POLLARD banknote limited

News Release

POLLARD BANKNOTE REPORTS 3RD QUARTER FINANCIAL RESULTS

WINNIPEG, Manitoba, November 9, 2022 /CNW/ - Pollard Banknote Limited (TSX: PBL) ("Pollard") today released its financial results for the three and nine months ended September 30, 2022.

Results and Highlights for the Third Quarter ended September 30, 2022

- Sales reached $125.5 million, a quarterly record, up 7.4% from the third quarter of 2021
- Combined sales(1) in the quarter, including our share of our NeoPollard Interactive LLC ("NPi") joint venture's sales, reached $139.2 million, up 9.9% from the $126.7 million achieved in 2021
- Income from operations was $6.7 million, compared to $4.4 million in the third quarter of 2021
- Adjusted EBITDA(1) achieved in the third quarter of 2022 of $20.2 million, increased from $19.4 million in the third quarter of 2021
- iLottery operations continued to demonstrate strong organic growth and the impact of a large Mega Millions® jackpot resulting in record quarterly earnings of $8.2 million
- Charitable gaming and eGaming systems businesses continue to benefit from strong demand, providing a very positive impact on revenues and earnings
- Our instant ticket production volumes increased from the second quarter, with production volumes achieving a quarterly record
- Retail dollar sales of instant tickets remain at the high levels achieved in 2021 and earlier in 2022
- Ongoing inflationary cost increases on our key instant ticket inputs (paper, ink and freight) continue to place negative pressure on our margins
- Our instant ticket average selling price was higher in the third quarter due to a greater mix of higher value and option work for the holiday season
- We continue to pursue our strategy of increasing selling prices on contract extensions and RFP's to help mitigate inflationary cost increases and, ultimately over time, the success of this strategy will help our instant ticket margins return to the levels achieved in prior years

(1) See Non-GAAP measures for explanation

"Our third quarter results generated improved numbers compared to the third quarter of 2021 and the previous quarters of 2022, due to strong demand across all of our main product categories," stated John Pollard, Co-Chief Executive Officer. "Charitable gaming, both printed products and eGaming systems, continues to generate higher revenue and earnings, addressing the significant consumer demand for our product offerings."

"Our instant ticket business attained a quarterly production volume record. This was a nice return to more efficient production following some challenges in the second quarter, which negatively impacted production. Fewer mechanical issues and, while still a challenge, our ability to staff and maintain full operations throughout our production facilities improved in the third quarter."

"Notwithstanding the positive demand for our instant ticket products, the inflationary increases in prices of key inputs such as paper, ink and freight, which began in the later part of 2021, continued to put significant negative pressure on our margins throughout the third quarter. Previously announced supplier price increases on our inputs came into effect in the third quarter, with additional, albeit smaller, price increases still to come in the fourth quarter. As we disclosed in previous quarters, our instant ticket contracts average around 4 years in length, with primarily fixed prices for the entirety of the term. As such, it is very difficult to pass on input cost increases in the short term."

"One of our key strategies to offset these significant inflationary input cost increases is through raising our selling prices during contract extensions and RFP's as they come up for bid. While still early in the process, we have had a number of successes retaining work at higher pricing in new bid situations, reflective of the input cost increases we have to absorb. Indications within the marketplace so far appear to confirm the industry recognizes the need to adjust pricing and we believe this will continue."

"Most new contracts are awarded in advance of the end of the existing contract's term and come into effect sometime in the future. Therefore, most of the price changes we have already negotiated will be implemented throughout 2023. However, ultimately, these higher prices will allow us to improve our margins on our instant ticket business. We also continue to diligently review our customer profiles to identify opportunities to focus our efforts on more profitable clients, which may result in lower volumes as we reduce sales to lower margin clients."

"Our iLottery operations grew both revenue and earnings, driven in part by ongoing organic growth experienced over the past few quarters, plus the impact of a large U.S. draw-based jackpot in July, which drove higher sales and increased the number of new customers on our U.S. platforms. Our iLottery operations generated earnings of $8.2 million in the third quarter, which was a new quarterly record. While the jackpot spike certainly helped this terrific achievement, the ongoing sales strength retained after the large jackpot was won is testament to the growth we are seeing in this business segment."

"Our charitable gaming operations, including both paper-based products and eGaming systems, continue to turn out tremendous results," noted Doug Pollard, Co-Chief

Executive Officer. "The charitable gaming industry is becoming increasingly focused on innovative products to address consumer demand in conjunction with raising funds for important good causes. The growth of our eGaming systems, which make gaming in social settings such as bars and fraternal organizations available, is a great example of working in partnership with charities to help them achieve their fundraising goals."

"One of our new instant ticket in-lane retailing innovations debuted recently in Arizona, allowing the lottery to enable consumers to purchase their instant tickets while in-lane in large multi-lane retail environments, rather than using a separate vending machine or having to go to a dedicated kiosk. This new distribution method is a significant development in expanding the retailing of instant tickets and our focus on innovation. We are very confident in its future success."

"The fundamentals of all of our business lines remain very strong," concluded John Pollard, "and we are confident that our higher pricing strategy for instant tickets will, over time, allow us to increase our margins back to historic levels. We believe our charitable gaming operations will continue their market leadership and generate excellent results, and the large investments we are making in the digital areas are laying the foundation for further growth, in partnership with our lottery and charitable gaming customers."

Use of GAAP and Non-GAAP Financial Measures

The selected financial and operating information has been derived from, and should be read in conjunction with, the unaudited condensed consolidated financial statements of Pollard as at and for the three and nine months ended September 30, 2022. These financial statements have been prepared in accordance with the International Financial Accounting Standards ("IFRS" or "GAAP").

Reference to "EBITDA" is to earnings before interest, income taxes, depreciation, amortization and purchase accounting amortization. Reference to "Adjusted EBITDA" is to EBITDA before unrealized foreign exchange gains and losses, and certain non-recurring items including acquisition costs, litigation settlement costs, contingent consideration fair value adjustments and insurance proceeds (net). 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.

Reference to "Combined sales" is to sales recognized under GAAP plus Pollard's 50% proportionate share of NeoPollard Interactive LLC's ("NPi") sales, its iLottery joint venture operation. Reference to "Combined iLottery sales" is to sales recognized under GAAP for Pollard's 50% proportionate share of its Michigan Lottery joint iLottery operation plus Pollard's 50% proportionate share of NPi' s sales, its iLottery joint venture operation.

EBITDA, Adjusted EBITDA, Combined sales and Combined iLottery sales are measures not recognized under GAAP and do not have a standardized meaning prescribed by GAAP. Therefore, these measures may not be comparable to similar measures presented by other entities. Investors are cautioned that EBITDA, Adjusted EBITDA, Combined sales and Combined iLottery sales should not be construed as alternatives to net income or sales as 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.

POLLARD BANKNOTE LIMITED

Pollard is one of the leading providers of products and solutions to lottery and charitable gaming industries throughout the world. Management believes Pollard is the largest provider of instant tickets based in Canada and the second largest producer of instant tickets in the world. In addition, management believes Pollard is also the second largest bingo paper and pull-tab supplier to the charitable gaming industry in North America and, through its 50% joint venture, the largest supplier of iLottery solutions to the U.S. lottery market.

HIGHLIGHTS	Three months ended September 30, 2022	Three months ended September 30, 2021[(1)]
Sales	$ 125.5 million	$ 116.9 million
Gross profit	$ 20.6 million	$ 22.7 million
Gross profit % of sales	*16.4%*	*19.4%*
Administration expenses	$ 12.5 million	$ 12.1 million
Selling expenses	$ 4.5 million	$ 4.5 million
NPi equity investment income	($ 6.0 million)	($ 2.6 million)
Other expenses	$ 2.9 million	$ 4.3 million
Unrealized foreign exchange loss	$ 4.9 million	$ 2.2 million
Net loss	($ 0.2 million)	($ 0.6 million)
Net loss per share – basic and diluted	($ 0.01)	($ 0.02)
Adjusted EBITDA	$ 20.2 million	$ 19.4 million

(1) Certain comparative figures have been reclassified to conform to the presentation adopted in the current period.

	Nine months ended September 30, 2022	Nine months ended September 30, 2021[(1)]
Sales	$ 355.3 million	$ 342.5 million
Gross profit	$ 63.8 million	$ 70.4 million
Gross profit % of sales	*18.0%*	*20.6%*
Administration expenses	$ 36.9 million	$ 35.3 million
Selling expenses	$ 13.4 million	$ 12.6 million
NPi equity investment income	($ 15.0 million)	($ 9.1 million)
Other expenses	$ 3.7 million	$ 2.8 million
Unrealized foreign exchange (gain) loss	$ 6.6 million	($ 0.3 million)
Net income	$ 8.7 million	$ 14.5 million
Net income per share – basic and diluted	$ 0.32	$ 0.54
Adjusted EBITDA	$ 58.1 million	$ 65.3 million

(1) Certain comparative figures have been reclassified to conform to the presentation adopted in the current period.

SELECTED FINANCIAL INFORMATION

(millions of dollars)	Three months ended September 30, 2022	Three months ended September 30, 2021(1)	Nine months ended September 30, 2022	Nine months ended September 30, 2021(1)
	(unaudited)	(unaudited)	(unaudited)	(unaudited)
Sales	$125.5	$116.9	$355.3	$342.5
Cost of sales	104.9	94.2	291.5	272.1
Gross profit	20.6	22.7	63.8	70.4
Administration expenses	12.5	12.1	36.9	35.3
Selling expenses	4.5	4.5	13.4	12.6
Equity investment income	(6.0)	(2.6)	(15.0)	(9.1)
Other expenses	2.9	4.3	3.7	2.8
Income from operations	6.7	4.4	24.8	28.8
Foreign exchange loss	4.7	1.7	6.9	1.5
Interest expense	2.0	1.2	5.9	3.4
Income before income taxes	0.0	1.5	12.0	23.9
Income taxes:				
Current	2.9	4.2	8.4	13.3
Deferred reduction	(2.7)	(2.1)	(5.1)	(3.9)
	0.2	2.1	3.3	9.4
Net income (loss)	($0.2)	($0.6)	$8.7	$14.5
Adjustments:				
Amortization and depreciation	10.1	9.6	29.5	28.8
Interest	2.0	1.2	5.9	3.4
Income taxes	0.2	2.1	3.3	9.4
EBITDA	$12.1	$12.3	$47.4	$56.1
Unrealized foreign exchange (gain) loss	4.9	2.2	6.6	(0.3)
Contingent consideration fair value adjustment	3.2	4.9	4.1	6.0
Litigation settlement cost	0.0	0.0	0.0	2.5
Acquisition costs	0.0	0.0	0.0	1.0
Adjusted EBITDA	$20.2	$19.4	$58.1	$65.3

(1) Certain comparative figures have been reclassified to conform to the presentation adopted in the current period.

	September 30, 2022	December 31, 2021
Total Assets	$481.4	$461.4
Total Non-Current Liabilities	$161.3	$163.5

Results of Operations – Three months ended September 30, 2022

During the three months ended September 30, 2022, Pollard achieved sales of $125.5 million, compared to $116.9 million in the three months ended September 30, 2021. Factors impacting the $8.6 million sales increase were:

- A higher instant ticket average selling price increased sales by $2.7 million as compared to 2021 due to increased proprietary product sales. Higher instant ticket sales volumes in 2022 further increased sales by $0.3 million.

- The higher average selling price of charitable games in 2022 also increased sales by $1.5 million, as we have been able to pass along inflationary cost increases to our charitable gaming customers. Charitable gaming sales volumes were lower in the third quarter of 2022 when compared to the record high pull-tab sales volumes achieved in the third quarter of 2021, decreasing sales by $0.9 million. In 2021, sales volumes were boosted by additional sales from pre-existing inventory.

- Higher sales of ancillary lottery products and services increased revenue by $1.4 million as compared to 2021. This increase was largely due to increased sales of digital and loyalty products, partially offset by lower retail merchandising product sales.

- eGaming systems revenue increased sales by $1.3 million, largely due to a higher number of eGaming machines placed at charitable establishments as compared to 2021.

- Higher sales from Michigan iLottery also increased revenue in 2022 by $0.4 million as compared to 2021.

- During the three months ended September 30, 2022, Pollard generated approximately 71.4% (2021 – 68.3%) of its revenue in U.S. dollars including a portion of international sales which are priced in U.S. dollars. During the third quarter of 2022, the actual U.S. dollar value was converted to Canadian dollars at $1.293, compared to a rate of $1.250 during the third quarter of 2021. This 3.4% increase in the U.S. dollar value resulted in an approximate increase of $3.0 million in revenue relative to the third quarter of 2021. In addition, during the quarter the value of the Canadian dollar strengthened against the Euro resulting in an approximate decrease of $1.1 million in revenue relative to the third quarter of 2021.

Cost of sales was $104.9 million in the third quarter of 2022 compared to $94.2 million in the third quarter of 2021. The increase of $10.7 million in cost of sales was primarily the result of inflationary pressures on raw material costs and higher exchange rates on U.S. dollar denominated expenses in 2022. In addition, increases in certain manufacturing overhead costs and increased sales of ancillary lottery products and services, including licensed product sales, further contributed to the increase in cost of sales as compared to 2021.

Gross profit was $20.6 million (16.4% of sales) in the third quarter of 2022 compared to $22.7 million (19.4% of sales) in the third quarter of 2021. This decrease of $2.1 million in gross profit was primarily a result of lower instant ticket sales margins, largely due to increased manufacturing costs, including the impact of inflation, and lower licensed product sales margins as compared to 2021. This decrease was partially offset by the increases in eGaming systems, charitable gaming, digital product and loyalty sales as compared to 2021. The lower gross margin percentage was largely due to the impact of inflationary cost increases on instant ticket inputs and lower licensed product sales margins, partially offset by increases in eGaming systems, charitable gaming, digital product and loyalty sales.

Administration expenses were $12.5 million in the third quarter of 2022 and $12.1 million in the third quarter of 2021. This increase was primarily due to higher travel related costs and professional fees in the third quarter of 2022.

Selling expenses were $4.5 million in both the third quarter of 2022 and the third quarter of 2021. Higher travel expenses were offset by lower customer contract costs in the third quarter of 2022 compared to 2021.

Pollard's share of income from its 50% owned iLottery joint venture, NPi, increased to $6.0 million in the third quarter of 2022 from the $2.6 million achieved in the third quarter of 2021. Contracts held by NPi continued to experience organic growth throughout the third quarter of 2022, increasing NPi's revenue as compared to 2021. In addition, in July 2022, there was a substantial Mega Millions® jackpot run which increased sales significantly in the beginning of the third quarter of 2022.

Other expenses were $2.9 million in the third quarter of 2022 compared to $4.3 million in the third quarter of 2021. This decrease of $1.4 million was primarily due to the decrease in contingent consideration fair value adjustment expense, as part of our Compliant Gaming, LLC ("Compliant") acquisition, of $1.7 million as compared to 2021. Partially offsetting this change in other expenses was the reduction in the Canada Emergency Wage Subsidy ("CEWS"), as Pollard received $nil in the third quarter of 2022 as compared to $0.7 million received in the third quarter of 2021.

The net foreign exchange loss was $4.7 million in the third quarter of 2022 compared to a net foreign exchange loss of $1.7 million in the third quarter of 2021. The 2022 net foreign exchange loss of $4.7 million consisted of an unrealized foreign exchange loss of $4.9 million, primarily 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, which was partially offset by an unrealized gain on U.S. dollar denominated cash and accounts receivable. Partially offsetting this unrealized foreign exchange loss was a realized foreign exchange gain of $0.2 million, primarily due to foreign currency denominated accounts receivable collected being converted into Canadian dollars at favorable foreign exchanges rates.

The 2021 net foreign exchange loss of $1.7 million consisted of a $2.2 million unrealized foreign exchange loss, comprised predominately of an unrealized loss on U.S. dollar denominated accounts payable and long-term debt, due to the weakening of the Canadian dollar at the end of the quarter, which was partially offset by an unrealized gain on U.S. dollar denominated cash and receivables. Partially offsetting the unrealized loss was a realized gain of $0.5 million as a result of foreign currency denominated account receivables collected being converted into Canadian dollars at favorable foreign exchange rates.

Adjusted EBITDA increased to $20.2 million in the third quarter of 2022 compared to $19.4 million in the third quarter of 2021. The primary reasons for the $0.8 million increase in Adjusted EBITDA include the increase in equity investment income of $3.4 million, partially offset by the reduction in gross profit of $1.6 million (net of amortization and depreciation), as a result of lower instant ticket sales margins, due to increased manufacturing costs, including the impact of inflation, and lower licensed product sales margins, partially offset by the increases in eGaming systems, charitable gaming, digital product and loyalty sales as compared to 2021. The increase in administration costs of $0.4 million, the reduction in other income (net of contingent consideration) of $0.3 million, and lower realized foreign exchange gain of $0.3 million also decreased Adjusted EBITDA in comparison to 2021.

Interest expense increased to $2.0 million in the third quarter of 2022 from $1.2 million in the third quarter of 2021, primarily due an increase in interest rates and an increase in average long-term debt outstanding as compared to 2021.

Amortization and depreciation totaled $10.1 million during the third quarter of 2022 which increased from $9.6 million during the third quarter of 2021. This increase of $0.5 million was largely due to amortization and depreciation taken on newly acquired property, plant and equipment, and intangible assets, partially offset by the reduction in amortization expense due to certain intangibles becoming fully amortized during 2021.

Income tax expense was $0.2 million in the third quarter of 2022, which was higher than the expense expected based on Pollard’s domestic rate of 27.0%. This increased expense was due primarily to the effect of non-taxable items related to foreign exchange, partially offset by the effect of the lower federal income tax rates in the United States.

Income tax expense was $2.1 million in the third quarter of 2021, which was higher than the expense expected based on Pollard’s domestic rate of 27.0%. This increased expense was due primarily to the tax effect of unrecognized non-capital losses and non-deductible expenses.

Net loss was $0.2 million in the third quarter of 2022 compared to a net loss of $0.6 million in the third quarter of 2021. The decrease in net loss of $0.4 million was due primarily to the increase in equity investment income of $3.4 million, the decrease in income tax expense of $1.9 million and the reduction in other expenses of $1.4 million. Partially offsetting these reductions in net loss were the increase in net foreign exchange loss of $3.0 million, the decrease in gross profit of $2.1 million, primarily as a result of lower instant ticket sales margins, largely due to increased manufacturing costs, including the impact of inflation, and lower licensed product sales margins, partially offset by the increases in eGaming systems, charitable gaming, digital product and loyalty sales as compared to 2021, the increase in interest expense of $0.8 million and the increase in administration expenses of $0.4 million.

Net loss per share (basic and diluted) decreased to ($0.01) per share in the third quarter of 2022 from ($0.02) per share in the third quarter of 2021.

Results of Operations – Nine months ended September 30, 2022

During the nine months ended September 30, 2022, Pollard achieved sales of $355.3 million, compared to $342.5 million in the nine months ended September 30, 2021. Factors impacting the $12.8 million sales increase were:

- Higher eGaming systems revenue increased sales by $7.3 million, largely due to a higher number of eGaming machines placed at charitable establishments as compared to 2021. In addition, more retail establishments were open for the first three quarters of 2022 as compared to 2021, further contributing to the increase in eGaming systems sales.

- The higher average selling price of charitable games in the first three quarters of 2022 also increased sales by $7.1 million, as we have been able to pass along inflationary cost increases to our customers. Charitable gaming sales volumes were lower in the first three quarters of 2022 when compared to the record high pull-tab sales volumes achieved in the first three quarters of 2021, decreasing sales by $3.4 million. In 2021, sales volumes were boosted by additional sales from pre-existing inventory.

- The higher instant ticket average selling price increased sales by $1.3 million as compared to 2021 due largely to increased proprietary product sales. Higher instant ticket sales volumes in 2022 further increased sales by $0.6 million. These increases were partially offset by lower sales of ancillary lottery products and services, which decreased revenue by $0.3 million, largely due to decreased sales of licensed products and retail merchandising products, partially offset by increased sales of digital and loyalty products.

- Michigan iLottery sales were lower by $2.8 million as compared to 2021, when Michigan iLottery sales were higher as a result of a double jackpot run in the first quarter of 2021.

- During the nine months ended September 30, 2022, Pollard generated approximately 71.5% (2021 – 69.2%) of its revenue in U.S. dollars including a portion of international sales which are priced in U.S. dollars. During the first nine months of 2022 the actual U.S. dollar value was converted to Canadian dollars at $1.278, compared to a rate of $1.251 the first nine months of 2021. This 2.1% increase in the U.S. dollar value resulted in an approximate increase of $5.3 million in revenue relative to the first nine months of 2021. In addition, during the first nine months of 2022, the value of the Canadian dollar strengthened against the Euro resulting in an approximate decrease of $2.3 million in revenue relative to the first nine months of 2021.

Cost of sales was $291.5 million in the nine months ended September 30, 2022, compared to $272.1 million in the nine months ended September 30, 2021. This increase of $19.4 million was primarily a result of inflationary pressures on raw material costs, higher exchange rates on U.S. dollar denominated expenses, increases in certain manufacturing overhead costs and the increase in digital product sales in 2022. Partially offsetting these increases was the decrease in charitable gaming and licensed product sales volumes as compared to 2021.

Gross profit decreased to $63.8 million (18.0% of sales) in the nine months ended September 30, 2022, from $70.4 million (20.6% of sales) in the nine months ended September 30, 2021. This decrease in gross profit of $6.6 million was primarily the result of lower instant ticket sales margins, due to increased manufacturing costs, including the impact of inflation, as well as lower Michigan iLottery sales as compared to 2021. This decrease was partially offset by increases in eGaming systems, charitable gaming and digital product sales, which increased gross profit as compared to 2021. The lower gross margin percentage was largely due to the impact of inflationary cost increases and lower Michigan iLottery sales, partially offset by increases in eGaming systems, charitable gaming and digital product gross margins as compared to 2021.

Administration expenses increased to $36.9 million in the first nine months of 2022 from $35.3 million in the first nine months of 2021. The increase of $1.6 million was primarily a result of increased compensation expenses, consulting costs, professional fees and travel related costs, partially offset by a reduction in acquisition costs.

Selling expenses increased to $13.4 million in the first nine months of 2022 from $12.6 million in the first nine months of 2021. The increase was primarily due to increased customer contract costs, and higher compensation and travel related expenses.

Pollard’s share of income from NPi increased to $15.0 million in the first nine months of 2022 from $9.1 million in 2021. This $5.9 million increase was primarily due to increased organic growth achieved on contracts held by NPi throughout the first three quarters of 2022, increasing NPi’s revenue as compared to 2021.

Other expenses were $3.7 million in the first nine months of 2022 compared to $2.8 million in 2021. This increase of $0.9 million was partially due to Pollard receiving $nil CEWS in 2022 compared to $5.9 million received in 2021. This was partially offset by Pollard entering into an agreement for a one-time payment of $2.5 million to settle all aspects of certain litigation regarding a patent dispute relating to our instant ticket production in 2021. In addition, lower contingent consideration fair value adjustment expenses, as part of our Compliant acquisition, further decreased other expenses by $1.9 million as compared to 2021.

The net foreign exchange loss was $6.9 million in the first nine months of 2022 compared to a net foreign exchange loss of $1.5 million in the first nine months of 2021. The 2022 net foreign exchange loss of $6.9 million resulted from a net unrealized foreign exchange loss of $6.6 million, comprised predominately of an unrealized loss on U.S. dollar denominated accounts payable and long-term debt due to the weakening of the Canadian dollar, which was partially offset by an unrealized gain on U.S. dollar denominated cash and accounts receivable. In addition, Pollard experienced a realized foreign exchange loss of $0.3 million as a result of foreign currency denominated accounts payable paid at unfavorable foreign exchange rates.

The 2021 net foreign exchange loss of $1.5 million consisted of a $1.8 million realized foreign exchange loss, which was predominately a result of foreign currency denominated accounts receivable collected being converted into Canadian dollars at unfavorable foreign exchange rates. Partially offsetting the realized foreign exchange loss was an unrealized foreign exchange gain of $0.3 million. This unrealized gain largely resulted from the decreased Canadian equivalent value of U.S. dollar denominated accounts payable and long-term debt due to the strengthening of the Canadian dollar, partially offset by an unrealized loss on U.S. dollar denominated accounts receivable.

Adjusted EBITDA decreased to $58.1 million in the first nine months of 2022 compared to $65.3 million in the first nine months of 2021. The primary reasons for the decrease of $7.2 million include the decrease in gross profit (net of amortization and depreciation) of $5.9 million, primarily the result of lower instant ticket sales margins, due to increased manufacturing costs, including the impact of inflation, and lower Michigan iLottery sales as compared to 2021. This decrease in gross profit (net of amortization and depreciation) was partially offset by increases in eGaming systems, charitable gaming and digital product sales as compared to 2021. Other factors contributing to the decrease in Adjusted EBITDA include the increase in other expenses (net of contingent consideration and litigation settlement) of $5.3 million, primarily due to the reduction in CEWS received of $5.9 million, higher administration expenses (net of acquisition costs) of $2.6 million and higher selling expenses of $0.8 million. These decreases were partially offset by the increase in equity investment income of $5.9 million and the reduction in the realized foreign exchange loss of $1.5 million.

Interest expense increased to $5.9 million in the first nine months of 2022 from $3.4 million in the first nine months of 2021, primarily as a result of the increase in interest accretion on the discounted contingent consideration liability relating to the Compliant purchase of $1.5 million and higher interest rates in 2022. Partially offsetting these increases to interest expense was the decrease in average long-term debt outstanding as compared to 2021.

Amortization and depreciation totaled $29.5 million during the first nine months of 2022 which increased from $28.8 million during the first nine months of 2021. The increase of $0.7 million was primarily as a result of amortization and depreciation taken on newly acquired property, plant and equipment, and intangible assets, partially offset by the reduction in amortization expense due to certain intangibles becoming fully amortized during 2021.

Income tax expense was $3.3 million in the first nine months of 2022, an effective rate of 27.3%, which was higher than our domestic rate of 27.0% due primarily to the changes enacted with regards to the United Kingdom's corporation tax rates and the effect of non-taxable items related to foreign exchange, partially offset by the effect of the lower federal income tax rates in the United States.

Income tax expense was $9.4 million in the first nine months of 2021, an effective rate of 39.2%, higher than our domestic rate of 27.0% due primarily to the tax effect of unrecognized non-capital losses and non-deductible expenses. Partially offsetting these increases in effective rate were the lower federal income tax rates in the United States.

Net income decreased to $8.7 million in the first nine months of 2022 from $14.5 million in the first nine months of 2021. The main reasons for the decrease of $5.8 million include the decrease in gross profit of $6.6 million, primarily the result of lower instant ticket sales margins, due to increased manufacturing costs, including the impact of inflation, and lower Michigan iLottery sales as compared to 2021. This decrease in gross profit was partially offset by increases in eGaming systems, charitable gaming and digital product sales, which increased gross profit as compared to 2021. Other factors contributing to the decrease in net income include the increase in net foreign exchange loss of $5.4 million, the increase in interest expense of $2.5 million, the increase in administration expenses of $1.6 million, the increase in other expenses of $0.9 million and the increase in selling costs of $0.8 million. Partially offsetting these decreases were the lower income tax expense of $6.1 million and the increase in equity investment income of $5.9 million as compared to 2021.

Net income per share (basic and diluted) decreased to $0.32 per share in the nine months ending September 30, 2022, as compared to $0.54 per share in the nine months ending September 30, 2021.

iLottery

Pollard and its iLottery partner, Neogames US LLP ("Neogames"), provide iLottery services to the North American Lottery market. In 2013, Pollard was awarded an iLottery contract from the Michigan Lottery. As a result, Pollard entered into a contract with Neogames to provide its technology in return for a 50% financial interest in the operation. Under IFRS, Pollard recognizes its 50% share in the Michigan Lottery contract in its consolidated statements of income in revenue and cost of sales.

In 2014 Pollard, in conjunction with Neogames, established NeoPollard Interactive LLC ("NPi"). All iLottery related customer contracts, excluding the Michigan Lottery iLottery contract, have been awarded to NPi. Under IFRS, Pollard accounts for its investment in its joint venture, NPi, as an equity investment. Under the equity method of accounting, Pollard recognizes its share of the income and expenses of NPi separately as equity investment income.

SELECT iLOTTERY RELATED FINANCIAL INFORMATION

(millions of dollars)

	Q3 2022	Q2 2022	Q1 2022	Q4 2021	Q3 2021	Q2 2021	Q1 2021	Q4 2020	Q3 2020
Sales – Pollard's share									
Michigan iLottery	$6.5	$6.2	$5.9	$5.6	$5.9	$6.8	$8.4	$8.6	$9.5
NPi	13.7	12.4	11.3	10.5	9.8	9.9	9.9	6.1	3.1
Combined iLottery sales	$20.2	$18.6	$17.2	$16.1	$15.7	$16.7	$18.3	$14.7	$12.6
Income before income taxes – Pollard's share									
Michigan iLottery	$2.2	$2.4	$2.0	$1.8	$2.0	$2.8	$4.0	$4.5	$5.4
NPi	6.0	5.1	3.9	3.2	2.6	2.5	4.0	1.6	0.8
Combined income before income taxes – Pollard's share	$8.2	$7.5	$5.9	$5.0	$4.6	$5.3	$8.0	$6.1	$6.2

Following the onset of COVID-19 in 2020, revenues from Pollard's contract with the Michigan Lottery increased substantially. Contracts held by NPi also experienced significant organic growth, in addition to the sales increase from the Virginia Lottery operation which added e-Instants on July 1, 2020. As well, NPi's contract with Alberta Gaming, Liquor & Cannabis ("AGLC"), went live with a limited product launch on September 30, 2020, with additional gaming verticals launching throughout 2021. The substantial jackpots for POWERBALL® and Mega Millions® awarded in the latter half of January 2021 further increased sales significantly in the fourth quarter of 2020 and the first quarter of 2021.

Sales and income before income taxes from our Michigan iLottery operation declined starting in the second quarter of 2021 due to reduced draw-based game sales after the double jackpots in the first quarter of 2021, increased online gaming competition and new pricing coming into effect with our four-year contract extension, starting at the beginning of 2021. In 2022, NPi continues to achieve strong organic growth, adding to sales and income before taxes. In July 2022, there was another substantial Mega Millions® jackpot awarded which increased sales in the third quarter of 2022.

Outlook

Our main business lines continue to experience strong demand, including both our instant ticket and charitable gaming segments. Retail dollar sales of instant tickets have remained at the higher levels achieved over the past year, and charitable gaming demand also remains very strong, in both printed products and eGaming systems. We anticipate this strong consumer demand will continue, which translates into positive demand from lotteries and charitable gaming organizations to Pollard.

Historically, demand for our offerings has been very resilient during challenging economic environments such as we are experiencing now, and we believe this will remain the case in our current retail atmosphere.

Our third quarter instant ticket sales reflected a greater proportion of higher value product in preparation for the holiday selling season. Instant ticket sales mix will continue to vary quarter to quarter going forward, consistent with our historical selling pattern, with these higher value sales expected to be reduced in the next few quarters.

Inflationary cost increases absorbed in our instant ticket cost structure will continue to be a strong negative headwind on our margins. Significant new additional cost increases do not appear imminent; however, some previously announced increases will not come into effect until the fourth quarter and these will continue to put further pressure on our margins. We are working diligently on a number of strategies to manage these cost increases, including investigating potential alternate sources for key inputs, increasing production output and expanding capacity.

We remain focused on our strategy of increasing our instant ticket pricing as contracts come up for extension or rebid. It remains early in the cycle of repricing our contracts, given many of our contracts are multiple years in length, however, the industry and lotteries worldwide appear to recognize the need to properly compensate suppliers in light of these inflationary cost increases. Repricing our entire contract portfolio will take three to four years. We have already achieved higher pricing for some contracts during 2022, although very little financial impact has been reflected in our financial results so far, as most of the new contract pricing does not come into effect until 2023. We also continue to diligently review our customer profiles to identify opportunities to focus our efforts on more profitable clients, which may result in lower volumes as we reduce sales to lower margin clients.

Our iLottery operations continue to show strong organic growth assisted by the occasional draw-based jackpot run as experienced in July. While still limited, interest in new iLottery opportunities are increasing with greater activity in formal requests for information, informal discussions, as well as increased interest in RFP's, which reflects the desire for this solution amongst lotteries. We will remain engaged with the industry in developing concrete opportunities, for both iLottery platform and game content.

Our cash flows remain strong, supported by positive demand in our main product lines and solutions, allowing us to continue to make the necessary investments in innovation and growing our businesses. We anticipate demand for our lottery and charitable gaming products and solutions will continue at these strong levels and believe over time our strategy of increasing our selling prices to offset the inflationary margin pressures on instant tickets will ultimately allow us to return to more historical margins.

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