POLLARD banknote limited

News Release

POLLARD BANKNOTE REPORTS 4TH QUARTER AND ANNUAL FINANCIAL RESULTS

WINNIPEG, Manitoba, March 11, 2020 /CNW/ - Pollard Banknote Limited (TSX: PBL) ("Pollard") today released its financial results for the three months and year ended December 31, 2019, reporting record annual revenue and continued strong income before taxes.

"2019 was a very good year for Pollard, as we continued to invest significantly in expanding our product portfolio and acquiring new expertise, while at the same time generating record financial results," stated John Pollard, Co-Chief Executive Officer. "2019 revenue reached almost $400 million, an impressive level in comparison to our sales of just a few year ago. More importantly our revenue growth has been mirrored by strong earnings growth, with our near record net income of $22 million. Adjusted EBITDA attained a record amount of $54.8 million, not including the impact of the new IFRS lease rules. Prior to our investments in working capital, our operations generated over $52 million in free cashflow, a new record level. This high cash conversion rate allows us to invest in the products and solutions necessary to ensure Pollard remains the thought leader in the industry."

"These financial results reflect the success of our strategic vision of being the partner of choice for the lottery and charitable gaming industries. Our focused approach allows us to provide the best products and solutions to this highly specialized industry and assist organizations in raising more funds for their good causes."

"Over the last three years an important aspect of our vision has been a focus on strategic and accretive acquisitions to supplement our product offering and grow our company. During 2019 we were successful in acquiring our second specialized lottery merchandising operation, with the purchase of Fastrak. Their innovative team has integrated very effectively with our existing Schafer operation, providing a springboard for new ideas to assist lotteries in generating greater retail sales."

"Charitable gaming is undergoing a renaissance with positive retail growth in a number of key jurisdictions after many years of flat or declining sales. Our recently merged operations of American Games and International Gamco continue to capture increased market share and generate revenue growth in the pull-tab and bingo paper sectors."

“Diamond Game has expanded our footprint of egaming machines to over 2,900 machines during the past year and remains focused on expanding the number of states and provinces allowing this gaming solution. While certain jurisdictions changed the economic model lowering our revenue in the short term, at the same time these markets have been opened up to allow more machines. We are hopeful that, over time, the return from a greater number of machines will more than offset the reduction in revenue per machine.”

“Our fourth quarter continued to show strong revenue and earnings, reflecting the cumulative impact of our acquisitions and a record quarter for both sales and production of instant tickets. We achieved $100 million in revenue for only the second time, driven by strong orders from our portfolio of clients and ongoing demand for our proprietary innovative products including our Scratch FX® product line. Our gross profit was $22 million, with our gross margin percentage of 22% consistent with levels achieved throughout 2019, but as expected, slightly lower than our third quarter margin which traditionally features a higher level of premium products in the run up to the pre-holiday selling season. Adjusted EBITDA achieved $12.8 million, not including the impact of IFRS 16.”

“Our gross margin percentage was additionally impacted negatively during the quarter due to certain production inefficiencies stemming from the large increase in instant ticket order volumes impacting our scheduling and throughput. Additional incremental manufacturing costs were incurred to meet the higher demands during a relatively short time frame including higher levels of overtime, increased spoilage and increased freight costs incurred to meet delivery deadlines. We are incrementally expanding our capacity on our existing production lines and increasing our staffing, which will enable us to produce higher volumes more efficiently in 2020.”

“We continued to invest heavily in the development of our digital solutions in the fourth quarter which is reflected in our administration expenses. Although higher than last year, our quarterly expenses in both administration and selling are consistent with the third quarter of 2019. These are important investments in expanding our product portfolio and driving the innovation that is critical for the long-term growth of our business.”

“The lottery and charitable gaming industries remain robust with continued growth at the retail level and increasing interest among our customers for new and innovative ideas to grow their business”, commented Doug Pollard, Co-Chief Executive Officer. “The lottery industry remains very strong with retail customer demand for instant tickets growing steadily. The constantly increasing variety of offerings which include new innovative play themes, multiple price points, specialty features and eye-catching graphics helps to both meet and generate higher consumer demand. With growing needs for more funds to provide for good causes, lotteries are increasingly looking to organizations like Pollard to deliver innovative solutions.”

“Our customer contract portfolio remains strong, with many long-term relationships in place into the future. During 2019 we received a number of renewals of key contracts, including a ten-year extension of our contract with the British Columbia Lottery Corporation, a two-year extension with Loto-Quebec and new renewals with a number of important lotteries including the lotteries of France, Sweden, Michigan and California, and a new secondary contract to provide instant tickets to the Florida Lottery.”

“In March 2020 our warehousing and distribution operations for the Arizona State Lottery went live. This is an important new contract building on our expanded lottery management product offerings and underlining the importance of traditional services in addition to our expanding digital and technological solutions.”

“Our iLottery operations are the undisputed industry leader, culminating in winning Lottery Supplier of the Year from the prestigious eGaming Review. In conjunction with our 50% joint venture partner, our four live operations now include the North Carolina Education Lottery, which began operations in November 2019. Two of our jurisdictions currently sell only draw-based game tickets, such as Powerball®, but this is an important foundational step to ultimately expand and include the sale of other products including e-instant tickets. Our operation with the Michigan Lottery had another record year in 2019 and is contributing significantly to the operations of the Lottery. Our other iLottery clients continue to grow though these initial phases of operation and our joint venture will continue to invest resources to support this early stage industry development. We are aware of a number of other state and provincial lotteries investigating iLottery solutions and, although it will be a slow evolution, we believe ultimately iLottery will play a significant role in the industry.”

“Subsequent to our year-end we completed the acquisition of mkodo Limited, a specialized technology organization focused on providing mobile interfaces and apps exclusively to the lottery and gaming world. We are very pleased to have the mkodo team join Pollard and believe our expanded expertise in this critical area for customer engagement will provide creative solutions to our lottery clients.”

“We are very proud of our success in 2019 and we remain excited about the opportunities going forward,” concluded John Pollard. “Balancing short-term operating success with the investments required for long-term growth is an important commitment for all of us at Pollard. We will not “fall out of love” with our core business of instant tickets and will maintain our ongoing investments to both capitalize on the growing consumer demand for traditional lottery products while, at the same time, developing new solutions such as digital and iLottery innovations. As well, we will continue thoughtfully investigating additional strategic acquisitions to add unique and specialized resources to further expand our portfolio of solutions, enhancing our position as partner of choice to lottery and charitable organizations throughout the world.”

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 tickets based in Canada, the second largest producer of instant tickets in the world and the second largest supplier of charitable gaming products in North America.

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, acquisition costs and contingent consideration fair value adjustments. 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.

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.

HIGHLIGHTS	Three months ended December 31, 2019	Three months ended December 31, 2018
Sales	$ 100.0 million	$ 70.2 million
Gross profit	$ 22.0 million	$ 13.3 million
Gross profit % of sales	*22.0%*	*18.9 %*
Administration expenses	$ 10.9 million	$ 7.9 million
Selling expenses	$ 4.1 million	$ 3.6 million
Net income (loss)	$ 4.6 million	($ 1.9 million)
Net income (loss) per share (basic and diluted)	$ 0.18	($ 0.08)
Adjusted EBITDA*:		
Lotteries and charitable gaming	$ 10.7 million	$ 4.9 million
Diamond Game	$ 2.1 million	$ 2.6 million
Total adjusted EBITDA*	$ 12.8 million	$ 7.5 million

	Year ended December 31, 2019	Year ended December 31, 2018
Sales	$ 397.8 million	$ 331.9 million
Gross profit	$ 91.1 million	$ 75.7 million
Gross profit % of sales	*22.9 %*	*22.8 %*
Administration expenses	$ 40.6 million	$ 32.2 million
Selling expenses	$ 15.9 million	$ 13.4 million
Net income	$ 22.0 million	$ 14.9 million
Net income per share (basic and diluted)	$ 0.86	$ 0.58
Adjusted EBITDA*:		
Lotteries and charitable gaming	$ 45.5 million	$ 38.4 million
Diamond Game	$ 9.3 million	$ 10.4 million
Total adjusted EBITDA*	$ 54.8 million	$ 48.8 million

* excludes impact of IFRS 16 Leases implemented effective January 1, 2019

Results of Operations – Year ended December 31, 2019

SELECTED FINANCIAL INFORMATION

(millions of dollars)	Year ended December 31, 2019	Year ended December 31, 2018
Sales	$397.8	$331.9
Cost of sales	306.7	256.2
Gross profit	91.1	75.7
Administration expenses	40.6	32.2
Selling expenses	15.9	13.4
Other expenses	2.0	0.4
Income from operations	32.6	29.7
Finance costs	7.5	9.8
Finance income	(3.9)	(0.9)
Income before income taxes	29.0	20.8
Income taxes:		
Current	2.1	5.2
Future	4.9	0.7
	7.0	5.9
Net income	$22.0	$14.9
Adjustments:		
Amortization and depreciation	27.1	18.0
Interest	6.4	4.2
Unrealized foreign exchange loss (gain)	(3.3)	4.6
Acquisition costs	1.2	0.8
Severance costs	-	0.4
Contingent consideration fair value adjustment	(0.2)	-
Income taxes	7.0	5.9
Adjusted EBITDA	$60.2	$48.8
Less impact of implementation of IFRS 16 Leases:		
IFRS 16 related depreciation	$4.7	-
IFRS 16 related interest	0.7	-
Total Adjusted EBITDA without IFRS 16 Impact	$54.8	$48.8

	December 31, 2019	December 31, 2018
Total Assets	$352.3	$305.6
Total Non-Current Liabilities	$175.6	$142.9

On February 3, 2020, Pollard completed the previously announced acquisition of mkodo Limited ("mkodo"). On December 6, 2019, Pollard signed a definitive agreement to purchase 100% of the equity of mkodo for a purchase price of £7.8 million prior to standard working capital adjustments and potential future earn-out payments based on certain EBITDA targets. mkodo is a leading provider of digital apps and user interfaces for the lottery and gaming industry.

Results of Operations – Year ended December 31, 2019

Sales

During the year ended December 31, 2019 ("Fiscal 2019" or "2019"), Pollard achieved sales of $397.8 million, compared to $331.9 million in the year ended December 31, 2018 ("Fiscal 2018" or "2018"). Factors impacting the $65.9 million sales increase were:

Higher sales of ancillary lottery products and services increased revenue in Fiscal 2019 by $28.8 million. This increase included the addition of Fastrak and a full year of Schafer in 2019, as well as increased sales of licensed products, iLottery, and digital and loyalty products. Higher instant ticket volumes in 2019 increased revenue by $19.4 million. Pollard achieved record quarterly instant ticket volumes in the fourth quarter of 2019 due to increased orders from existing customers. The fourth quarter of 2018 volumes were substantially lower due to a temporary reduction in customer orders. An increase in the instant ticket average selling price in 2019 further increased sales by $6.5 million. This increase was a result of significant sales of Pollard's proprietary Scratch FX® product and other value-added products in 2019.

Diamond Game's sales decreased slightly in 2019, reducing sales by $0.7 million compared to 2018 due to lower pricing in certain jurisdictions, which took effect midway through 2019. An increase in charitable gaming volumes increased sales by $3.4 million from 2018. In addition, a higher average selling price for charitable gaming products in 2019 further increased sales by $2.2 million.

During Fiscal 2019, Pollard generated approximately 71.8% (2018 – 69.8%) of its revenue in U.S. dollars including a portion of international sales which are priced in U.S. dollars. During Fiscal 2019 the actual U.S. dollar value was converted to Canadian dollars at an average rate of $1.327 compared to an average rate of $1.292 during Fiscal 2018. This 2.7% increase in the U.S. dollar value resulted in an approximate increase of $7.1 million in revenue relative to Fiscal 2018. During 2019 the value of the Canadian dollar strengthened against the Euro resulting in an approximate decrease of $0.7 million in revenue relative to 2018.

Cost of sales and gross profit

Cost of sales was $306.7 million in Fiscal 2019 compared to $256.2 million in Fiscal 2018. Cost of sales was higher as a result of the inclusion of Fastrak and a full year of Schafer in 2019, the increase in instant ticket and charitable gaming volumes, and higher exchange rates on U.S. dollar denominated transactions. Additionally, increased instant ticket manufacturing overheads contributed to the increase in cost of sales in 2019.

Gross profit was $91.1 million (22.9% of sales) in Fiscal 2019 compared to $75.7 million (22.8% of sales) in Fiscal 2018. This increase of $15.4 million in gross profit was primarily the result of the additions of Fastrak and a full year of Schafer in 2019, and higher instant ticket volumes, partially offset by increased manufacturing overheads. Higher charitable gaming sales also contributed to the increase in gross profit. The higher gross profit percentage was due to increased instant ticket volumes and ancillary lottery products and services which was offset by increased production inefficiencies. Gross margin percentage was impacted negatively during the fourth quarter of 2019 due to certain production inefficiencies stemming from a large increase in instant ticket order volumes impacting scheduling. Additional manufacturing costs were incurred to meet the higher demands during this time frame including higher levels of overtime, increased spoilage and increased freight costs.

Administration expenses

Administration expenses increased to $40.6 million in Fiscal 2019 from $32.2 million in Fiscal 2018. The increase of $8.4 million was partially a result of the inclusion of Fastrak and a full year of Schafer in 2019 which increased administration expenses by $2.2 million. In addition, higher compensation expenses to support Pollard’s growth strategies of developing digital innovation products and higher professional fees further increased administration expenses. Professional fees, excluding acquisition costs, were higher by $1.5 million primarily due to higher legal fees incurred by Pollard to defend our intellectual property including certain patents. Acquisition costs were $0.4 million higher in 2019 relative to Fiscal 2018. These increases were partially offset by a $0.4 million reduction in severance costs as compared to 2018.

Selling expenses

Selling expenses increased to $15.9 million in Fiscal 2019 from $13.4 million in Fiscal 2018 primarily due to the addition of Fastrak and a full year of Schafer, as well as higher compensation and contract support costs.

Other expenses

Other expenses increased to $2.0 million in Fiscal 2019 from $0.4 million in Fiscal 2018, primarily due to the increased loss on equity investment as compared to 2018.

Foreign exchange

The net foreign exchange gain was $2.8 million in Fiscal 2019 compared to a net loss of $4.7 million in Fiscal 2018. The 2019 net foreign exchange gain consisted of a $3.3 million unrealized gain primarily 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. Partially offsetting the unrealized foreign exchange gain, Pollard incurred a realized foreign exchange loss of $0.5 million as a result of foreign currency denominated accounts receivable collected being converted into Canadian dollars at unfavorable foreign exchange rates.

The 2018 net foreign exchange loss consisted of a $4.6 million unrealized loss primarily 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.

Adjusted EBITDA

Adjusted EBITDA excluding the impact of IFRS 16 Leases increased to $54.8 million in Fiscal 2019 compared to $48.8 million in Fiscal 2018. The primary reason for the increase of $6.0 million was the increase in gross profit of $19.1 million (net of amortization and depreciation and IFRS 16 impact). This increase was partially offset by higher administration expenses (net of acquisition and severance costs) of $8.4 million, an increase in selling expenses of $2.5 million, an increase in other expenses of $1.6 million and an increase in the realized foreign exchange loss of $0.4 million.

Interest expense

Interest expense increased to $6.4 million in Fiscal 2019 from $4.2 million in Fiscal 2018 primarily as a result of the additional interest expense related to increased long-term debt due to the acquisitions of Schafer and Fastrak, and additional interest expense incurred with the implementation of IFRS 16 effective January 1, 2019 of $0.7 million.

Amortization and depreciation

Amortization and depreciation, including amortization of intangible assets and depreciation of property and equipment, totaled $27.1 million during Fiscal 2019 which increased from $18.0 million during Fiscal 2018. The increase of $9.1 million was partially a result of $4.7 million of former operating lease costs being characterized as depreciation with the implementation of IFRS 16 effective January 1, 2019. The addition of Fastrak and a full year of Schafer, including the amortization and depreciation relating to the identifiable assets acquired, including intangible assets and property, plant and equipment, and higher depreciation and amortization on new equipment and intangible assets increased expenses in 2019.

Income taxes

Income tax expense was $7.0 million in Fiscal 2019, an effective rate of 24.1%, which was lower than our domestic rate of 27.0% due primarily to lower federal income tax rates in the United States and the effect of foreign exchange. Partially offsetting these reductions in effective rate was the non-deductible amounts relating to expenses incurred in the acquisitions.

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 in effective rate was the lower federal income tax rates in the United States.

Net income

Net income was $22.0 million in Fiscal 2019 compared to net income of $14.9 million in Fiscal 2018. The primary reasons for the increase in net income of $7.1 million were the increase in gross profit of $15.4 million and the higher foreign exchange gain of $7.5 million. These increases were partially offset by the higher administration expenses of $8.4 million, the increase in selling costs of $2.5 million, the increase in other expenses of $1.6 million, additional interest expense of $2.2 million and the increase in income tax expense of $1.1 million.

Net income per share (basic and diluted) increased to $0.86 per share in Fiscal 2019 from $0.58 per share in Fiscal 2018.

Results of Operations – Three months ended December 31, 2019

SELECTED FINANCIAL INFORMATION

(millions of dollars)	Three months ended December 31, 2019	Three months Ended December 31, 2018
	(unaudited)	(unaudited)
Sales	$100.0	$70.2
Cost of sales	78.0	56.9
Gross profit	22.0	13.3
Administration	10.9	7.9
Selling	4.1	3.6
Other income	0.2	(0.1)
Income from operations	6.8	1.9
Finance costs	1.6	4.2
Finance income	(1.0)	-
Income (loss) before income taxes	6.2	(2.3)
Income taxes:		
Current (recovery)	(0.9)	(0.4)
Future	2.5	-
	1.6	(0.4)
Net income (loss)	$4.6	($1.9)
Adjustments:		
Amortization and depreciation	7.1	5.3
Interest	1.6	1.2
Unrealized foreign exchange (gain) loss	(1.1)	3.1
Acquisition costs	0.6	0.2
Contingent consideration fair value adjustment	(0.2)	-
Income taxes (recovery)	1.6	(0.4)
Adjusted EBITDA	$14.2	$7.5
Less impact of implementation of IFRS 16 Leases:		
IFRS 16 related depreciation	$1.2	-
IFRS 16 related interest	0.2	-
Adjusted EBITDA excluding IFRS 16 impact	$12.8	$7.5

Results of Operations – Three months ended December 31, 2019

During the three months ended December 31, 2019, Pollard achieved sales of $100.0 million, compared to $70.2 million in the three months ended December 31, 2018. Factors impacting the $29.8 million sales increase were:

Instant ticket sales volumes for the fourth quarter of 2019 were significantly higher, 57%, than the fourth quarter of 2018, which increased sales by $23.7 million. The reasons for this significant increase in instant ticket volumes were two-fold. The fourth quarter of 2019 saw record volumes of instant tickets sold, a result of increased orders from existing customers; while the comparative quarter from 2018 was significantly lower than the quarterly volumes achieved over the past few years. The fourth quarter 2018 reduction was a result of a temporary decline in orders from our customer portfolio as a number of our larger customers had lower orders during the quarter.

Additionally, higher sales of ancillary lottery products and services increased revenue in the fourth quarter of 2019 by $4.7 million. This growth was due to higher sales of licensed products, digital and loyalty products, and iLottery. The addition of Fastrak and a full quarter of Schafer in 2019 further increased ancillary lottery related sales. An increase in the instant ticket average selling price in the quarter compared to the fourth quarter of 2018 further grew sales by $0.8 million. This increase was, in part, a result of significant sales of Pollard's proprietary Scratch FX® product in 2019.

Diamond Game's sales decreased slightly in the fourth quarter of 2019, which reduced sales by $0.5 million when compared to 2018 due to lower pricing in a certain jurisdiction. An increase in charitable gaming volumes increased sales by $0.3 million from 2018. In addition, a higher average selling price for charitable gaming products in 2019 further increased sales by $0.8 million.

During the three months ended December 31, 2019, Pollard generated approximately 70.9% (2018 – 80.5%) 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 2019 the actual U.S. dollar value was converted to Canadian dollars at an average rate of $1.314, compared to an average rate of $1.311 during the fourth quarter of 2018. This 0.2% increase in the value of the U.S. dollar resulted in an approximate increase of $0.1 million in revenue relative to 2018. During the fourth quarter of 2019 the value of the Canadian dollar strengthened against the Euro resulting in an approximate decrease of $0.1 million in revenue relative to 2018.

Cost of sales was $78.0 million in the fourth quarter of 2019 compared to $56.9 million in the fourth quarter of 2018. Cost of sales was higher in the quarter as a result of the substantial increase in instant ticket volumes. In addition, higher ancillary lottery product sales and the inclusion of Fastrak and a full quarter of Schafer in 2019 increased cost of goods sold as compared to the fourth quarter of 2018.

Gross profit was $22.0 million (22.0% of sales) in the fourth quarter of 2019 compared to $13.3 million (18.9% of sales) in the fourth quarter of 2018. This increase in gross profit was primarily the result of the significant increase in instant ticket volumes. Gross margin percentage was significantly higher than the fourth quarter of 2018, with higher margins achieved on instant tickets being partially offset by lower margins in Diamond Game due to the reduction in pricing. Gross margin percentage was impacted negatively during the fourth quarter of 2019 due to certain production inefficiencies stemming from a large increase in instant ticket order volumes impacting scheduling. Additional manufacturing costs were incurred to meet the higher demands during this time frame including higher levels of overtime, increased spoilage and increased freight costs.

Administration expenses increased to $10.9 million in the fourth quarter of 2019 compared to $7.9 million in the fourth quarter of 2018. The increase of $3.0 million was partially a result of the inclusion of Fastrak and a full quarter of Schafer, increasing administration expenses by $0.4 million. Additionally, higher compensation expenses to support Pollard's growth strategies of developing digital innovation products, increased incentive accruals and additional acquisition costs of $0.4 million contributed to the increase. Partially offsetting these increases was a decrease in professional services of $0.4 million. Administration expenses in the fourth quarter of 2019 were similar to the amount incurred in the third quarter of 2019.

Selling expenses increased to $4.1 million in the fourth quarter of 2019 from $3.6 million in the fourth quarter of 2018. The increase was primarily due to the addition of Fastrak and a full quarter of Schafer, as well as higher compensation and contract support costs. Selling expenses in the fourth quarter of 2019 were similar to the amount incurred in the third quarter of 2019.

The net foreign exchange gain was $1.0 million in the fourth quarter of 2019 compared to a net loss of $3.0 million in the fourth quarter of 2018. The 2019 net foreign exchange gain consisted of a $1.1 million unrealized gain primarily as a result of the decreased Canadian equivalent value of U.S. dollar denominated accounts payable and long-term debt due to the strengthening of the Canadian dollar relative to the U.S. dollar. The unrealized foreign exchange gain was partially offset by the 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 exchanges rates.

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 accounts receivable collected being converted into Canadian dollars at favorable foreign exchanges rates.

Adjusted EBITDA excluding the impact of IFRS 16 Leases was $12.8 million in the fourth quarter of 2019 compared to $7.5 million in the fourth quarter of 2018. The primary reason for the $5.3 million increase was the higher gross profit of $9.1 million (net of amortization and depreciation and IFRS 16 impact) due primarily to the increase in instant ticket volumes. This increase was partially offset by the higher administration costs (net of acquisition costs) of $2.6 million, the increase in selling costs of $0.5 million, higher other expenses of $0.3 million and an increase in realized foreign exchange loss of $0.2 million.

Interest expense increased to $1.6 million in the fourth quarter of 2019 from $1.2 million in the fourth quarter of 2018 primarily as a result of the additional interest expense related to increased long-term debt incurred with the acquisitions of Schafer and Fastrak, and additional interest expense incurred with the implementation of IFRS 16 effective January 1, 2019 of $0.2 million for the quarter.

Amortization and depreciation, including amortization of intangible assets and depreciation of property and equipment, totaled $7.1 million during the fourth quarter of 2019 which increased from $5.3 million during the fourth quarter of 2018. The increase was primarily a result of $1.2 million of former operating lease costs being characterized as depreciation with the implementation of IFRS 16 effective January 1, 2019. Also, the addition of Schafer and Fastrak, including the amortization and depreciation relating to the identifiable assets acquired, including intangible assets and property, plant and equipment, and higher depreciation and amortization on new equipment and intangible assets increased expenses in 2019.

Income tax expense was $1.6 million in the fourth quarter of 2019, an effective rate of 25.5% which was lower than our domestic rate of 27.0% due primarily to lower federal income tax rates in the United States and the effect of foreign exchange. Partially offsetting these reductions in effective rate was non-deductible amounts relating to expenses incurred in the acquisitions.

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 reductions in effective rate was the lower federal income tax rates in the United States.

Net income was $4.6 million in the fourth quarter of 2019 compared to net loss of $1.9 million in the fourth quarter of 2018. The primary reasons for the $6.5 million increase in net income were the higher gross profit of $8.7 million, due primarily to the increase in instant ticket volumes, and the increase in the foreign exchange gain of $4.0 million. Partially offsetting these increases were the increase in administration expenses of $3.0 million, higher selling expenses of $0.5 million, additional interest expense of $0.4 million and the increase in income taxes of $2.0 million.

Net income per share (basic and diluted) increased to $0.18 per share in the fourth quarter of 2019 from a loss of $0.08 per share in the fourth quarter of 2018.

Outlook

The lottery and charitable gaming industries remain very healthy with growth at the retail level continuing. In particular, consumer demand for instant tickets, and products and services related to instant tickets, remains strong with a number of factors driving greater retail sales: constantly changing ticket offerings, higher price points, larger and varied prize payouts, eye-catching graphics, licensed themes, innovative merchandising and focused advertising. Growth rates at the manufacturing levels are traditionally lower than growth rates at the retail level however we expect these positive growth rates to continue.

Lotteries are expanding their usage of ancillary products like innovative merchandising options, loyalty programs, digital apps, distribution and warehousing, retail support and other “back office” products. They are exploring more of these solutions, however many remain in development or early stages and lotteries have traditionally been slow to adopt these new methods and ideas. Revenue generated from these solutions are still developing and Pollard will continue to invest the necessary resources for the long-term growth of these products. We believe these products, in addition to the revenues generated directly from their sale, will also increase sales of instant tickets.

The foundation of our business is our instant ticket contract portfolio, which remains very strong. We do not have any major contracts coming due during 2020 but as is typical there are a few of our existing mid-size contracts that regularly come up for bid including in the next twelve months. We are hopeful of retaining or growing the long-term relationships we currently have in place. Our strategy is not to aggressively bid for large contract opportunities simply in order to gain market share, rather we look for opportunities to compete and strategically bid with a focus on positive margins through expanding our higher value and proprietary products.

At the beginning of March 2020 our new instant ticket warehousing and distribution operation for the Arizona Lottery went live. This is just another example of a key ancillary service we can provide lotteries which expands our touches with our clients and helps drive higher instant ticket sales.

A factor in our success has been the development of a number of unique proprietary products that allow our clients to generate greater returns for their good causes. Key examples of these include Scratch FX®, laminated products, such as PlayBooks®, and Clear Play™*.* Our ongoing growth and success in maintaining strong average selling prices on our products depends on our ability to develop more specialty value-added enhancements and we will continue to invest resources to develop more innovative products and services.

Interest in iLottery continues to be active among lotteries in North America. Traditionally, lotteries and state legislatures are slow to make the changes required to enable new revenue streams such as iLottery, and the adoption of these complex operations can take long periods. As a result, we do not anticipate many new iLottery operations going live during the next year. However, we believe in the long term new iLottery implementations will grow as lotteries recognize the critical importance of expanding distribution methods and the positive impact it can have on incremental revenue. Our existing operations in this space continue to develop, with stronger growth in those jurisdictions that allow a broader range of gaming options including selling e-instants versus jurisdictions that only allow the online sale of draw based game tickets.

The charitable gaming market has shown positive growth at the retail level over the last year and this renewed growth translates into additional incremental opportunities for our American Games/International Gamco operations. We have invested resources in additional press capabilities for our pull-tab production and we believe the positive market reception of our combined businesses will continue to provide strong free cashflow. Our Diamond Game operation will continue to focus on new jurisdictions for their charitable egaming machines. The impact of new pricing environments in certain jurisdictions, introduced in 2019, will continue to have a negative impact on a full year basis in 2020, however we believe this will be partially mitigated by our ability to introduce additional machines in these same markets.

We continue to invest heavily in our business through an ongoing capital expenditure program and increasingly, our development of digital solutions and other important intangible assets. We expect CAPEX in 2020 to be at similar or slightly higher levels then expended in 2019. Included in our planned capital expenditures are new egaming machines for our Diamond Game and Oasis operations, however this amount will vary depending on the timing of new jurisdiction implementation. With our continued strong cash conversion from earnings and a large senior debt facility in place, our cash resources allow us to fund required investments while still generating free cash-flow to provide for dividends, investment in working capital and make significant payments in servicing our debt.

On February 1, 2020, we completed the acquisition of mkodo Limited, a specialized technology company focused on mobile apps and user interfaces for the lottery and gaming industry. A key component of our vision is to expand our offerings and expertise through strategic acquisitions. We will continue to pursue appropriate opportunities which are both financially prudent and can enhance our business offerings.

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