		2017
Foreign exchange gain	$	881	$	1,104
	$	881	$	1,104

21. Net income per share:

		2018		2017
Net income attributable to shareholders for basic and diluted net income per share	$	14,852	$	16,784
Weighted average number of shares (basic)		25,439,952		23,543,158
Weighted average impact of share options		247,397		212,329
Weighted average number of shares (diluted)		25,687,349		23,755,487
Net income per share (basic)	$	0.58	$	0.71
Net income per share (diluted)	$	0.58	$	0.71

(In thousands of Canadian dollars, except for share amounts)

22. Personnel expenses:

		2018		2017
Wages and salaries	$	100,622	$	84,718
Benefits and government payroll remittances		16,760		12,327
Profit share		2,010		2,792
Expenses related to defined contribution plans		517		323
Expenses related to defined benefit plans		5,932		4,759
	$	125,841	$	104,919

23. Supplementary cash flow information:

		2018		2017
Change in non-cash operating working capital:				
Accounts receivable	$	14,002	$	632
Inventories		(7,799)		(3,184)
Prepaid expenses and deposits		(509)		(1,236)
Income taxes		(531)		(1,086)
Accounts payable and accrued liabilities		(1,222)		2,877
Contract liabilities		56		(882)
	$	3,997	$	(2,879)

24. Related party transactions:

Pollard Equities Limited and affiliates

During the year ended December 31, 2018, Pollard paid property rent of $3,187 (2017 – $3,177) and $528 (2017 – $379) in plane charter costs to affiliates of Equities. In addition, during the year, Pollard paid Equities $421 (2017 – $1,006) interest on Pollard's subordinated debt.

During the year, Equities paid Pollard $72 (2017 – $72) for accounting and administration fees.

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 (2017 – $1,900).

Neogames S.à r.l. and affiliates

During the year ended December 31, 2018, Pollard reimbursed operating costs and paid software royalties of $3,321 (2017 – $2,878) to its iLottery partner, which are recorded in cost of sales.

(In thousands of Canadian dollars, except for share amounts)

24. Related party transactions (continued):

At December 31, 2018, included in accounts payable and accrued liabilities is a net amount owing to Pollard's iLottery partner of $940 (2017 – $698) for reimbursement of operating costs and capital expenditures, and its share of operating profits.

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:

		2018		2017
Wages, salaries and benefits	$	3,543	$	3,115
Profit share		20		22
Expenses related to defined benefit plans		619		512
	$	4,182	$	3,649

As at December 31, 2018, the Directors and Named Executive Officers of Pollard, as a group, beneficially owned or exercised control or direction over 17,456,558 common shares of Pollard.

25. Sales to major customers:

For the year ended December 31, 2018, sales to one customer amounted to 12.7 percent of consolidated sales and 11.1 percent to a second customer. In 2017, sales to one customer amounted to 12.0 percent of consolidated sales and 11.7 percent to a second customer.

26. 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 Diamond Game segment was acquired August 3, 2017, therefore in 2017, Pollard had only one segment for a portion of the year.

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 for share amounts)

26. Segmented information (continued):

	Year ended December 31, 2018		
	Lotteries and charitable gaming	Diamond Game	Total
Revenues from external customers	$ 305,762	$ 26,106	$ 331,868
Operating costs and expenses	288,673	22,426	311,099
Earnings before income taxes	17,089	3,680	20,769
Total assets	242,692	62,908	305,600

	2018	2017
Sales:		
Canada	$ 77,093	$ 64,302
U.S.	185,406	159,583
Other	69,369	61,769
	$ 331,868	$ 285,654

	December 31, 2018	December 31, 2017
Property, plant and equipment and goodwill:		
Canada	$ 66,227	$ 63,188
U.S.	75,046	42,899
	$ 141,273	$ 106,087

27. Financial instruments:

The fair value of a financial instrument is the estimated amount that Pollard would receive or pay to terminate the instrument agreement at the reporting date. The following methods and assumptions were used to estimate the fair value of each type of financial instrument by reference to various market value data and other valuation techniques as appropriate.

The fair values of accounts receivable, accounts payable and accrued liabilities and dividends payable approximate their carrying values given their short-term maturities.

The fair value of the long-term debt approximates the carrying value due to the variable interest rate of the debt.

27. Financial instruments (continued):

The fair value of the other non-current liabilities approximates the carrying value based on the expected settlement amount of these liabilities.

Certain financial instruments recorded at fair value on the statements of financial position are classified using a fair value hierarchy that reflects the significance of the inputs used in making the measurements. The fair value hierarchy has the following levels:

Level 1 – valuation based on the quoted prices observed in active markets for identical assets or liabilities

Level 2 – valuation techniques based on inputs that are quoted prices of similar instruments in active markets; quoted prices for identical or similar instruments in markets that are not active; other than quoted prices used in a valuation model that are observable for that instrument; and inputs that are derived principally from or corroborated by observable market data by correlation or other means

Level 3 – valuation techniques with significant unobservable market inputs

A financial instrument is classified to the lowest level of the hierarchy for which a significant input has been considered in measuring fair value.

As at December 31, 2018, the cash and restricted cash recorded at fair value was classified as level one of the fair value hierarchy.

28. 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.

(In thousands of Canadian dollars, except for share amounts)

28. Financial risk management (continued):

Credit risk

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

	December 31, 2018	December 31, 2017
Current	$ 30,929	$ 37,786
Past due for 1 to 60 days	2,647	2,635
Past due for more than 60 days	1,289	366
Less: Allowance for losses	(190)	(38)
	$ 34,675	$ 40,749

In accordance with IFRS 9, Pollard has applied the expected credit loss model in evaluating the credit risk associated with its accounts receivable. As part of this analysis, Pollard has grouped its customers into two tranches: government lottery organizations and charitable gaming distribution networks. For sales to government lottery organizations, Pollard has assessed the loss allowance at zero based on the nature of the customer organizations, and no history of losses, collection issues, or significantly overdue receivables, as well as other customer-specific and forward-looking macroeconomic factors. Pollard has performed the same assessment for charitable gaming distribution network customers, resulting in the provision of a loss allowance, as shown in the table above.

Liquidity risk

Liquidity risk is the risk that Pollard will not be able to meet its financial obligations as they fall due.

The following table outlines Pollard's maturity analysis of the undiscounted cash flows, including related interest payments, of certain non-current financial liabilities and leases as of December 31, 2018:

	Total	2019	2020	2021	2022	2023
Long-term debt	$ 129,387	4,818	5,606	118,963	–	–
Operating leases	19,981	5,704	4,887	3,832	3,205	2,353
	$ 149,368	10,522	10,493	122,795	3,205	2,353

28. Financial risk management (continued):

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.

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 by approximately $23 for year ended December 31, 2018 (2017 – $147). A 50 basis point strengthening/weakening in the foreign exchange rate between the Canadian dollar and Euro would decrease/increase the income before income taxes due to changes in operating cashflow by approximately $75 for year ended December 31, 2018 (2017 – $65).

In addition, translation differences arise when foreign currency monetary assets and liabilities are translated at foreign exchange rates that change over time. As at December 31, 2018, the amount of financial liabilities denominated in U.S. dollars exceeded the amount of financial assets denominated in U.S. dollars by approximately $36,147 (2017 – $1,305). 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 $181 for the year ended December 31, 2018 (2017 – $7).

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 December 31, 2018, 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 $581 for the year ended December 31, 2018 (2017 – $423).

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Independent Auditors

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Winnipeg, Manitoba

Transfer Agent

Computershare Trust Company of Canada,
Toronto, Ontario

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Gordon Pollard EXECUTIVE CHAIR
Dave Brown [1]
Jerry Gray [1,2]
Garry Leach [1]
John Pollard
Douglas Pollard

[1] Member of the Audit Committee, Compensation Committee and the Governance and Nominating Committee
[2] Lead Director

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CO-CHIEF EXECUTIVE OFFICER

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EXECUTIVE VICE PRESIDENT, CORPORATE DEVELOPMENT

Pedro Melo
EXECUTIVE VICE PRESIDENT, INFORMATION TECHNOLOGY

Riva Richard
GENERAL COUNSEL AND EXECUTIVE VICE PRESIDENT, LEGAL AFFAIRS

Robert Rose
EXECUTIVE VICE PRESIDENT, FINANCE AND CHIEF FINANCIAL OFFICER

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ANNUAL REPORT

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