June 30, 2017

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

FOR THE THREE AND SIX MONTHS ENDED JUNE 30, 2017

August 9, 2017

This management's discussion and analysis ("MD&A") of Pollard Banknote Limited ("Pollard") for the three and six months ended June 30, 2017, is prepared as at August 9, 2017, and should be read in conjunction with the accompanying unaudited condensed consolidated interim financial statements of Pollard and the notes therein as at June 30, 2017, and the audited consolidated financial statements of Pollard for the year ended December 31, 2016, and the notes therein. Results are reported in Canadian dollars and have been prepared in accordance with International Financial Reporting Standards ("IFRS" or "GAAP").

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, unrealized foreign exchange gains and losses, mark-to-market gains and losses on foreign currency contracts, and certain non-recurring items including start-up 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 unaudited consolidated results of Pollard for the three and six months ended June 30, 2017. 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.

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 gaming, Social Instants™, retail management services and instant ticket vending machines. 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 250 independent distributors with the majority of revenue generated from repeat business.

Product line breakdown of revenue

	Three months ended June 30, 2017	Three months ended June 30, 2016	Six months ended June 30, 2017	Six months ended June 30, 2016
Instant Tickets	91.3%	87.6%	89.4%	88.3%
Charitable Gaming Products	8.7%	12.4%	10.6%	11.7%

Geographic breakdown of revenue

	Three months ended June 30, 2017	Three months ended June 30, 2016	Six months ended June 30, 2017	Six months ended June 30, 2016
United States	60%	58%	58%	57%
Canada	16%	17%	19%	19%
International	24%	25%	23%	24%

The following financial information should be read in conjunction with the accompanying unaudited consolidated financial statements of Pollard and the notes therein as at and for the three and six months ended June 30, 2017.

SELECTED FINANCIAL INFORMATION

(millions of dollars, except per share information)

	Three months ended June 30, 2017	Three months ended June 30, 2016	Six months ended June 30, 2017	Six months ended June 30, 2016
Sales	$77.9	$54.0	$135.3	$118.0
Cost of sales	59.3	43.1	105.3	95.7
Gross profit	18.6	10.9	30.0	22.3
Gross profit as a % of sales	*23.9%*	*20.2%*	*22.2%*	*18.9%*
Administration expenses	6.6	5.1	12.0	10.4
Administration expenses as a % of sales	*8.5%*	*9.4%*	*8.9%*	*8.8%*
Selling expenses	2.1	1.8	4.1	3.7
Selling expenses as a % of sales	*2.7%*	*3.3%*	*3.0%*	*3.1%*
Net income	6.0	2.0	7.8	5.6
Net income as a % of sales	*7.7%*	*3.7%*	*5.8%*	*4.7%*
Adjusted EBITDA	13.1	6.0	19.4	12.8
Adjusted EBITDA as a % of sales	*16.8%*	*11.1%*	*14.3%*	*10.8%*
Net income per share (basic and diluted)	$0.25	$0.09	$0.33	$0.24

	June 30, 2017	December 31, 2016
Total Assets	$173.5	$176.8
Total Non-Current Liabilities	$86.6	$94.4

RECONCILIATION OF NET INCOME TO ADJUSTED EBITDA

(millions of dollars)

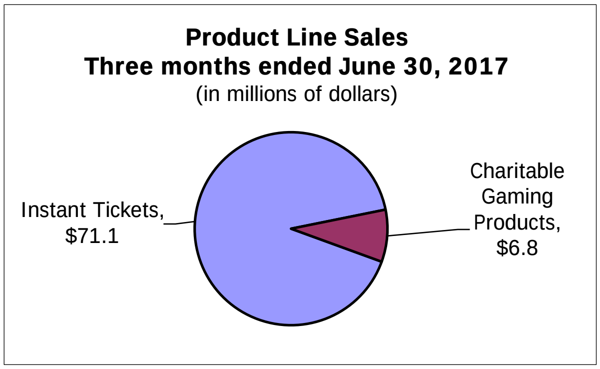
	Three months ended June 30, 2017	Three months ended June 30, 2016	Six months ended June 30, 2017	Six months ended June 30, 2016
Net income	$6.0	$2.0	$7.8	$5.6
Adjustments:				
Amortization and depreciation	2.6	2.9	5.2	5.6
Interest	0.7	0.8	1.5	1.7
Acquisition costs	0.7	-	1.0	-
Unrealized foreign exchange (gain) loss	0.5	(0.9)	0.3	(2.0)
Income taxes	2.6	1.2	3.6	1.9
Adjusted EBITDA	$13.1	$6.0	$19.4	$12.8

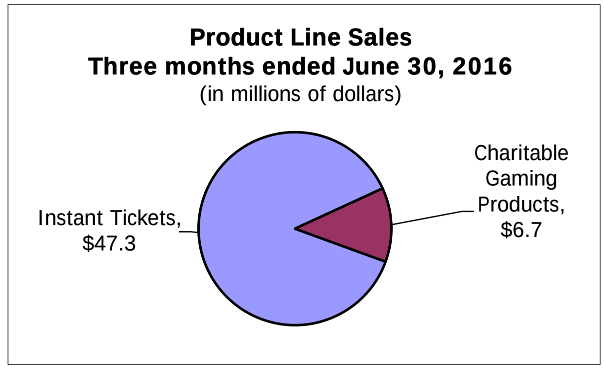
REVIEW OF OPERATIONS

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

ANALYSIS OF RESULTS FOR THE THREE MONTHS ENDED JUNE 30, 2017

Sales

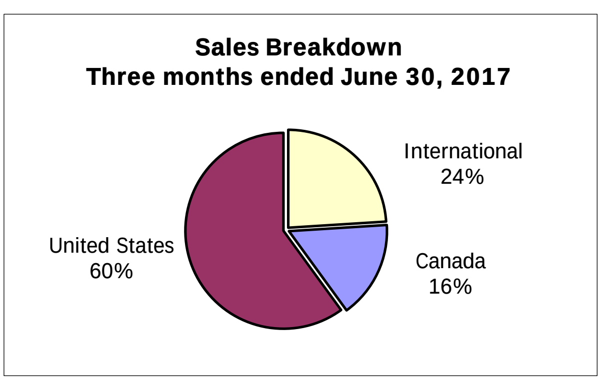


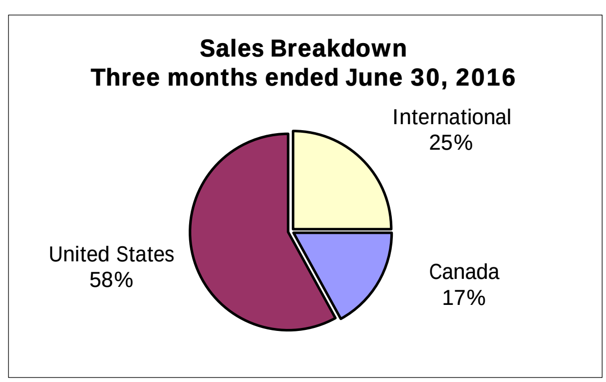


During the three months ended June 30, 2017, Pollard achieved sales of $77.9 million, compared to $54.0 million in the three months ended June 30, 2016. Factors impacting the $23.9 million sales increase were:

Instant ticket sales volumes in the quarter increased significantly when compared to the second quarter of 2016 increasing sales by $19.0 million. The record sales volume was partially a result of a significant amount of goods in transit to international customers at March 31, 2017, being recognized in sales in this quarter, and partially reflective of the record amount of production in the quarter, based on greater orders from existing customers. Sales of ancillary instant ticket products and services increased in 2017, increasing sales by $3.7 million due primarily to higher sales of licensed products as well as from iLottery. An increase in the charitable gaming average selling price improved sales by $0.2 million when compared to the second quarter of 2016.

Partially offsetting these increases was a decrease in the instant ticket average selling price in the second quarter of 2017 compared to the prior year which decreased sales by $1.2 million. A slight decrease in the charitable gaming volumes decreased sales by $0.3 million when compared to the second quarter of 2016.





During the three months ended June 30, 2017, Pollard generated approximately 75.0% (2016 – 69.0%) of its revenue in U.S. dollars including a portion of international sales which are priced in U.S. dollars. During the second quarter of 2017 the actual U.S. dollar value was converted to Canadian dollars at $1.347, compared to a rate of $1.288 during the second quarter of 2016. This 4.5% increase in the U.S. dollar value resulted in an approximate increase of $2.5 million in revenue relative to the second quarter of 2016.

Cost of sales and gross profit

Cost of sales was $59.3 million in the second quarter of 2017 compared to $43.1 million in the second quarter of 2016. Cost of sales were higher in the quarter relative to 2016 as a result of higher volumes of instant tickets, increased ancillary instant ticket products and services sales and the impact of higher exchange rates on U.S. dollar transactions.

Gross profit was $18.6 million (23.9% of sales) in the second quarter of 2017 compared to $10.9 million (20.2% of sales) in the second quarter of 2016. This increase in gross profit was primarily the result of the increase in instant ticket volumes, greater ancillary instant ticket products and services sales and higher exchange rates on net U.S. dollar transactions. The higher gross profit percentage was due to the higher instant ticket volumes, the instant ticket sales mix weighted to higher margin products, increased sales of ancillary instant ticket products and services and improved manufacturing efficiencies.

Administration expenses

Administration expenses increased to $6.6 million in the second quarter of 2017 from $5.1 million in the second quarter of 2016. The increase was primarily a result of $0.7 million in acquisition costs in the second quarter of 2017 compared to 2016 and increased compensation expenses (which primarily related to expansion of our ancillary lottery product and services sales and acquisition efforts) including incentive accruals. This increase was partially offset by lower professional fees, primarily legal costs, of $0.3 million in the first quarter of 2017 compared to the first quarter of 2016.

Selling expenses

Selling expenses increased to $2.1 million in the second quarter of 2017 from $1.8 million in the second quarter of 2016 primarily as a result of increased compensation costs.

Interest expense

Interest expense decreased to $0.7 million in the second quarter of 2017 from $0.8 million in the second quarter of 2016 primarily as a result of lower interest rates and higher cash flow reducing long-term debt in 2017.

Foreign exchange (gain) loss

The net foreign exchange gain was $0.1 million in the second quarter of 2017 compared to a net loss of $0.3 million in the second quarter of 2016. The 2017 net foreign exchange gain of $0.1 million resulted from a $0.6 million realized foreign exchange gain relating to the increased value on the collections of U.S. dollar denominated receivables. Partially offsetting the realized gain was the unrealized foreign exchange loss of $0.5 million, comprised predominately of an unrealized loss on U.S. dollar denominated receivables, partially offset by an unrealized gain on U.S. dollar denominated liabilities.

The 2016 net foreign exchange loss was due to the strengthening of the Canadian dollar. Partially offsetting the realized foreign exchange loss of $1.2 million, relating to the decreased value on the collections of U.S. dollar denominated receivables, was the reversal of $0.9 million unrealized loss recognized in prior quarters.

Adjusted EBITDA

Adjusted EBITDA was $13.1 million in the second quarter of 2017 compared to $6.0 million in the second quarter of 2016. The primary reasons for the increase in Adjusted EBITDA of $7.1 million were the increase in gross profit (net of amortization and depreciation) of $7.4 million and a decrease in realized foreign exchange loss of $1.8 million. These increases were partially offset by the increase in administration costs (net of acquisition costs) of $0.8 million, the increase in selling costs of $0.3 million, the increase in loss of equity investment of $0.4 million and the reduction in other income of $0.5 million.

Income taxes

Income tax expense was $2.6 million in the second quarter of 2017, an effective rate of 30.1%, higher than our expected effective rate of 27.0% due primarily to the impact of permanent differences from non-deductible expenditures.

Income tax expense was $1.2 million in the second quarter of 2016, an effective rate of 36.9%, which was higher than our expected effective rate of 27.0% due primarily to differences relating to the foreign exchange impact relating to permanent differences on the foreign exchange translation of property, plant and equipment and other net liabilities.

Amortization and depreciation

Amortization and depreciation, including amortization of deferred financing costs and intangible assets and depreciation of property and equipment, totaled $2.6 million during the second quarter of 2017 which decreased from $2.9 million during the second quarter of 2016 primarily as a result of decreased depreciation of property, plant and equipment.

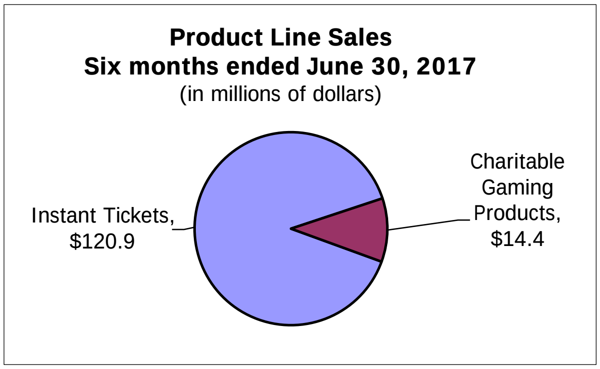
Net income

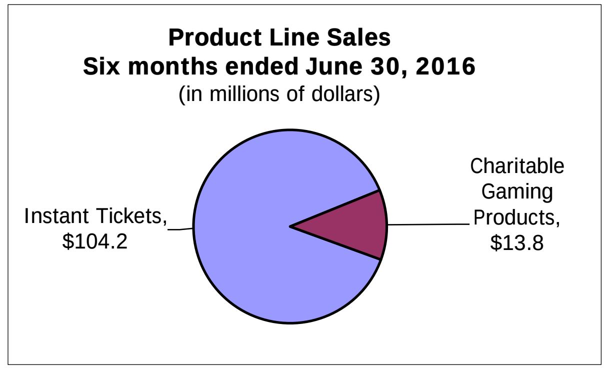
Net income increased to $6.0 million in the second quarter of 2017 from $2.0 million in the second quarter of 2016. The primary reasons for the increase of $4.0 million in net income were the increase in gross profit of $7.7 million and the decrease in foreign exchange loss of $0.4 million. These increases were partially offset by increase in administration expenses of $1.5 million the increase in selling costs of $0.3 million, the increase in loss of equity investment of $0.4 million, the reduction in other income of $0.5 million and the increase in income tax expense of $1.4 million.

Net income per share (basic and diluted) increased to $0.25 per share in the second quarter of 2017 from $0.09 per share in the second quarter of 2016.

ANALYSIS OF RESULTS FOR THE SIX MONTHS ENDED JUNE 30, 2017

Sales

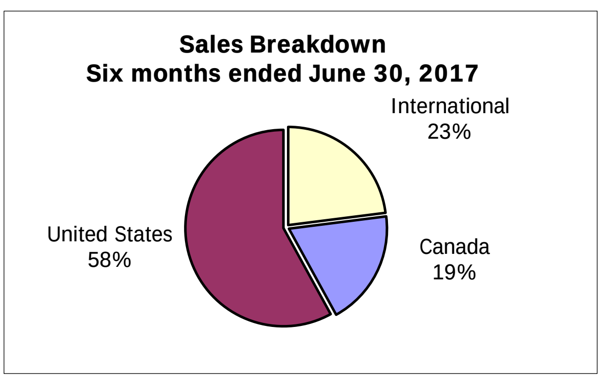


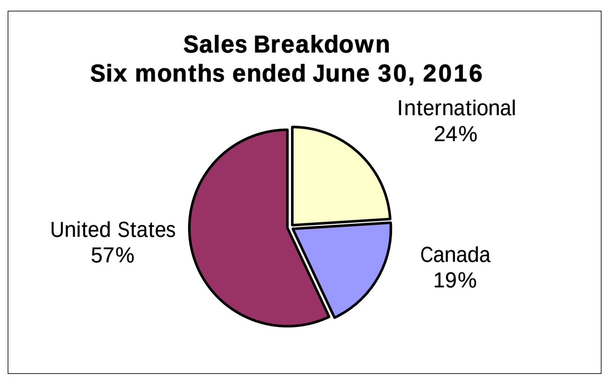


During the six months ended June 30, 2017, Pollard achieved sales of $135.3 million, compared to $118.0 million in the six months ended June 30, 2016. Factors impacting the $17.3 million sales increase were:

Higher instant ticket sales volumes increased sales by $8.8 million in the first six months of 2017 compared to the first six months of 2016 due to a record amount of production this year, based on increased orders from existing customers. Additionally, the higher instant ticket average selling price increased sales by $4.5 million when compared to the first half of 2016.

Higher sales of our ancillary instant ticket products and services increased sales by $3.7 million from the first half of 2016. The increase in sales was due primarily to higher sales of licensed products, greater revenues from iLottery and added sales from our loyalty solution. These increases were partially offset by the reduction in lottery management systems sales compared to the prior year. An increase in the charitable gaming average selling price increased sales by $0.6 million when compared to the first half of 2016.





During the six months ended June 30, 2017, Pollard generated approximately 72.1% (2016 – 70.0%) of its revenue in U.S. dollars including a portion of international sales which are priced in U.S. dollars. During the first six months of 2017 the actual U.S. dollar value was converted to Canadian dollars at $1.339, a similar rate to the first six months of 2016. As a result, there was no change in sales resulting from changes in the U.S. dollar value. However, during the first half of 2017, the value of the Euro weakened against the Canadian dollar resulting in an approximate decrease of $0.3 million in revenue relative to the first half of 2016.

Cost of sales and gross profit

Cost of sales was $105.3 million in the six months ended June 30, 2017, compared to $95.7 million in the six months ended June 30, 2016. Cost of sales was higher in the first half of 2017 relative to 2016 as a result of higher volumes of instant tickets and increased ancillary instant ticket products and services sales.

Gross profit increased to $30.0 million (22.2% of sales) in the six months ended June 30, 2017, from $22.3 million (18.9% of sales) in the six months ended June 30, 2016. This increase in gross profit was primarily the result of the increase in instant ticket volumes and higher ancillary instant ticket products and services sales. The higher gross profit percentage was due to the larger volumes of instant tickets, the instant ticket sales mix weighted to higher margin products, increased sales of ancillary instant ticket products and services and improved manufacturing efficiencies.

Administration expenses

Administration expenses increased to $12.0 million in the first six months of 2017 from $10.4 million in the first six months of 2016. The increase was a result of $1.0 million in acquisition costs in the first half of 2017 compared to 2016 and increased compensation expenses (which primarily related to expansion of our ancillary lottery product and services sales and acquisition efforts) including incentive accruals. This increase was partially offset by lower professional fees, primarily legal costs, which were lower by $1.0 million in the first quarter of 2017 compared to the first quarter of 2016.

Selling expenses

Selling expenses increased to $4.1 million in the first six months of 2017 from $3.7 million in the first six months of 2016 primarily as a result of increased compensation costs.

Interest expense

Interest expense decreased to $1.5 million in the first six months of 2017 from $1.7 million in the first six months of 2016 primarily as a result of lower interest rates and higher cash flow reducing long-term debt in 2017.

Foreign exchange (gain) loss

The net foreign exchange gain was $nil in the first six months of 2017 compared to a net gain of $0.7 million in the first half of 2016. The 2017 foreign exchange gain resulted from a net unrealized foreign exchange loss of $0.3 million, comprised predominately of an unrealized loss on U.S. denominated receivables, partially offset by an unrealized gain on U.S. denominated liabilities. The unrealized loss was fully offset by a realized gain of $0.3 million, relating to the increased value on the collections of U.S. dollar denominated receivables.

The 2016 foreign exchange gain resulted from unrealized foreign exchange gain of $2.0 million, comprised predominately of an unrealized gain on U.S. dollar denominated debt (caused by the strengthening of the value of the Canadian dollar versus the U.S. dollar) in addition to an unrealized gain on other U.S. dollar denominated accounts payable. The unrealized gain was partially offset by a realized loss of $1.3 million, relating to the decreased value on the collections of U.S. dollar denominated receivables.

Adjusted EBITDA

Adjusted EBITDA was $19.4 million in the first six months of 2017 compared to $12.8 million in the first six months of 2016. The primary reason for the increase in Adjusted EBITDA of $6.6 million were the increase in gross profit (net of amortization and depreciation) of $7.3 million and a decrease in realized foreign exchange loss of $1.6 million. These increases were partially offset by the increase in administration costs (net of acquisition costs) of $0.6 million, the increase in selling costs of $0.4 million, the increase in loss of equity investment of $0.6 million and the reduction in other income of $0.6 million.

Income taxes

Income tax expense was $3.6 million in the first six months of 2017, an effective rate of 31.6%, which was higher than our expected effective rate of 27.0% due primarily to the impact of permanent differences from non-deductible expenditures.

Income tax expense was $1.9 million in the first six months of 2016, an effective rate of 24.7%, which was lower than our expected effective rate of 27.0% due primarily to differences relating to the foreign exchange impact of Canadian dollar denominated debt in its U.S. subsidiaries. Pollard has capitalized its U.S. operations using intercompany Canadian dollar debt. The strengthening of the Canadian dollar versus the U.S. dollar results in a future loss on debt repayment for U.S. tax purposes in the subsidiary, creating a deferred tax recovery with no related income (as the loss is eliminated on consolidation). This decreased the effective tax rate by approximately 13 percentage points. Other differences relating to permanent differences on the foreign exchange translation of property, plant and equipment, and other net liabilities increased the effective tax rate by approximately 10 percentage points on a net basis.

Amortization and depreciation

Amortization and depreciation, including amortization of deferred financing costs and intangible assets and depreciation of property and equipment, totaled $5.2 million during the first six months of 2017 which decreased from $5.6 million during the first six months of 2016 primarily as a result of decreased depreciation of property, plant and equipment.

Net income

Net income increased to $7.8 million in the first six months of 2017 from $5.6 million in the first six months of 2016. The primary reason for the increase was the increase in gross profit of $7.7 million. This increase was partially offset by the increase in administration expenses of $1.6 million, the increase in selling costs of $0.4 million, the increase in loss of equity investment of $0.6 million, the reduction in other income of $0.6 million, the decrease in foreign exchange gain of $0.7 million and the increase in income tax expense of $1.7 million.

Net income per share (basic and diluted) increased to $0.33 per share in the six months ending June 30, 2017, as compared to $0.24 per share in the six months ending June 30, 2016.

Liquidity and Capital Resources

Cash provided by operating activities

For the six months ended June 30, 2017, cash flow provided by operating activities was $17.4 million compared to cash flow provided by operating activities of $4.6 million for the first six months of 2016. Higher net income before income taxes after non-cash adjustments in the first six months of 2017 contributed to an increase in cash provided by operating activities compared to 2016. For the six months ended June 30, 2017, changes in the non-cash component of working capital increased cash by $3.2 million. The increase was due primarily to the decreased investment in accounts receivables and an increase in accounts payable and accrued liabilities, partially offset by an increase prepaid expenses. For the six months ended June 30, 2016, changes in the non-cash component of working capital decreased cash by $5.5 million. The decrease was due primarily to the increased investment in accounts receivables and inventories, partially offset by increased accounts payable and accrued liabilities.

Cash used for interest decreased to $1.4 million in 2017 as compared to $1.6 million in 2016. Cash used for pension plan contributions increased to $2.0 million in 2017 as compared to $1.5 million in 2016. Cash used for income tax payments increased to $4.0 million in 2017 from $1.3 million in 2016. Cash payments in 2017 included the final installment for the 2016 tax year and initial installments for 2017. Increasing income in 2016 resulted in this higher installment requirement.

Cash used for investing activities

In the six months ended June 30, 2017, cash used for investing activities was $3.4 million compared to cash used of $3.0 million in the first half of 2016. In the six months ended June 30, 2017, capital expenditures were $1.8 million. In addition, Pollard expended $1.0 million on its investment in its iLottery joint venture and $0.6 million on additions to intangible assets.

In the six months ended June 30, 2016, capital expenditures were $2.3 million. In addition, Pollard expended $0.6 million on its investment in its iLottery joint venture and $0.5 million on additions to intangible assets. Proceeds from the sale of Pollard's investment in associate provided cash of $0.5 million.

Cash used for financing activities

Cash used for financing activities was $15.0 million in the six months ended June 30, 2017, compared to cash used for financing activities of $0.1 million in the six months ended June 30, 2016.

During the first half of 2017 cash was used to repay $13.0 million of long-term debt, $0.7 million of subordinated debt, decrease other non-current liabilities by $0.2 million and pay dividends of $1.4 million.

During the first half of 2016 cash proceeds from long-term debt of $1.6 million were offset by $0.1 million of financing costs and dividends paid of $1.4 million.

As at June 30, 2017, Pollard had unused credit facility of $61.9 million, in addition to $6.2 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.

Quarterly Information
(unaudited)
(millions of dollars)

	Q2 2017	Q1 2017	Q4 2016	Q3 2016	Q2 2016	Q1 2016	Q4 2015	Q3 2015	Q2 2015
Sales	$77.9	$57.4	$65.7	$62.7	$54.0	$64.0	$57.2	$57.9	$51.5
Adjusted EBITDA	13.1	6.3	9.1	7.8	6.0	6.8	6.3	7.5	6.3
Net Income	6.0	1.8	3.8	2.8	2.0	3.6	1.2	1.9	3.0

Q2 2017 sales, Adjusted EBITDA and net income were all higher as a result of higher instant ticket volumes.

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 impact significantly 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 June 30, 2017, Pollard's investment in non-cash working capital decreased $3.2 million compared to December 31, 2016, primarily as a result of decreased investment in accounts receivables and an increase in accounts payable and accrued liabilities, partially offset by an increase prepaid expenses.

	June 30, 2017	December 31, 2016
Working Capital	$43.0	$49.5
Total Assets	$173.5	$176.8
Total Non-Current Liabilities	$86.6	$94.4

Credit Facility

Pollard's credit facility was renewed effective June 22, 2017. The credit facility provides loans of up to $105.0 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 $105.0 million Canadian equivalent. The credit facility also includes an accordion feature which can increase the facility by $15 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 June 30, 2017, the outstanding letters of guarantee were $1.3 million. The remaining balance available for drawdown under the credit facility was $61.9 million.

Under the terms and conditions of the credit facility agreement Pollard is required to maintain certain financial covenants including working capital ratios, debt to income before interest, income taxes, amortization and depreciation ("Adjusted EBITDA") ratios and certain debt service coverage ratios. As at June 30, 2017, 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. The facility can be prepaid without penalties. Under the terms of the agreement the facility was committed for a two year period, renewable June 22, 2019.

Pollard believes that its credit facility, subordinated loan from Pollard Equities Limited 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 Loan

On April 2, 2014, Pollard entered into a loan agreement with Pollard Equities Limited ("Equities") for a subordinated term loan facility with a seven year term in the amount of $6.8 million. Equities owns approximately 73.5% of Pollard's outstanding shares.

Quarterly principal payments on the subordinated loan facility commenced the quarter following June 30, 2016. Interest on the subordinated debt commenced with the first draw at a rate of 9%. The loan is fully subordinated to the secured credit facility. The subordinated term loan may be prepaid at any time, subject to certain financial covenants under the secured credit facility.

Outstanding Share Data

As at June 30, 2017 and August 9, 2017, outstanding share data was as follows:

Common shares	23,543,158

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 March 13, 2017, the Board of Directors approved the award of 125,000 options to purchase common shares of Pollard for certain key management personnel. The options were granted on April 24, 2017 and have a seven year term, vesting 25% per year over the first four years. The exercise price of the options was equal to the closing price of the common shares on April 21, 2017. As at June 30, 2017, the total share options outstanding were 250,000.

Contractual Obligations

There have been no material changes to Pollard's contractual obligations since December 31, 2016, that are outside the normal course of business, other than noted below.

Pension Obligations

For the quarter ending June 30, 2017, Pollard recorded a remeasurement loss of $4.6 million (net of $1.8 million of income tax reduction) on its defined pension plans. The remeasurement loss resulted from a decrease in the discount rate, partially offset by remeasurement gains arising on plan assets.

Pollard sponsors four non-contributory defined benefit pension plans, of which three are final pay plans and one is a flat benefit plan. One of Pollard's Canadian pension plans required a solvency valuation as of December 31, 2016. Preliminary estimates from the valuation suggest an estimated deficit of approximately $10.1 million, due the low current levels of the mandated interest rate used to discount the future liabilities. As a result Pollard will be subject to additional special pension plan payments beginning in the third quarter of 2017 of approximately $1.1 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.

Off-Balance Sheet Arrangements

There have been no material changes to Pollard's off-balance sheet arrangements since December 31, 2016, that are outside the normal course of business.

Financial Instruments

The financial instruments of Pollard remain substantially unchanged from those identified in the MD&A for Pollard for the year ended December 31, 2016.

Critical Accounting Policies and Estimates

The preparation of the financial statements in conformity with GAAP requires management to make estimates and assumptions that affect the reported amounts of assets and liabilities and disclosure of contingent assets and liabilities at the dates of the financial statements and the reported amounts of revenue and expenses during the reporting period. Management of Pollard regularly reviews its estimates and assumptions based on historical experience and various other assumptions that it believes would result in reasonable estimates given the circumstances. Actual results could differ from those estimates under different assumptions. The following is a discussion of accounting policies which require significant management judgment and estimation.

Impairment of goodwill

Goodwill represents the excess of the purchase price over the fair value of the net assets acquired of Pollard's U.S. subsidiaries and the excess purchase price over the underlying carrying amount of the portion of the net assets sold as at August 5, 2005, as part of the 26.7% of Pollard sold in conjunction with the IPO, and is not amortized. Goodwill is subject to an annual impairment review. 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 and also to choose a suitable discount rate in order to calculate the present value of those cash flows.

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.

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.

Related Party Transactions

In August 2017, as a result of the purchase of shares in INNOVA Gaming Group Inc., Equities advanced Pollard $22.4 million in funds to partially finance the acquisition. The funds are fully subordinated to the secured credit facility, are to be amortized over 7 years and bear interest at 8%. Other than this financing transaction, Pollard has not entered into any other significant transactions with related parties during the six months ended June 30, 2017, which are not disclosed in the unaudited condensed consolidated interim financial statements.

Industry Risks and Uncertainties

The risk factors affecting Pollard remain substantially unchanged from those identified in the MD&A for Pollard for the year ended December 31, 2016.

Purchase of INNOVA Gaming Group Inc.

On April 17, 2017, Pollard announced that a wholly-owned subsidiary formally commenced an offer (the "Offer") to acquire all of the issued and outstanding common shares ("Shares") of INNOVA Gaming Group Inc. ("INNOVA"), a provider of gaming systems to the North American gaming industry. On June 30, 2017, INNOVA's Board of Directors unanimously recommended that the shareholders of INNOVA accept Pollard's revised offer of cash consideration of $2.50 per Share.

On August 3, 2017, the final day of the original offer, Pollard acquired 17,929,021 Shares (89.3%) of INNOVA, for consideration of $44.8 million. The Offer is subject to a mandatory minimum extension for the remaining shareholders of INNOVA to tender their shares, which will expire August 15, 2017.

Assuming the remaining 2,144,878 shares are tendered, additional incremental consideration of $5.4 million will be paid.

In the three and six months ended June 30, 2017, Pollard expensed acquisition costs of $0.7 million and $1.0 million respectively. These costs are included in administration expenses. Pollard anticipates expending an additional $1.5 million in acquisition costs in the third quarter.

In addition to cash resources and unused credit facility available for drawdown, Equities has committed to provide an additional subordinated term loan, up to $25.1 million, to assist in the financing of this acquisition. This subordinated term loan will bear interest at 8%, with all other terms consistent with the existing subordinated term loan.

The allocation of the purchase price to acquired assets and liabilities is to be determined.

Outlook

Our outlook for the lottery industry, and in particular the market for instant tickets, continues to be very positive. Consumer demand for lottery products including instant tickets is strong and lotteries continue to look for new ways to generate additional funds to support their good causes. This includes looking at new distribution methods and developing unique and innovative products, in addition to maximizing the effectiveness of the traditional instant win scratch lottery tickets. Sales of instant tickets continue to grow across many jurisdictions and we anticipate this trend to continue.

Our volume expectation for 2017 remains strong. We anticipate we will remain at similar levels to those achieved in the first half of the year. Longer term, we are confident our success in the marketplace, combined with our additional available capacity, is a solid recipe for continued long term volume growth.

As noted previously our second quarter revenue figures and related earnings numbers were positively impacted by the tickets in transit at the end of the first quarter being recognized in revenue in the second quarter, an impact that is not expected to be recurring. As a result our revenue and related earnings figures in the near term should be more consistent with results generated by the first half of 2017 in total rather than the second quarter taken in isolation.

Our current contract portfolio remains solid with no major existing contracts coming due in the next year, while conversely there are a number of major lotteries for which Pollard does not have a contract (or is only a minor secondary supplier) which have contacts that are expiring in the next 18 months. This presents an opportunity for us to bid strategically on these new contracts.

A factor in our improved results was our ongoing improvements in our manufacturing efficiencies. Increasing production volumes allow a certain amount of margin leverage relative to our fixed costs, but also our continued improvements in the operation of our Tresu press in our Ypsilanti facility played an important role in our improved cost structure and we expect this trend to continue.

Approximately 60% to 70% of our revenue is sourced in U.S. dollars and changes in the exchange rate between the Canadian and U.S. dollar will have an impact on our financial results. Recently the Canadian dollar has strengthened considerably relative to the U.S. dollar and assuming that trend continues, there will be a negative impact on our financial results. Over time we have transitioned substantial cost inputs into U.S. dollars as a natural hedge which helps mitigate the net impact, including the costs relating to our facilities in the United States as well as significant amounts of our manufacturing inputs utilized in our Canadian facilities.

On August 3, 2017, we acquired 17,929,021 common shares (89.3%) of INNOVA Gaming Group Inc. in conjunction with our board supported bid to acquire the company. The mandatory 10 day extension for the remaining shareholders to tender their shares will end August 15, 2017. We encourage all remaining shareholders to tender their shares in accordance with the bid instructions. We expect to commence the normal steps to privatize the company upon completion of the extension. We look forward to combining the two businesses going forward, which will include consolidating INNOVA's financial results with Pollard Banknote starting in the third quarter of 2017. In addition we remain committed to growth through external acquisitions where appropriate and remain very active in sourcing and investigating ongoing opportunities.

Our budgeted capital expenditures for the remainder of 2017 should remain at similar levels as experienced the first half of the year, with no major projects anticipated. Strong positive cash flow is expected going forward, which will provide us with important flexibility to invest in the areas of our business as needed, manage our debt levels and provide us appropriate financing to pursue and complete acquisitions.

In the second quarter our growth resulted in the use of a portion of our free cash flow to increase working capital. As is typical in our business, our investment in working capital does vary quarter to quarter based on the timing of shipments and the impact of few in number but large individual dollar sized transactions. Over a period of time we expect the variation in working capital levels to stabilize, allowing our free cash flow to be used for additional investments in our business.

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") for the interim period regarding the design of the disclosure controls and procedures. Pollard's management, with the participation of the Certifying Officers of Pollard, has concluded that the design of the disclosure controls and procedures as defined in National Instrument 52-109 will provide reasonable assurance of achieving the disclosure objectives.

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 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 design of the internal controls over financial reporting as defined in National Instrument 52-109 will provide reasonable assurance of achieving the financial reporting objectives.

No changes were made in Pollard's internal control over financial reporting during the three and six months ended June 30, 2017, 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 of Pollard for the year ended December 31, 2016, is available on SEDAR at www.sedar.com.

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