POLLARD banknote limited

2019 ANNUAL REPORT

CONTENTS

LETTER TO SHAREHOLDERS

Enclosed please find our 2019 Annual Report. In 2019 Pollard Banknote achieved record revenue of $397.8 million dollars, a 19.9% increase over 2018, and strong Net Income of $22.0 million, up over 48% from the prior year. Our adjusted EBITDA, not including the impact of IFRS 16, increased to record levels of $54.8 million, 12% higher than 2018. These results were driven by contributions from our acquisitions completed over the past few years as well as strong growth from our main lottery operations, including both instant tickets and digital solutions.

Our strategic vision of being the partner of choice for the lottery and charitable gaming industries has resulted in our growing stature in these industries and this is reflected in our 2019 financial achievements. Pollard is recognized as the thought leader among lotteries and charitable gaming organizations through the provision of creative and innovative products and solutions that help our customers maximize the generation of more funds to distribute to good causes.

Sales

Our record revenue of $397.8 million reflects the third year in a row of sales growth in excess of at least 16%. Sales of our main product, instant tickets, were significantly higher in 2019 driven by increased orders across a number of our lottery customers.

Consumer demand for instant tickets remained strong during 2019. Through the development of a number of unique proprietary products such as Clear Play™ and Scratch FX®, we have been able to increase our volumes while at the same time maintain, and in some cases increase, our average selling price. Sustaining strong selling prices in a very price competitive market is important for Pollard's success, however, this strategy can only be achieved when our products actually generate greater sales and success for our lottery customers. Pollard Banknote achieved a record level of instant ticket volume sold in 2019 because of the creative and innovative solutions offered to our customers.

Our lottery contract portfolio remains healthy. During 2019 we retained all of our existing contracts, including obtaining renewals for all contracts with renewal options available during they year. These renewals include a new ten-year contract to provide instant tickets for the British Columbia Lottery Corporation, a two-year extension with Loto-Quebec and renewals with a number of important customers including the lotteries of France, Sweden, Michigan and California. Our weighted average length of our existing instant ticket contracts, assuming all available renewals are exercised, is currently in excess of 4 years and while we have a few mid-size contracts coming due during 2020, as is typical with the lottery contract cycle, we have no major contracts expiring over the next year.

While still small in overall financial impact, our significant investments in ancillary lottery products continue to generate traction in the marketplace. In 2019 we achieved key installations of our PlayOn™ loyalty platform, rolled out our proprietary SureTrack® 2.0 Lottery Management System to a number of customers and maintained a strong sales record of digital lottery products such as individual game apps and second chance draw solutions. During the year we were awarded a contract to operate the instant ticket warehousing and distribution system on behalf of the Arizona Lottery, which began successful operation in March 2020. While the financial impact of this one contract will be small, it is an important strategic development to showcase our ongoing multifaceted service offering to the market.

In addition to strong growth in our lottery operation, our sales and earnings increased due to the ongoing contribution of our recent acquisitions. During 2019, our financial results included a full year of International Gamco operations (compared to 11 months in 2018), a full year of Schafer Systems business results (versus only 2 months in 2018) and 8 months of impact from the acquisition of Fastrak Retail. Incremental revenue based on the timing of these acquisitions increased revenue by approximately $20 million.

Our iLottery operations continue to lead the market with continued growth in Michigan and the launching of the iLottery operation for the North Carolina Education Lottery in the fall of 2019. Our 50% joint venture, NeoPollard, now operates 4 iLottery solutions in the United States and we remain the clear leader in providing successful innovative solutions in this space.

Charitable gaming revenue attained a new record of $62.5 million, driven by higher demand for pull-tab tickets as well as pull-tab vending machines. In a number of important jurisdictions, we have seen positive growth at the retail level for charitable gaming products and this factor, in conjunction with broader product offerings of pull-tab tickets, has helped generate a 13.4% increase in charitable gaming revenue.

Diamond Game and Oasis branded egaming machines continued to generate solid returns. A number of markets in which our machines are deployed have changed their economic model. Previous single supplier markets have become multiple supplier markets with more competitive pricing, however in most of these situations the previous cap or limited number of machines has been modified or lifted, allowing Pollard the opportunity to place more machines. Our 2019 revenue declined by 1% overall, with lower pricing in certain jurisdictions being substantially offset by slightly increased number of machines and improved per machine performance. The North Dakota market, originally opened in 2018, continued to grow, with additional machines and improving per machine performance.

Operations

In 2019 we achieved a record gross margin of $91.1 million, 20.3% higher than last year. The higher gross margin was due to the higher levels of revenue from greater instant ticket volumes and the impact of acquisitions. Our gross margin percentage of 22.9% was consistent with our 2018 gross margin of 22.8%. Instant ticket production volume set a new record, approximately 7% higher than the previous year.

Our gross margin percentage during the fourth quarter of 2019 was impacted negatively 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.

Administration expenses increased $8.4 million due partially to the inclusion of a full year of International Gamco, Schafer Systems and 8 months of Fastrak Retail operations. In addition, increased personnel costs were incurred relating to our growth strategies and product development of our digital innovations and increased investment in our technology infrastructure, including implementation of a number of product installations. Higher acquisition costs increased expenditures by $0.4 million and additional professional fees of $1.5 million relating to legal fees to defend our intellectual property, including certain patents, were incurred. Selling expenses increased $2.5 million over 2018 primarily due to the inclusion of a full year of our earlier acquisitions and ongoing investments in additional personnel to support our expanded portfolio of products and services offered to the lottery market.

Our capital expenditures and investments in intangibles totaled $25.8 million during 2019, covering a number of important manufacturing improvements as well as new product development. Additional equipment was added to our original press in Ypsilanti to grow instant ticket capacity and increase scheduling flexibility. Upgrades to our finishing lines were undertaken to expand and improve product handling. Significant investments were made in our charitable gaming business, including a new state of the art digital press and additional manufacturing equipment, to improve efficiency and increase capacity. We continued to invest in our digital product offerings with major expenditures on our PlayOn™ loyalty solution, complete upgrades for our SureTrack® 2.0 Lottery Management Systems and a substantial investment in expanding our electronic game portfolio for our egaming machines.

Acquisitions

Over the last three years, acquisitions have been an important feature of our strategic plan, with a focus on building our portfolio of lottery products and services, expanding our presence in the charitable gaming market and growing additional technological solutions. 2019 continued this successful avenue of growth.

On May 2, 2019, Pollard acquired 100% of the common shares of Fastrak Retail (UK) Limited for initial consideration of £4.0 million, subject to a working capital adjustment and future contingent consideration based on certain earn-outs. Fastrak Retail is a leading supplier of creative and innovative instant ticket lottery merchandising including key relationships with a number of major lotteries. Fastrak Retail and our existing lottery merchandising business, Schafer Systems, have already integrated many aspects of their marketing and research and development and we are very pleased with the results.

Subsequent to year end, Pollard acquired 100% of the equity of mkodo Limited for a consideration of £7.8 million subject to a working capital adjustment and future contingent consideration based on certain earn-outs. mkodo is a leading technology developer focused on mobile apps and user interfaces specifically in the lottery and gaming industries. mkodo expands our capabilities in this important link between lotteries and their customers in all things digital and is a key strategic addition for Pollard.

On March 20, 2020, Pollard acquired certain fixed assets and intellectual property for a purchase price of $3.8 million which were being sold under a bankruptcy process. These assets had previously been used in the operation of a business producing pull-tab tickets for the lottery and charitable gaming industry and will be utilized to expand our existing charitable gaming operations.

Pollard continues to be actively engaged in seeking out future acquisitions to further enhance Pollard’s position in the market. We believe there are actionable opportunities to acquire valuable organizations at reasonable prices available, however we will remain very disciplined in our approach.

Capital

The preservation and appropriate allocation of capital is a critical component of Pollard’s strategic vision. To that end, during 2019 we were successful on a number of fronts ensuring our capital management program and structure provided the optimal results.

In the first quarter of 2019 we raised our dividend for the very first time in our history of being a public company, increasing it by 33%. We believe there is an important balance between retaining capital for investment and ensuring a minimum return is available for our shareholders.

On December 31, 2019, we renewed our senior bank facility for a further three-year period. The new facility increased the available capacity, improved the flexibility relative to operations and future acquisitions, and lowered costs.

Our balance sheet remains very strong with significant availability of funds through cash on hand and substantial unused capacity within our senior credit facility, including a separate accordion feature to expand our source of capital.

Our cash conversion rate of our operating earnings is high, resulting in very strong organic cashflow. This allows us to utilize a very conservative approach to funding our initiatives, including important capital additions when needed and enabling us to finance large increases in our working capital as occurred in 2019.

Conclusion

As we write this letter, the world today is undergoing very significant uncertainty and challenges due to the COVID-19 virus and all organizations, including Pollard, are dealing with the issues as best as they can. Despite these temporary headwinds, the underlying fundamentals for Pollard and the lottery and charitable gaming industry remain positive. The long-term consumer demand for our products and solutions we believe will be strong, including traditional instant tickets and charitable gaming products, as well as the increasing interest in the emerging area of digital solutions, including iLottery.

We will make the necessary investments to continue to be the thought leader to the industries we are privileged to serve. New market-leading instant ticket innovations, expanded ancillary lottery products, growing production capacity across all our business lines and enlarging our digital solutions portfolio will allow us to be the partner of choice to lotteries and charitable gaming organizations around the world. We will supplement these initiatives with a discerning acquisition strategy, allowing us to selectively add to Pollard expertise and unique products and services to further meet our objectives.

2019 was a successful year for Pollard, which would not have been attained without the support and hard work of so many people. The Pollard family extends to 1,900 enthusiastic employees who provide an unmatched level of dedication in doing the right thing. We are fortunate to work with dozens of lottery and charitable gaming organizations, all leaders in generating record amounts to fund so many good causes. In many ways our suppliers are the silent partners, working around the clock to ensure the highest quality inputs for Pollard's operations. Despite a relatively small public share float, many of our investors have been long-standing supporters of our vision and, notwithstanding the extreme volatility experienced in the stock market thus far in 2020, remain very committed to the long-term success of Pollard. And lastly, our Board of Directors provides us with a critically important sounding board, delivering invaluable advice and leadership at both the strategic and operational level. To all of you, thank you very much, and together we are confident in our ability to take on the challenges we will face in 2020.

Douglas Pollard	**John Pollard**
Co-Chief Executive Officer	Co-Chief Executive Officer

March 30, 2020

DIRECTORS OF POLLARD BANKNOTE LIMITED

Gordon Pollard

Executive Chair

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

Dave Brown

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

Jerry Gray

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

Garry Leach

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

Douglas Pollard

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

John Pollard

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

December 31, 2019

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

FOR THE YEAR ENDED DECEMBER 31, 2019

March 11, 2020

This management's discussion and analysis ("MD&A") of Pollard Banknote Limited ("Pollard") for the year ended December 31, 2019, is prepared as at March 11, 2020, and should be read in conjunction with the accompanying audited financial statements of Pollard and the notes therein as at December 31, 2019. Results are reported in Canadian dollars and have been prepared in accordance with International Financial Reporting Standards ("GAAP" or "IFRS").

Forward-Looking Statements

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

Use of Non-GAAP Financial Measures

Reference to "Adjusted EBITDA" is to earnings before interest, income taxes, depreciation and amortization, purchase accounting amortization, unrealized foreign exchange gains and losses and certain non-recurring items including severance costs, 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.

Basis of Presentation

The results of operations in the following discussions encompass the consolidated results of Pollard for the year ended December 31, 2019. 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. In addition, management believes Pollard is also the second largest bingo paper and pull-tab supplier to the charitable gaming industry in North America.

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

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

On May 1, 2019, Pollard acquired 100% of the common shares of Fastrak Retail (UK) Limited ("Fastrak") for a purchase price of £4.0 million, subject to standard working capital adjustments and potential future EBITDA and revenue earn-out payments. Fastrak, based in the United Kingdom, is a leading provider of lottery ticket dispensers, lottery play points and other retail merchandising products.

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.

Product line breakdown of revenue

	Year ended December 31, 2019	Year ended December 31, 2018
Lottery [(1)] [(2)]	77.8%	75.5%
Charitable [(3)]	15.7%	16.6%
Gaming systems	6.5%	7.9%

(1) Includes Fastrak Retail (UK) Limited ("Fastrak") which was acquired on May 1, 2019.

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

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

Geographic breakdown of revenue

	Year ended December 31, 2019	Year ended December 31, 2018
United States	60%	56%
Canada	21%	23%
International	19%	21%

The following financial information should be read in conjunction with the accompanying financial statements of Pollard and the notes therein as at and for the year ended December 31, 2019.

SELECTED FINANCIAL INFORMATION

(millions of dollars, except per share information)

	Year ended December 31, 2019	Year ended December 31, 2018	Year ended December 31, 2017
Sales	**$397.8**	$331.9	$285.6
Cost of sales	**306.7**	256.2	219.9
Gross profit	**91.1**	75.7	65.7
Gross profit as a % of sales	***22.9%***	*22.8%*	*23.0%*
Administration expenses	**40.6**	32.2	28.6
Expenses as a % of sales	***10.2%***	*9.7%*	*10.0%*
Selling expenses	**15.9**	13.4	9.4
Expenses as a % of sales	***4.0%***	*4.0%*	*3.3%*
Net income	**22.0**	14.9	16.8
Net income as a % of sales	***5.5%***	*4.5%*	*5.9%*
Adjusted EBITDA	**60.2**	48.8	44.0
Adjusted EBITDA as a % of sales	***15.1%***	*14.7%*	*15.4%*
Adjusted EBITDA excluding IFRS 16	**54.8**	48.8	44.0
Adjusted EBITDA as a % of sales	***13.8%***	*14.7%*	*15.4%*
Net income per share (basic and diluted)	**$0.86**	$0.58	$0.71

	December 31, 2019	December 31, 2018	December 31, 2017
Total Assets	**$352.3**	$305.6	$228.3
Total Non-Current Liabilities	**$175.6**	$142.9	$124.8

RECONCILIATION OF NET INCOME TO ADJUSTED EBITDA

(millions of dollars)

	Year ended December 31, 2019	Year ended December 31, 2018	Year ended December 31, 2017
Net income	**$22.0**	$14.9	$16.8
Adjustments:			
Amortization and depreciation	**27.1**	18.0	13.1
Interest	**6.4**	4.2	3.9
Unrealized foreign exchange (gain) loss	**(3.3)**	4.6	(1.4)
Acquisition costs	**1.2**	0.8	2.7
Severance costs	**-**	0.4	1.7
Contingent consideration fair value adjustment	**(0.2)**	-	-
Income taxes	**7.0**	5.9	7.2
Adjusted EBITDA	**$60.2**	$48.8	$44.0
Less impact of implementation of IFRS 16 Leases*:			
IFRS 16 related depreciation	**4.7**	-	-
IFRS 16 related interest	**0.7**	-	-
Adjusted EBITDA excluding IFRS 16 impact	**$54.8**	$48.8	$44.0
Lotteries and charitable gaming	**$50.2**	$38.4	$40.0
Diamond Game	**10.0**	10.4	4.0
Adjusted EBITDA	**$60.2**	$48.8	$44.0
Lotteries and charitable gaming	**$45.5**	$38.4	$40.0
Diamond Game	**9.3**	10.4	4.0
Adjusted EBITDA excluding IFRS 16 impact	**$54.8**	$48.8	$44.0

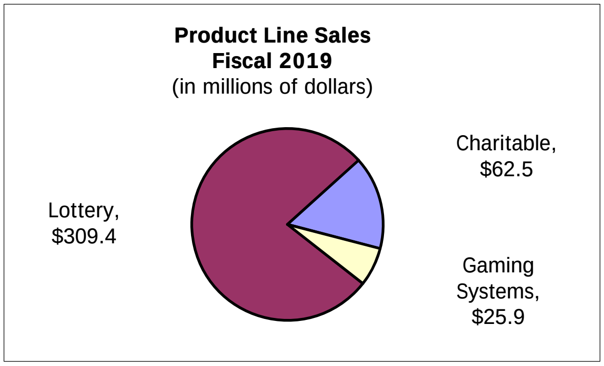
* IFRS 16 Leases was implemented effective January 1, 2019. Qualifying leases are now capitalized and an offsetting liability is recorded. The right-of-use asset is depreciated over the term of the lease and interest expense related to the liability is expensed over the term of the lease. As a result, Adjusted EBITDA has been increased by the conversion of operating lease expenses into depreciation and interest.

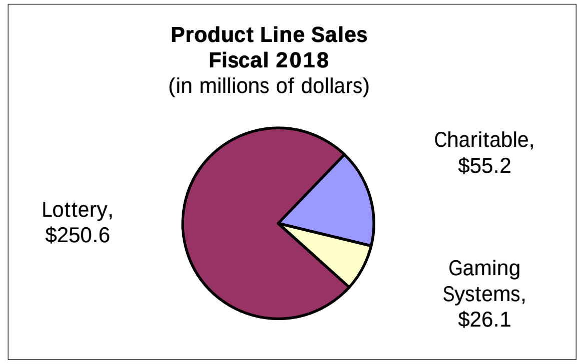
REVIEW OF OPERATIONS

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

ANALYSIS OF RESULTS FOR THE YEAR ENDED DECEMBER 31, 2019

Sales

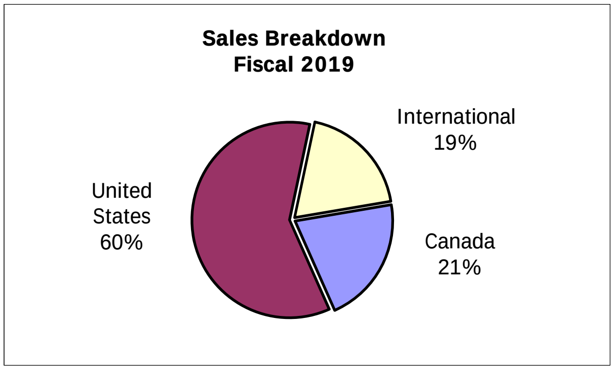


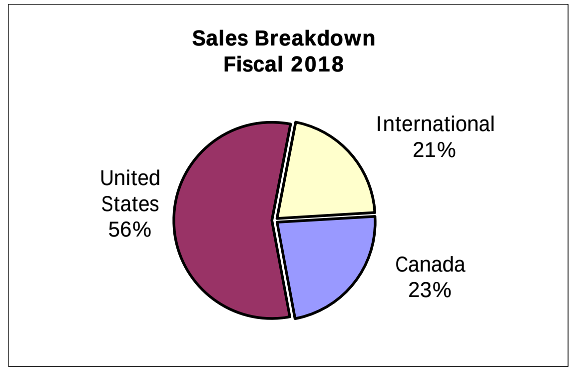


During the year ended December 31, 2019 ("Fiscal 2019" or "2019"), Pollard achieved sales of $397.8 million, compared to $331.9 million in the year ended December 31, 2018 ("Fiscal 2018" or "2018"). Factors impacting the $65.9 million sales increase were:

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.

Liquidity and Capital Resources

Cash provided by operating activities

For the year ended December 31, 2019, cash flow provided by operating activities was $29.3 million compared to $39.7 million in Fiscal 2018.

The primary reason for the reduction in cash flow provided by operations was a significant increase in our investment in non-cash working capital in 2019. In Fiscal 2019, increases in non-cash working capital used $22.5 million compared to decreases in 2018 which generated $4.0 million in cash, a $26.5 million difference.

In 2019, changes in the non-cash component of working capital decreased cash flow from operations due primarily to an increase in accounts receivable. The higher investment in accounts receivable reflects the higher sales volume from higher order levels building throughout Fiscal 2019, relative to a very low order level in the fourth quarter of 2018. In 2018, changes in the non-cash component of working capital increased cash flow from operations due primarily to a decrease in accounts receivable, partially offset by an increase in inventory and a decrease in accounts payable and accrued liabilities.

Higher net income before income taxes and after non-cash adjustments in Fiscal 2019 contributed $69.6 million to the cash provided by operating activities compared to $55.9 million in Fiscal 2018. Cash used for interest payments increased to $6.4 million in 2019 as compared to $4.5 million in 2018. Cash used for pension plan contributions increased to $7.4 million in 2019 as compared to $5.5 million in 2018. Cash used for income taxes paid was $4.0 million in 2019 compared to $10.2 million in 2018.

Cash used for investing activities

In the year ended December 31, 2019, cash used for investing activities was $38.3 million compared to $77.1 million in the year ended December 31, 2018. In Fiscal 2019, Pollard used $8.5 million, net of cash acquired, to purchase Fastrak. In addition, Pollard expended $17.2 million in capital expenditures, $4.0 million on our investment in our iLottery joint venture and $8.6 million on additions to intangible assets.

In Fiscal 2018, Pollard used $21.6 million, net of cash acquired, to purchase Gamco and $30.4 million to purchase Schafer. In addition, Pollard expended $15.1 million in capital expenditures, $2.8 million on our investment in our iLottery joint venture and $7.1 million on additions to intangible assets.

Cash provided by financing activities

Cash provided by financing activities was $5.6 million in the year ended December 31, 2019, compared to $42.6 million in the year ended December 31, 2018.

During Fiscal 2019, Pollard received net proceeds from long-term debt of $14.3 million. This receipt of cash was partially offset by $4.4 million of lease principal payments, which, starting in 2019 with the implementation of IFRS 16, are now shown as financing activities, and $3.8 million of dividends.

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

As at December 31, 2019, Pollard had unused committed credit facility of $69.7 million, in addition to $7.4 million in available cash resources. These amounts, in addition to cash flow provided by operating activities, are available to be used for future working capital requirements, contractual obligations, capital expenditures, dividends and to assist in financing future acquisitions.

ANALYSIS OF RESULTS FOR THE PERIOD OCTOBER 1, 2019 TO DECEMBER 31, 2019
FOURTH QUARTER OF 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 expense (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
Lotteries and charitable gaming	$11.9	$4.9
Diamond Game	2.3	2.6
Adjusted EBITDA	$14.2	$7.5
Lotteries and charitable gaming	$10.7	$4.9
Diamond Game	2.1	2.6
Adjusted EBITDA excluding IFRS 16 impact	$12.8	$7.5

Sales

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 and gross profit

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

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

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.

Foreign exchange

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

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

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

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 taxes

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 (loss)

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.

Quarterly Information
(unaudited)
(millions of dollars)

	Q4 2019	Q3 2019	Q2 2019	Q1 2019	Q4 2018	Q3 2018	Q2 2018	Q1 2018
Sales	$100.0	$103.2	$97.1	$97.5	$70.2	$94.5	$86.8	$80.4
Adjusted EBITDA	14.2	16.1	13.6	16.3	7.5	14.2	14.1	13.0
Net income (loss)	4.6	4.4	5.0	8.0	(1.9)	7.2	5.0	4.6

Effective the first quarter 2019 Adjusted EBITDA increased as a result of the implementation of IFRS 16 Leases. The amounts per quarter were $1.4 million in Q4 2019, $1.2 million in Q3 2019, $1.3 million in Q2 2019 and $1.3 million in Q1 2019.

The trend of increased sales, Adjusted EBITDA and net income, starting the first quarter of 2018, with the exception of the fourth quarter of 2018, was primarily as a result of higher instant ticket volumes and the acquisitions made during this timeframe.

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

Working Capital

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

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

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

As at December 31, 2019, Pollard's investment in non-cash working capital increased $22.5 million compared to December 31, 2018, primarily a result of the increased investment in accounts receivable. The higher investment in accounts receivable reflects the increasing sales volume from increased orders levels building throughout 2019, relative to a period of very low orders in the fourth quarter of 2018.

	December 31, 2019	December 31, 2018
Working Capital	$79.2	$65.5
Total Assets	$352.3	$305.6
Total Non-Current Liabilities	$175.6	$142.9

Credit Facility

Pollard's credit facility was renewed effective December 31, 2019. The credit facility provides loans of up to $190.0 million for its Canadian operations and US$14.0 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 $190.0 million Canadian equivalent. The credit facility also includes an accordion feature which can increase the facility by $35.0 million. Borrowings under the credit facility bear interest at fixed and floating rates based on Canadian and U.S. prime bank rates, banker's acceptances or LIBOR. At December 31, 2019, the outstanding letters of guarantee were $10.7 million. The remaining balance available for drawdown under the credit facility was $69.7 million.

Under the terms and conditions of the credit facility agreement Pollard is required to maintain certain financial covenants including debt to income before interest, income taxes, amortization and depreciation ("Adjusted EBITDA") ratios and certain debt service coverage ratios. As at December 31, 2019, Pollard is in compliance with all financial covenants.

Pollard's credit facility is secured by a first security interest in all of the present and after acquired property of Pollard. Under the terms of the agreement the facility is committed for a three-year period, renewable December 31, 2022. Principal payments are not required until maturity. The facility can be prepaid without penalties.

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

Outstanding Share Data

As at December 31, 2019 and March 11, 2020, outstanding share data was as follows:

Common shares	25,635,658

On March 19, 2019, 5,000 common shares were issued through the exercise of stock options.

On May 24, 2019, 5,000 common shares were issued through the exercise of stock options.

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 19, 2019, 5,000 stock options were exercised and an additional 5,000 stock options were exercised on May 24, 2019.

On November 5, 2019, the Board of Directors approved the award of 150,000 options to purchase common shares of Pollard for key management personnel. The options were granted on November 8, 2019, and have a seven-year term, vesting 25% per year over the first four years. The exercise price of the options is $20.70. As at December 31, 2019, the total share options issued and outstanding were 377,500.

Contractual Obligations

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

(millions of dollars)	Total	2020	2021	2022	2023	2024
Long-term debt	$146.0	$5.4	$6.4	$134.2	-	-
Operating leases	$18.1	$5.5	$4.5	$4.0	$3.2	$0.9
Total	$164.1	$10.9	$10.9	$138.2	$3.2	$0.9

Pension Obligations

Pollard sponsors four non-contributory defined benefit pension plans, of which three are final pay plans and one is a flat benefit plan. As of December 31, 2019, the aggregate fair value of the assets of Pollard's defined benefit pension plans was $65.5 million and the accrued benefit plan obligations were $92.0 million. Pollard's total annual funding contribution for its defined pension plans in 2020 is expected to be approximately $6.5 million, compared to $6.3 million in 2019, including $1.5 million in additional solvency payments.

One of Pollard's Canadian pension plans was subject to a solvency valuation beginning with its December 31, 2016 valuation. The solvency valuation is required to be updated annually. As at the December 31, 2018 valuation there was a deficit of $9.9 million, due to the low current levels of the mandated interest rate used to discount the future liabilities. As a result, Pollard is subject to additional special pension plan payments of approximately $1.5 million per year through to 2026. These additional solvency payments do not impact pension expense and therefore will not affect our net income or Adjusted EBITDA and will be funded from operating cash flows.

Off-Balance Sheet Arrangements

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

Related Party Transactions

Pollard Equities Limited and affiliates

During the year ended December 31, 2019, Pollard paid property rent of $3.2 million (2018 - $3.2 million) and $0.4 million (2018 - $0.5 million) in plane charter costs to affiliates of Equities. In addition, Pollard paid Equities $nil (2018 - $0.4 million) of interest on Pollard's subordinated debt.

During the year ended December 31, 2019, Equities paid Pollard $0.07 million (2018 - $0.07 million) for accounting and administration fees.

At December 31, 2019, Pollard owed Equities and its affiliates $0.5 million (2018 - $0.6 million) for rent, interest, expenses and other items. Included within property, plant and equipment and lease liabilities on the consolidated statement of financial position are right-of-use assets and corresponding liabilities for premises leased to Pollard from Equities. As at December 31, 2019, the net book value of the right-of-use assets was $10.8 million and the present value of the lease liabilities was $11.8 million.

Neogames S.à r.l. and affiliates

During the year ended December 31, 2019, Pollard reimbursed operating costs and paid software royalties of $5.7 million (2018 - $3.3 million) to its iLottery partner, which are recorded in cost of sales.

At December 31, 2019, included in accounts payable and accrued liabilities is a net amount owing to Pollard's iLottery partner of $0.1 million (2018 - $0.9 million) for reimbursement of operating costs and capital expenditures, and its share of operating profits.

At December 31, 2019, included in restricted cash and accounts payable and accrued liabilities is an amount owing to Pollard's iLottery partner of $2.6 million (2018 - $1.6 million) for funds relating to contractual performance guarantees.

Critical Accounting Policies and Estimates

Described in the notes to Pollard's 2019 audited consolidated financial statements are the accounting policies and estimates that Pollard believes are critical to its business. Please refer to note 2 (c) to the audited consolidated financial statements for the year ended December 31, 2019, for a discussion of the significant accounting estimates and judgements.

Future Changes in Accounting Policies

In October 2018, the International Accounting Standards Board issued amendments to IFRS 3 *Business Combinations,* that seek to clarify whether a transaction results in an asset or a business acquisition. The amendments include an election to use a concentration test. This is a simplified assessment that results in an asset acquisition if substantially all of the fair value of the gross assets is concentrated in a single identifiable asset or a group of similar identifiable assets. The amendments apply to businesses acquired in annual reporting periods beginning on or after January 1, 2020. Pollard does not expect the amendments to have a significant impact on the consolidated financial statements upon adoption.

Industry Risks and Uncertainties

Pollard is exposed to numerous risks and uncertainties which are described in this MD&A and Pollard's most recent Annual Information Form dated March 11, 2020, which is available under Pollard's profile on SEDAR (www.sedar.com).

Financial Instruments

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

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

Risk Exposure

Currency risk

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

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

Interest rate risk

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

Credit risk

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

Liquidity risk

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

Risk Management

Currency risk

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

A 50 basis point strengthening/weakening in the foreign exchange rate between the Canadian and U.S. dollar would decrease/increase the income before income taxes by approximately $0.04 million for year ended December 31, 2019 (2018 - $0.02 million). A 50 basis point strengthening/weakening in the foreign exchange rate between the Canadian dollar and Euro would decrease/increase the income before income taxes due to changes in operating cashflow by approximately $0.08 million for year ended December 31, 2019 (2018 - $0.08 million).

Five manufacturing facilities are located in the U.S. and a significant amount of cost inputs for all production facilities are denominated in U.S. dollars, offsetting a large portion of the U.S. dollar revenue in a natural hedge.

As at December 31, 2019, the amount of financial liabilities denominated in U.S. dollars exceeded the amount of financial assets denominated in U.S. dollars by approximately $27.9 million (2018 - $36.1 million). A 50 basis point weakening/strengthening in the value of the Canadian dollar relative to the U.S. dollar would result in a decrease/increase in income before income taxes of approximately $0.1 million (2018 - $0.2 million).

Pollard also uses financial hedges, including foreign currency contracts, to help manage foreign currency risk. At December 31, 2019, Pollard had no outstanding foreign currency contracts.

Interest rate risk

A 50 basis point decrease/increase in interest rates would result in an increase/decrease in income before income taxes of $0.6 million for the year ended December 31, 2019 (2018 - $0.6 million).

Credit risk

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

Liquidity risk

Pollard's approach is to ensure that it will always have sufficient liquidity to meet its liabilities when due. Pollard maintains a committed credit facility including up to $190.0 million for its Canadian operations and up to US$14.0 million for its U.S. subsidiaries. At December 31, 2019, the unused balance available for drawdown was $69.7 million (2018 - $58.9 million).

The 2020 requirements for capital expenditures, working capital and dividends are expected to be financed from cash flow provided by operating activities and unused portion of Pollard's credit facility. Pollard enters into contractual obligations in the normal course of business operations.

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.

Disclosure Controls and Procedures

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

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

Internal Controls over Financial Reporting

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

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

No changes were made in Pollard's internal control over financial reporting during the year ended December 31, 2019, that have materially affected, or are reasonably likely to materially affect, Pollard's internal control over financial reporting.

Additional Information

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

Additional information relating to Pollard, including the Audited Consolidated Financial Statements and the Annual Information Form for the year ended December 31, 2019, is available on SEDAR at www.sedar.com.

Pollard Banknote Limited
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www.Pollardbanknote.com

Management's Report

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

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

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

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

March 30, 2020

Consolidated Financial Statements of

POLLARD BANKNOTE LIMITED

Years ended December 31, 2019 and 2018

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INDEPENDENT AUDITORS' REPORT

To the Shareholders of Pollard Banknote Limited

Opinion

We have audited the consolidated financial statements of Pollard Banknote Limited (the "Entity"), which comprise the consolidated statements of financial position as at December 31, 2019 and December 31, 2018, the consolidated statements of income, comprehensive income, changes in equity and cash flows for the years then ended, and notes to the financial statements, including a summary of significant accounting policies (hereinafter referred to as the "financial statements").

In our opinion, the accompanying financial statements present fairly, in all material respects, the consolidated financial position of the Entity as at December 31, 2019 and December 31, 2018, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards (IFRS).

Basis for Opinion

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

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

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

Other Information

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

- the information included in Management's Discussion and Analysis filed with the relevant Canadian Securities Commissions.
- the information, other than the financial statements and the auditors' report thereon, included in a document likely to be entitled "Annual Report 2019".

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

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

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

We have nothing to report in this regard.

The information, other than the financial statements and the auditors' report thereon, included in a document likely to be entitled "Annual Report 2019" is expected to be made available to us after the date of this auditors' report. If, based on the work we will perform on this other information, we conclude that there is a material misstatement of this other information, we are required to report that fact to those charged with governance.

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

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

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

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

Auditors' Responsibilities for the Audit of the Financial Statements

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

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

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

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

We also:

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

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

- Obtain an understanding of internal control relevant to the audit in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the Entity's internal control.
- Evaluate the appropriateness of accounting policies used and the reasonableness of accounting estimates and related disclosures made by management.
- Conclude on the appropriateness of management's use of the going concern basis of accounting and, based on the audit evidence obtained, whether a material uncertainty exists related to events or conditions that may cast significant doubt on the Entity's ability to continue as a going concern. If we conclude that a material uncertainty exists, we are required to draw attention in our auditors' report to the related disclosures in the financial statements or, if such disclosures are inadequate, to modify our opinion. Our conclusions are based on the audit evidence obtained up to the date of our auditors' report. However, future events or conditions may cause the Entity to cease to continue as a going concern.
- Evaluate the overall presentation, structure and content of the financial statements, including the disclosures, and whether the financial statements represent the underlying transactions and events in a manner that achieves fair presentation.
- Communicate with those charged with governance regarding, among other matters, the planned scope and timing of the audit and significant audit findings, including any significant deficiencies in internal control that we identify during our audit.
- Provide those charged with governance with a statement that we have complied with relevant ethical requirements regarding independence, and communicate with them all relationships and other matters that may reasonably be thought to bear on our independence, and where applicable, related safeguards.
- Obtain sufficient appropriate audit evidence regarding the financial information of the entities or business activities within the group Entity to express an opinion on the financial statements. We are responsible for the direction, supervision and performance of the group audit. We remain solely responsible for our audit opinion.

KPMG LLP

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

Winnipeg, Canada

March 11, 2020

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

	December 31, 2019	December 31, 2018*
Assets		
Current assets		
Cash	$ 7,448	$ 11,174
Restricted cash	13,000	10,158
Accounts receivable	57,213	34,675
Inventories (note 7)	42,540	45,353
Prepaid expenses and deposits	7,224	6,943
Income tax receivable	5,200	2,279
Total current assets	132,625	110,582
Non-current assets		
Property, plant and equipment (note 8)	91,904	71,606
Equity investment (note 9)	1,161	1,164
Goodwill (note 10)	69,993	69,667
Intangible assets (note 11)	54,207	50,086
Deferred income taxes (note 12)	2,375	2,495
Total non-current assets	219,640	195,018
Total assets	$ 352,265	$ 305,600

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

		December 31, 2019		December 31, 2018*
Liabilities and Shareholders' Equity				
Current liabilities				
Accounts payable and accrued liabilities	$	47,368	$	43,058
Dividends payable		1,025		768
Income taxes payable		641		408
Contract liabilities (note 17)		–		814
Current portion lease liabilities (note 3)		4,375		–
Current portion long-term debt (note 13)		–		40
Total current liabilities		53,409		45,088
Non-current liabilities				
Long-term debt (note 13)		127,295		115,756
Contract liabilities (note 17)		–		43
Other non-current liabilities		337		466
Pension liability (note 14)		26,547		20,357
Lease liabilities (note 3)		11,554		–
Deferred income taxes (note 12)		9,839		6,252
Total non-current liabilities		175,572		142,874
Shareholders' equity				
Share capital (note 15)		108,642		108,605
Reserves		5,705		12,698
Retained earnings (deficit)		8,937		(3,665)
Total shareholders' equity		123,284		117,638
Commitments and contingencies (note 16)				
Subsequent event (note 28)				
Total liabilities and shareholders' equity	$	352,265	$	305,600

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

See accompanying notes to consolidated financial statements.

On behalf of the Board:

"Dave Brown" Director

"John Pollard" Director

Pollard Banknote Limited

Consolidated Statements of Income

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

Years ended December 31

		2019		2018*
Sales (note 17)	$	397,839	$	331,868
Cost of sales		306,733		256,131
Gross profit		91,106		75,737
Administration		40,625		32,154
Selling		15,912		13,395
Other expenses (note 18)		1,955		464
Income from operations		32,614		29,724
Finance costs (note 19)		7,544		9,836
Finance income (note 19)		(3,931)		(881)
Income before income taxes		29,001		20,769
Income taxes (note 12)				
Current		2,136		5,175
Deferred		4,848		742
		6,984		5,917
Net income	$	22,017	$	14,852
Net income per share (basic) (note 20)	$	0.86	$	0.58
Net income per share (diluted) (note 20)	$	0.86	$	0.58

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

See accompanying notes to consolidated financial statements.

Pollard Banknote Limited

Consolidated Statements of Comprehensive Income

(*In thousands of Canadian dollars*)

Years ended December 31

		2019		2018*
Net income	$	22,017	$	14,852
Other comprehensive income (loss)				
Items that are or may be reclassified to profit and loss				
Foreign currency translation differences – foreign operations		(6,993)		9,733
Items that will never be reclassified to profit and loss				
Defined benefit plans remeasurements, net of income tax (reduction) (note 12 & note 14)		(5,409)		2,720
Other comprehensive income (loss)		(12,402)		12,453
Comprehensive income	$	9,615	$	27,305

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

See accompanying notes to consolidated financial statements.

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

Year ended December 31, 2019

		Share capital	Translation reserve	Retained earnings (deficit)	Total equity
Balance at December 31, 2018	$	108,605	12,698	(3,665)	117,638
Net income		–	–	22,017	22,017
Other comprehensive loss					
Foreign currency translation differences – foreign operations		–	(6,993)	–	(6,993)
Defined benefit plans remeasurements, net of income tax reduction (note 12 & note 14)		–	–	(5,409)	(5,409)
Total other comprehensive loss	$	–	(6,993)	(5,409)	(12,402)
Total comprehensive income (loss)	$	–	(6,993)	16,608	9,615
Issue of common shares (note 15)		37	–	(18)	19
Share based compensation		–	–	114	114
Dividends to owners of Pollard Banknote Limited		–	–	(4,102)	(4,102)
Balance at December 31, 2019	$	108,642	5,705	8,937	123,284

Year ended December 31, 2018

		Share capital	Translation reserve	Deficit	Total equity
Balance at December 31, 2017	$	73,209	2,965	(18,605)	57,569
Adjustment on initial application of IFRS 15, net of income tax		–	–	332	332
Adjusted balance at January 1, 2018		73,209	2,965	(18,273)	57,901
Net income		–	–	14,852	14,852
Other comprehensive income					
Foreign currency translation differences – foreign operations		–	9,733	–	9,733
Defined benefit plans remeasurements, net of income tax (note 12 & note 14)		–	–	2,720	2,720
Total other comprehensive income	$	–	9,733	2,720	12,453
Total comprehensive income	$	–	9,733	17,572	27,305
Issue of common shares (note 15)		35,396	–	–	35,396
Share based compensation		–	–	110	110
Dividends to owners of Pollard Banknote Limited		–	–	(3,074)	(3,074)
Balance at December 31, 2018	$	108,605	12,698	(3,665)	117,638

See accompanying notes to consolidated financial statements.

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

Years ended December 31

	2019	2018*
Cash increase (decrease)		
Operating activities		
Net income	$ 22,017	$ 14,852
Adjustments		
Income taxes	6,984	5,917
Amortization and depreciation	27,138	18,017
Interest expense	6,415	4,243
Unrealized foreign exchange loss (gain)	(3,361)	4,533
Loss on equity investment (note 9)	3,942	2,631
Pension expense (note 14)	6,476	6,449
Contract liabilities (note 17)	(43)	(773)
Interest paid	(6,372)	(4,484)
Income tax paid	(3,988)	(10,187)
Pension contribution	(7,413)	(5,534)
Change in non-cash operating working capital (note 22)	(22,500)	3,997
	29,295	39,661
Investing activities		
Additions to property, plant and equipment (note 8)	(17,240)	(15,090)
Acquisition of Fastrak Retail (UK) Limited (note 6)	(8,542)	–
Acquisition of International Gamco, Inc.	–	(21,558)
Acquisition of Schafer (note 6)	–	(30,447)
Proceeds from sale of equipment	20	–
Equity investment (note 9)	(3,997)	(2,842)
Additions to intangible assets (note 11)	(8,553)	(7,145)
	(38,312)	(77,082)
Financing activities		
Proceeds from issue of share capital (note 15)	19	35,396
Net proceeds from long-term debt (note 13)	14,321	27,878
Net repayments of subordinated debt	–	(16,734)
Change in other non-current liabilities	(107)	(328)
Deferred financing charges paid (note 13)	(450)	(561)
Change in dividend payable	–	62
Lease principal payments	(4,378)	–
Dividends paid	(3,845)	(3,074)
	5,560	42,639
Foreign exchange gain (loss) on cash held in foreign currency	(269)	353
Change in cash position	(3,726)	5,571
Cash position, beginning of year	11,174	5,603
Cash position, end of year	$ 7,448	$ 11,174

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

See accompanying notes to consolidated financial statements.

1. Reporting entity:

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

The consolidated financial statements of Pollard as at and for the year ended December 31, 2019, comprise Pollard, Pollard's subsidiaries and its interest in other entities. Pollard is primarily involved in the manufacture and sale of lottery and gaming products.

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

The operations of Fastrak Retail (UK) Limited ("Fastrak"), acquired during the second quarter of 2019, are included in the consolidated financial statements from May 1, 2019. Further details are provided in note 6.

2. Basis of preparation:

(a) Statement of compliance:

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

On March 11, 2020, Pollard's Board of Directors approved these consolidated financial statements.

(b) Basis of preparation:

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

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

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

2. Basis of preparation (continued):

(c) Use of estimates and judgments:

The preparation of the consolidated financial statements in conformity with IFRS requires management to make judgments, estimates and assumptions that affect the application of accounting policies and the reported amounts of assets, liabilities, income and expenses. Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognized prospectively. Actual results may differ from these estimates.

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

Impairment of goodwill:

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

Employee future benefits:

Accounting for defined benefit plans requires Pollard to use actuarial assumptions. These assumptions include the discount rate and the rate of compensation increases. These assumptions depend on underlying factors such as economic conditions, government regulations, investment performance, employee demographics and mortality rates. Further details are provided in note 14.

Income taxes:

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

Leases:

Upon inception of all leases, Pollard assesses whether it is reasonably certain that lease extension options will be exercised.

2. Basis of preparation (continued):

Pollard also makes assumptions as to the discount rate applied to the lease liability upon recognition. If there is a significant event or change in circumstances within Pollard's control, these judgments and assumptions could change and may result in material adjustments to right-of-use assets and corresponding lease liabilities.

Acquisition accounting:

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

3. Accounting standards implemented in 2019:

(a) Leases:

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

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

Impact on the 2019 Consolidated Financial Statements

On initial application, Pollard has elected to record right-of-use assets based on the corresponding lease liability. Right-of-use assets (included in property, plant and equipment on the statement of financial position) of $18,279, current portion of lease liabilities of $4,348 and long-term portion of lease liabilities of $13,931 were recorded as of January 1, 2019, with no net impact on retained earnings. When measuring lease liabilities, Pollard discounted lease payments using its incremental borrowing rate of 4.0% at January 1, 2019.

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

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

3. Accounting standards implemented in 2019 (continued):

The following tables summarize the impact of adopting IFRS 16 on Pollard's consolidated statement of financial position as at December 31, 2019 and its consolidated statement of income for the twelve months ended December 31, 2019.

Impact on Pollard's consolidated statement of financial position as at December 31, 2019:

	Amount without IFRS 16	IFRS 16 Adjustment	As Reported
Property, plant and equipment	$ 76,315	$ 15,589	$ 91,904
Current portion lease liabilities	–	4,375	4,375
Lease liabilities	–	11,554	11,554
Retained earnings (deficit)	9,277	(340)	8,937

Impact on Pollard's consolidated statement of income for the twelve months ended December 31, 2019:

	Amount without IFRS 16	IFRS 16 Adjustment	As Reported
Cost of sales	$ 307,055	$ (322)	$ 306,733
Finance costs	6,882	662	7,544

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

	Buildings	Equipment	Furniture, Fixtures and Computers	Total
Opening balance, January 1, 2019	$ 17,750	$ 132	$ 397	$ 18,279
Acquisition	322	100	–	422
Additions	1,756	–	5	1,761
Depreciation	(4,492)	(72)	(178)	(4,742)
Effect of movements in exchange rates	(104)	(18)	(9)	(131)
Closing balance, December 31, 2019	$ 15,232	$ 142	$ 215	$ 15,589

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

3. Accounting standards implemented in 2019 (continued):

For the year ended December 31, 2019, Pollard's total cash outflow, principal and interest, relating to its lease obligations classified under IFRS 16 *Leases* was $5,039.

4. Significant accounting policies:

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

(a) Principles of consolidation:

These consolidated financial statements include the accounts of Pollard and all its subsidiaries.

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

Significant subsidiaries:	Percent Ownership Interest	
	December 31, 2019	December 31, 2018
Pollard Holdings, Inc.	100	100
Pollard (U.S.) Ltd.	100	100
Pollard Games, Inc.	100	100
Pollard iLottery Inc.	100	100
Diamond Game Enterprises	100	100
Diamond Game Enterprises Canada ULC	100	100
International Gamco Inc.*	–	100
Schafer Systems (2018) Inc.	100	100
Fastrak Retail (UK) Limited	100	–

*Effective December 31, 2019, International Gamco Inc. and Pollard Games, Inc. were amalgamated. The amalgamated entity retained the Pollard Games, Inc. legal name.

Pollard has entered into a contractual joint agreement with Neogames S.à r.l. for the operation of iLottery gaming for the Michigan Lottery. As such Pollard has recognized in relation to its interest in the joint operation: its assets, including its share of any assets held jointly; its liabilities, including its share of any liabilities incurred jointly and its share of revenue and expenses.

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

4. Significant accounting policies (continued):

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

(b) Business combinations:

Business combinations are accounted for using the acquisition method. The cost of an acquisition is measured as the fair value of the assets given, equity instruments and liabilities incurred or assumed at the date of exchange.

Acquisition costs for business combinations are expensed as incurred and included in administration expenses. Identifiable assets acquired and liabilities assumed are measured at their fair value at the acquisition date.

The excess of the fair value of consideration transferred over the fair value of the identifiable net assets acquired is recorded as goodwill.

(c) Restricted cash:

Pollard, under certain contractual arrangements, controls cash that is restricted in use. Pollard records an equal, offsetting liability classified within accounts payable and accrued liabilities. Restricted cash includes player deposits held for the benefit of Pollard's iLottery customer, in addition to funds held for security purposes and certain contractual liabilities. Pollard has excluded changes in the restricted cash and related liability from its calculation of the change in cash position in the statements of cash flows.

(d) Revenue recognition:

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

Many of Pollard's contracts have a single performance obligation, including the sale of instant tickets and related products, pull-tab (or break-open) tickets, bingo paper, pull-tab vending machines, ancillary products such as pull-tab counting machines and gaming machines. The single performance obligation in these contracts is the promise to transfer the individual goods. Revenue is recognized at a point in time when the customer obtains control of a product, which typically takes place when legal title and physical possession of the product is transferred to the customer. These conditions are usually fulfilled upon delivery. However, under certain contracts, Pollard is compensated for its products based on its customers' sales of those products at retail.

4. Significant accounting policies (continued):

Pollard has concluded that control transfers to its customers at delivery of the product to the customer. As such, recognition of sales under these contracts occurs upon receipt of shipment. Pollard's sales under these contracts could vary year over year depending on the timing of shipments.

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

Where Pollard provides software and related infrastructure, revenue is recognized over time based on the relevant measure of progress of the asset being transferred to the customer.

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

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

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

(e) Inventories:

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

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

4. Significant accounting policies (continued):

(f) Goodwill:

Goodwill is comprised of the excess sale price over the underlying carrying amount of the net assets sold as at August 5, 2005, as part of the 26.7% of Pollard sold in conjunction with the Initial Public Offering ("IPO") and the excess fair value of the consideration transferred over the fair value of the identifiable net assets acquired of Pollard's subsidiaries.

Goodwill is not amortized but is subject to an annual impairment test to ensure its recoverable value remains greater than, or equal to, book value.

(g) Intangible assets:

Deferred development

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

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

Computer software and licenses

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

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

Customer assets and patents

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

4. Significant accounting policies (continued):

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

Asset	Rate
Customer assets	5 to 20 years
Patents	Term of patent
Computer software and licenses	3 to 15 years or term of license
Deferred development	5 years

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

Trademarks, trade names and brands

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

(h) Property, plant and equipment:

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

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

4. Significant accounting policies (continued):

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

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

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

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

(i) Investment in joint venture:

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

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

(j) Investment in joint operation:

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

The consolidated financial statements include Pollard's interest in the Michigan Lottery iLottery joint operations: its assets, including its share of any assets held jointly; its liabilities, including its share of any liabilities incurred jointly and its share of revenue and expenses.

4. Significant accounting policies (continued):

(k) Financial instruments:

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

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

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

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

Hedge accounting

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

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

4. Significant accounting policies (continued):

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

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

(l) Impairment:

Financial assets

Pollard applies the simplified approach to providing for expected credit losses, which requires the use of the lifetime expected credit loss provision for all accounts receivable. Expected credit losses are measured as the difference in the present value of the contractual cash flows that are due under the contract and the cash flows that Pollard expects to receive. The expected cash flows reflect all available information, including Pollard's historical experience, the past due status, and forward-looking macroeconomic factors. Further details are provided in note 26 and note 27.

Non-financial assets

The carrying amount of Pollard's non-financial assets, other than inventories and deferred income tax assets, are reviewed at each reporting date to determine whether there is an indication that an asset may be impaired.

If any such indication exists, or when the annual impairment testing for an asset is required, Pollard estimates the asset's recoverable amount. For goodwill the recoverable amount is estimated as of December 31 each year. An impairment loss is recognized if the carrying amount of an asset or its related CGU exceeds its estimated recoverable amount.

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. In assessing value in use, the estimated future cash flows are discounted to their present value using a pre-tax discount rate that reflects current market assessments of the time value of money and the risks specific to the asset of CGU.

4. Significant accounting policies (continued):

For the purpose of impairment testing, assets that cannot be tested individually are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of cash inflows of other assets or CGUs.

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

(m) Share capital:

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

(n) Translation of foreign currencies:

The functional currency for each of Pollard's subsidiaries is the currency of the primary economic environment in which the entity operates. Transactions in foreign currencies are translated to the respective functional currencies of each entity within the consolidated group using the exchange rates in effect at the date of the transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rates prevailing at the end of the reporting period. Non-monetary items measured at historical cost in a foreign currency are translated to the functional currency using the exchange rate prevalent at the date of acquisition. Non-monetary items denominated in foreign currencies that are measured at fair value are translated to the functional currency at the exchange rate prevalent at the date that the fair value was determined.

Foreign currency differences arising from translation are recognized in net income, except for exchange differences arising on the translation of financial instruments qualifying as a cash flow hedge, which are recognized directly in other comprehensive income ("OCI").

The results and financial position of entities within the consolidated group that have a functional currency different from the presentation currency are translated into Canadian dollars as follows: assets and liabilities are translated at the exchange rate prevailing at the end of the reporting period; income and expenses are translated at the average rate for the reporting period; all resulting exchange differences are recognized in OCI.

4. Significant accounting policies (continued):

On disposal of a foreign operation, the deferred cumulative amount recognized in OCI relating to that particular foreign operation is recognized in net income.

(o) Employee benefits:

Share based compensation

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

Defined contribution plans

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

Defined benefit plans

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

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

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

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

4. Significant accounting policies (continued):

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

(p) Income taxes:

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

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

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

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

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

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

4. Significant accounting policies (continued):

(q) Provisions:

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

(r) Finance costs and finance income:

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

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

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

(s) Leases:

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

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

Pollard recognizes a right-of-use asset and a lease liability at the lease commencement date. The right-of-use asset is initially measured at cost, which comprises the initial amount of the lease liability adjusted for any lease payments made at or before the commencement date, plus any direct costs incurred and an estimate of costs to dismantle and remove the underlying asset or to restore the underlying asset or the site on which it is located, less any lease incentives received.

The right-of-use asset is subsequently depreciated using the straight-line method from the commencement date to the earlier of the end of the useful life of the right-of-use asset or the end of the lease term.

4. Significant accounting policies (continued):

The estimated useful lives of right-of-use assets are determined on the same basis as those of property, plant and equipment. The right-of-use asset is subsequently measured at cost less any accumulated depreciation and impairment losses.

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

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

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

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

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

5. Future accounting standards:

Amendments to IFRS 3 – definition of a business:

In October 2018, the International Accounting Standards Board ("IASB") issued amendments to IFRS 3 *Business Combinations,* that seek to clarify whether a transaction results in an asset or a business acquisition. The amendments include an election to use a concentration test. This is a simplified assessment that results in an asset acquisition if substantially all of the fair value of the gross assets is concentrated in a single identifiable asset or a group of similar identifiable assets. The amendments apply to businesses acquired in annual reporting periods beginning on or after January 1, 2020. Pollard does not expect the amendments to have a significant impact on the consolidated financial statements upon adoption.

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

6. Acquisitions:

(a) Schafer Systems Inc.:

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

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

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

As at September 30, 2019, the acquisition accounting was finalized.

(b) Fastrak Retail (UK) Limited:

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

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

6. Acquisitions (continued):

Cash paid, net of cash acquired of $1,213	$	8,038
Contingent consideration		504
Total consideration transferred	$	8,542
Additional net tangible assets acquired:		
Accounts receivable	$	2,418
Inventories		885
Prepaid expenses and deposits		177
Property, plant and equipment		1,646
Income taxes receivable		128
Accounts payable and accrued liabilities		(2,121)
Lease liabilities		(402)
Deferred income tax liability		(997)
Net tangible assets acquired (excluding cash)	$	1,734
Customer relationships	$	3,770
Brand		457
Patents		342
Identifiable intangible assets acquired	$	4,569
Goodwill acquired	$	2,239

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

Acquisition costs related to the Fastrak purchase in the twelve months ended December 31, 2019, were $457. These costs were included in administration expenses.

During the period between May 1, 2019 and December 31, 2019, Fastrak generated revenues of approximately $7,435 and net income of $13, after depreciation and amortization of the fair values of identifiable assets acquired, which have been recorded in the consolidated financial statements.

If Fastrak had been acquired on January 1, 2019, incremental revenue of $3,203 and net loss of $441, after depreciation and amortization of the fair values of identifiable assets acquired, would have been recognized in the twelve months ended December 31, 2019.

Contingent consideration, based on achievement of certain revenue and earnings before interest, taxes, depreciation and amortization (“EBITDA”) targets, may be paid to the vendor. The revenue earn-out target is based on achievement of certain sales volumes to one customer during the period 2019 through 2023. The maximum potential payment under the revenue-based earn-out

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

6. Acquisitions (continued):

is £2 million. Pollard believes the likelihood of future revenue earn-out payments is low, and as such, has not accrued a liability for the revenue earn-out.

The EBITDA earn-out is based on Fastrak's achievement of certain EBITDA targets during the period 2019 through 2021. The potential payment under the EBITDA earn-out is unlimited. Pollard initially accrued $504 relating to the EBTIDA earn-out upon acquisition. Subsequent to December 31, 2019, payment under the EBITDA earn-out was made to the vendor in the amount of $312. Pollard believes the likelihood of additional future EBITDA earn-out payments is low, and as such, reversed the remaining accrual of $192 through other income. As a result, Pollard has no liability accrued for the EBITDA earn-out as at December 31, 2019.

7. Inventories:

	December 31, 2019	December 31, 2018
Raw materials	$ 17,957	$ 18,537
Work-in-process	1,726	2,861
Finished goods	22,857	23,955
	$ 42,540	$ 45,353

During 2019, Pollard recorded inventory write-downs of $580 representing an increase in the obsolescence reserves and write-downs of $46 due to changes in foreign exchange rates.

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

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

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

8. Property, plant and equipment:

Cost	Land	Buildings	Leasehold improve-ments	Equipment	Furniture, fixture and computers	Assets in progress & spare parts	Total
Balance at January 1, 2018	$ 803	12,156	3,527	157,800	6,830	2,352	183,468
Acquisitions	881	7,496	–	3,832	–	225	12,434
Additions/net transfers	–	195	1,460	6,549	510	6,376	15,090
Disposals	–	–	–	(65)	–	–	(65)
Effect of movements in exchange rates	47	145	74	2,269	26	44	2,605
Balance at December 31, 2018	$ 1,731	19,992	5,061	170,385	7,366	8,997	213,532
Recognition of right-of-use assets on initial application of IFRS 16 – January 1, 2019	–	17,750	–	132	397	–	18,279
Acquisitions	–	321	128	1,170	28	–	1,647
Additions/net transfers*	–	2,684	247	17,096	453	(382)	20,098
Disposals	–	–	–	(1,361)	–	–	(1,361)
Effect of movements in exchange rates	(39)	(557)	(40)	(1,184)	(28)	(120)	(1,968)
Balance at December 31, 2019	$ 1,692	40,190	5,396	186,238	8,216	8,495	250,227

*Included within additions/net transfers is $1,097 of machine costs previously classified as inventory, which were reclassified to property, plant and equipment during 2019. Also included within additions/net transfers, within the buildings asset class, is $1,761 of right-of-use lease asset additions.

Accumulated depreciation	Land	Buildings	Leasehold improve-ments	Equipment	Furniture, fixture and computers	Assets in progress & spare parts	Total
Balance at January 1, 2018	$ –	5,281	2,150	117,335	4,383	–	129,149
Depreciation for the year	–	444	242	11,129	233	–	12,048
Disposals	–	–	–	(47)	–	–	(47)
Effect of movements in exchange rates	–	2	74	691	9	–	776
Balance at December 31, 2018	$ –	5,727	2,466	129,108	4,625	–	141,926
Depreciation for the year	–	5,265	391	12,376	433	–	18,465
Disposals	–	–	–	(1,343)	–	–	(1,343)
Effect of movements in exchange rates	–	(72)	(43)	(600)	(10)	–	(725)
Balance at December 31, 2019	$ –	10,920	2,814	139,541	5,048	–	158,323

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

8. Property, plant and equipment (continued):

Carrying amounts		Land	Buildings	Leasehold improve-ments	Equipment	Furniture, fixture and computers	Assets in progress & spare parts	Total
At December 31, 2018	$	1,731	14,265	2,595	41,277	2,741	8,997	71,606
At December 31, 2019	$	1,692	29,270	2,582	46,697	3,168	8,495	91,904

9. Equity investment:

Interest in joint venture		December 31, 2019		December 31, 2018
Balance, beginning of year	$	1,164	$	877
Investment		3,997		2,842
Equity loss		(3,942)		(2,631)
Effects of movements in exchange rates		(58)		76
Balance, end of year	$	1,161	$	1,164

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

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

10. Goodwill:

		December 31, 2019		December 31, 2018
Balance, beginning of year	$	69,667	$	51,768
Acquisition of Fastrak (note 6)		2,239		–
Acquisition of Gamco		–		5,884
Acquisition of Schafer (note 6)		–		9,233
Effects of movements in exchange rates		(1,913)		2,782
Balance, end of year	$	69,993	$	69,667

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

10. Goodwill (continued):

Impairment assessment methodology

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

		December 31, 2019		December 31, 2018
Lotteries	$	30,816	$	30,816
American Games		6,678		7,012
Diamond Game		14,991		15,741
Gamco		6,220		6,513
Schafer		9,128		9,585
Fastrak		2,160		–
Total	$	69,993	$	69,667

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

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

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

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

Revenue and related gross profit

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

10. Goodwill (continued):

Foreign exchange rates

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

Discount rates

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

Lotteries	12.0%
American Games	12.0%
Diamond Game	15.0%
Gamco	12.0%
Schafer	14.7%
Fastrak	16.0%

Growth rates

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

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

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

11. Intangible assets:

Cost		Customer assets	Patents	Trademarks	Deferred development	Computer software and licenses	Total
Balance at January 1, 2018	$	28,991	5,696	2,641	1,210	12,004	50,542
Acquisitions		15,484	167	1,539	–	579	17,769
Additions (net of investment tax credits)		–	742	–	429	678	1,849
Additions – internally developed (net of investment tax credits)		–	–	–	–	5,296	5,296
Effect of movements in exchange rates		1,769	46	323	–	460	2,598
Balance at December 31, 2018	$	46,244	6,651	4,503	1,639	19,017	78,054
Asset reclassifications*		–	(662)	–	–	662	–
Acquisitions		3,770	361	457	–	–	4,588
Additions (net of investment tax credits)		–	160	25	–	479	664
Additions – internally developed (net of investment tax credits)**		–	–	–	154	7,841	7,995
Effect of movements in exchange rates		(1,379)	(63)	(222)	–	(389)	(2,053)
Balance at December 31, 2019	$	48,635	6,447	4,763	1,793	27,610	89,248

Accumulated amortization		Customer assets	Patents	Trademarks	Deferred development	Computer software and licenses	Total
Balance at January 1, 2018	$	15,070	4,908	–	1,210	1,608	22,796
Amortization for the year		3,152	204	–	36	1,555	4,947
Effect of movements in exchange rates		120	6	–	–	99	225
Balance at December 31, 2018	$	18,342	5,118	–	1,246	3,262	27,968
Asset reclassifications*		–	(62)	–	–	62	–
Amortization for the year		4,294	167	–	102	2,823	7,386
Effect of movements in exchange rates		(184)	(13)	–	–	(116)	(313)
Balance at December 31, 2019	$	22,452	5,210	–	1,348	6,031	35,041

*During 2019, $662 of costs previously capitalized as intangible assets within the patents asset class were reclassified to the computer software and licenses asset class. Related amortization of $62 was also reclassified between patents and computer software and licenses.

**Included within additions – internally developed (net of investment tax credits) is $106 of software costs previously classified as inventory, which were reclassified to intangible assets during 2019.

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

11. Intangible assets (continued):

Carrying amounts		Customer assets	Patents	Trademarks	Deferred development	Computer software and licenses	Total
At December 31, 2018	$	27,902	1,533	4,503	393	15,755	50,086
At December 31, 2019	$	26,183	1,237	4,763	445	21,579	54,207

Amortization of intangible assets in 2019 of $7,386 (2018 – $4,947), was included in cost of sales.

As at December 31, 2019, the weighted average remaining useful life of customer assets was 8.9 years.

12. Income taxes:

Income tax expense

		2019		2018
Current	$	2,136	$	5,175
Deferred		4,848		742
Total	$	6,984	$	5,917

Income tax recognized in other comprehensive income (loss)

		Amount before tax	Tax benefit	2019 Amount net of tax		Amount before tax	Tax expense	2018 Amount net of tax
Defined benefit plans remeasurements gain (loss)	$	(7,300)	1,891	(5,409)	$	3,695	(975)	2,720

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

12. Income taxes (continued):

Reconciliation of effective tax rate

	2019	2019	2018	2018
Net income for the year		$ 22,017		$ 14,852
Total income tax expense		6,984		5,917
Income before income taxes		$ 29,001		$ 20,769
Income tax using Pollard's domestic tax rate	27.0%	7,829	27.0%	5,608
Effect of tax rates in foreign jurisdictions	(2.2%)	(632)	(2.5%)	(508)
Non-deductible amounts	1.8%	527	2.7%	553
Other items	(0.5%)	(162)	(2.4%)	(500)
Effect of non-taxable items related to foreign exchange	(2.0%)	(578)	3.7%	764
	24.1%	$ 6,984	28.5%	$ 5,917

Deferred income tax assets and liabilities

Recognized deferred income tax assets and liabilities

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

	Assets		Liabilities		Net	
	2019	2018	2019	2018	2019	2018
Property, plant and equipment	$ –	23	$ (12,375)	(9,319)	$ (12,375)	(9,296)
Intangible assets	2,253	2,954	(5,913)	(6,067)	(3,660)	(3,113)
Inventories	228	259	–	(57)	228	202
Employee benefits	9,070	7,409	(1,377)	(1,227)	7,693	6,182
Unrealized foreign exchange (gains) and losses	487	1,126	(655)	(874)	(168)	252
Unused tax losses	994	2,153	–	–	994	2,153
Contract liabilities	45	56	(247)	(272)	(202)	(216)
Other	301	101	(275)	(22)	26	79
Tax assets (liabilities)	$ 13,378	14,081	$ (20,842)	(17,838)	$ (7,464)	(3,757)

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

12. Income taxes (continued):

Movement in temporary differences during the year

		January 1, 2019	Recognized in profit or loss	Acquisitions	Recognized in other comprehensive income	Balance December 31, 2019
Property, plant and equipment	$	(9,296)	(2,942)	(137)	–	(12,375)
Intangible assets		(3,113)	310	(857)	–	(3,660)
Inventories		202	26	–	–	228
Employee benefits		6,182	(365)	–	1,891	7,708
Unrealized foreign exchange (gains) and losses		252	(435)	–	–	(183)
Unused tax losses		2,094	(1,100)	–	–	994
Contract liabilities		57	(259)	–	–	(202)
Other		(135)	161	–	–	26
Tax assets (liabilities)	$	(3,757)	(4,604)	(994)	1,891	(7,464)

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

* January 1, 2018 figure includes the impact of the transitional adjustment booked to opening deficit upon adoption of IFRS 15 of $123.

Recognized in the consolidated statements of comprehensive income as follows:

		2019		2018
Deferred income tax expense	$	4,848	$	742
Finance income (loss)		(244)		472
	$	4,604	$	1,214

Amounts included in finance income (loss) relate to unrealized foreign exchange.

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

13. Long-term debt:

	December 31, 2019	December 31, 2018
Credit facility, interest of 4.02% to 4.32%, payable monthly, maturing 2022	$ 127,820	$ 116,177
Equipment debt	–	4
Equipment lease	–	36
Deferred financing charges, net of amortization	(525)	(421)
	127,295	115,796
Less current portion	–	(40)
	$ 127,295	$ 115,756

	Credit facility	Deferred financing	Equipment debt	Equipment lease	Total
Balance at January 1, 2019	$ 116,177	(421)	4	36	115,796
Net proceeds (payments)	14,361	–	(4)	(36)	14,321
Payment of deferred financing charges	–	(450)	–	–	(450)
Total changes from financing cash flows	14,361	(450)	(4)	(36)	13,871
Effect of movements in exchange rates	(2,718)	–	–	–	(2,718)
Amortization of deferred financing charges	–	346	–	–	346
Total other changes	(2,718)	346	–	–	(2,372)
Balance at December 31, 2019	$ 127,820	(525)	–	–	127,295

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

13. Long-term debt (continued):

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

Credit facility

Effective December 31, 2019, Pollard renewed its credit facility. The credit facility provides loans of up to $190,000 for its Canadian operations and US$14,000 for its U.S. subsidiaries. The credit facility also includes an accordion feature which can increase the facility by $35,000. The borrowings for the Canadian operations can be denominated in Canadian or U.S. dollars, to a maximum of $190,000 Canadian equivalent. Borrowings under the credit facility bear interest at fixed and floating rates based on Canadian and U.S. prime bank rates, banker's acceptances or LIBOR. At December 31, 2019, the outstanding letters of guarantee drawn under the credit facility were $10,704 (2018 – $1,337).

Included in the total credit facility balance is a U.S. dollar denominated balance of US$36,400 (2018 – US$43,600).

Under the terms and conditions of the credit facility agreement Pollard is required to maintain certain financial covenants including debt to income before interest, income taxes, amortization, depreciation and certain other items ("Adjusted EBITDA") ratios and certain debt service coverage ratios. As at December 31, 2019, Pollard is in compliance with all financial covenants.

As of December 31, 2019, Pollard had unused credit facility available of $69,676 (2018 – $58,860).

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

13. Long-term debt (continued):

Pollard's credit facility is secured by a first security interest in all of the present and after acquired property of Pollard. Under the terms of the agreement the facility is committed for a three-year period, renewable December 31, 2022. Principal payments are not required until maturity. The facility can be prepaid without penalties.

14. Pension liability:

	December 31, 2019	December 31, 2018
Fair value of benefit plan assets	$ 65,481	$ 52,946
Present value of benefit plan obligations	(92,028)	(73,303)
Net pension liability	$ (26,547)	$ (20,357)

Pollard sponsors non-contributory defined benefit plans providing pension benefits to its employees. Pollard has four defined benefit pension plans of which three are final pay plans and one is a flat benefit plan. None of the plans have indexation features. The measurement date for all the plans is December 31. Two of the plans of the U.S. subsidiaries require valuations annually with the last valuations being as of January 1, 2019. One of the Canadian plans of Pollard currently requires valuation every year with the last valuation as of December 31, 2018. Pollard's other Canadian plan's valuation was as of January 1, 2017. Pollard's U.S. subsidiaries also maintain five defined contribution plans. The pension expense for these defined contribution plans is the annual funding contribution by the subsidiaries.

Pollard expects to contribute approximately $6,474 to its defined benefit plans in 2020. Included in the 2020 estimated contributions is $1,643 in additional solvency payments.

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

	December 31, 2019	December 31, 2018
Equities	61.0%	62.0%
Bonds	36.6%	35.8%
Cash and cash equivalents	2.4%	2.2%
	100.0%	100.0%

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

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

14. Pension liability (continued):

		2019		2018
Benefit plan assets				
Fair value, beginning of year	$	52,946	$	50,506
Expected return on plan assets		2,163		1,788
Employer contributions		6,310		4,720
Benefits paid		(2,281)		(1,548)
Remeasurement gains (losses)		6,689		(3,024)
Effect of movements in exchange rates		(346)		504
Fair value, end of year	$	65,481	$	52,946

		2019		2018
Accrued benefit plan obligations				
Balance, beginning of year	$	73,303	$	73,465
Current service cost		4,656		4,839
Interest cost		2,858		2,512
Benefits paid		(2,281)		(1,548)
Remeasurement (gains) losses		13,948		(6,790)
Effect of movements in exchange rates		(456)		825
Balance, end of year	$	92,028	$	73,303
Net pension liability	$	(26,547)	$	(20,357)

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

		2019		2018
Net defined benefit plans cost				
Current service cost	$	4,656	$	4,839
Interest on plan obligations		2,858		2,512
Actual return on plan assets		(8,852)		1,236
Difference between expected return and actual return on plan assets		7,059		(2,655)
Net defined benefit plans cost		5,721		5,932
Defined contribution plans cost		755		517
Net pension plans cost	$	6,476	$	6,449

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

14. Pension liability (continued):

Actuarial assumptions

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

	2019	2018
Discount rate	3.1% to 3.7%	3.9% to 4.6%
Rate of compensation increase	0% to 3.0%	0% to 3.0%

Assumptions regarding future mortality have been based on published statistics and mortality tables. As of December 31, 2019, Pollard used CPM2014 Private Sector projected CPM-B mortality table for its Canadian subsidiary's pension plans and the Pri-2012 mortality tables using scale MP-2019 for its U.S. subsidiary's pension plans. As of December 31, 2018, Pollard used CPM2014 Private Sector projected CPM-B mortality table for its Canadian subsidiary's pension plans and the RP-2018 healthy mortality tables for its U.S. subsidiary's pension plans.

Sensitivity analysis

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

		Increase		Decrease
Discount rate (1% movement)	$	(17,138)	$	22,936
Rate of compensation (1% movement)	$	2,462	$	(2,258)
Future mortality (one year)	$	1,372	$	(1,321)

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

14. Pension liability (continued):

Remeasurements

		2019		2018
Remeasurement gains (losses) arising on plan assets	$	6,689	$	(3,024)

		2019		2018
Remeasurement (gains) losses arising on plan liabilities from:				
Demographic assumptions	$	(232)	$	23
Financial assumptions		14,240		(8,601)
Experience adjustments		(60)		1,788
Remeasurement (gains) losses arising on plan liabilities	$	13,948	$	(6,790)

Remeasurements recognized in other comprehensive income

		2019		2018
Amount accumulated in deficit, beginning of year	$	(16,673)	$	(19,393)
Recognized during the year, net of income tax		(5,409)		2,720
Amount accumulated in retained earnings, end of year	$	(22,082)	$	(16,673)

15. Share capital:

	Shares		Amount
Authorized			
Unlimited common shares			
Unlimited preferred shares			
Issued			
Balance at January 1, 2018	23,543,158	$	73,209
Issuance of common shares	2,070,000		35,351
Stock option exercise	12,500		45
Balance at December 31, 2018	25,625,658		108,605
Stock option exercise	10,000		37
Balance at December 31, 2019	25,635,658	$	108,642

15. Share capital (continued):

Ownership restrictions:

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

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

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

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

Capital management:

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

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

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

15. Share capital (continued):

Pollard monitors capital on the basis of funded debt to Adjusted EBITDA, working capital ratio and debt service coverage. Pollard has externally imposed capital requirements as determined through its bank credit facility. As at December 31, 2019, Pollard is in compliance with all financial covenants.

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

Dividends:

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

On November 5, 2019, a dividend of $0.04 per share was declared, payable on January 15, 2020, to the shareholders of record on December 31, 2019.

Share based compensation:

Under the Pollard Banknote Limited Stock Option Plan the Board of Directors has the authority to grant options to purchase common shares to eligible persons and to determine the applicable terms.

The aggregate maximum number of common shares available for issuance from Pollard's treasury under the Option Plan is 2,354,315 common shares.

Options have been granted on four grant dates, with the exercise price being the common share price on the exercise price determination date. All of the outstanding options have seven year terms, vesting 25% per year over the first four years.

Option grant date	November 8, 2019	April 24, 2017	October 3, 2016	March 10, 2014
Fair value at grant date	$ 5.13	$ 2.27	$ 1.87	$ 0.82
Number of options granted	150,000	125,000	25,000	100,000
Share price	$ 20.70	$ 10.00	$ 8.12	$ 3.63
Exercise price	$ 20.70	$ 10.00	$ 8.12	$ 3.63
Exercise price determination date	November 7, 2019	April 21, 2017	September 30, 2016	March 7, 2014
Expected volatility	31.3%	29.3%	30.7%	33.7%
Option life (expected weighted average life)	4.75 years	4.75 years	4.75 years	4.75 years
Risk-free interest rate (based on Canadian government bonds)	1.5% to 1.6%	0.6% to 0.7%	0.6% to 0.7%	1.7% to 2.1%

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

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

15. Share capital (continued):

	2019			2018		
	Number		Weighted average exercise price	Number		Weighted average exercise price
Balance, beginning of year	237,500	$	7.46	250,000	$	7.26
Granted during the year	150,000	$	20.70	–	$	–
Exercised during the year	(10,000)	$	3.63	(12,500)	$	3.63
Balance, end of year	377,500	$	12.82	237,500	$	7.46

As of December 31, 2019, no share options had expired. Of the 377,500 options outstanding at December 31, 2019, 121,250 were exercisable.

16. Commitments and contingencies:

Pollard and certain subsidiaries rent premises and equipment under long-term leases. The majority of these leases have been classified as right-of-use assets under IFRS 16 *Leases*, effective January 1, 2019. Refer to note 3. The following is a schedule by fiscal year of rental payment commitments outstanding:

2020	$	5,473
2021		4,474
2022		4,021
2023		3,147
2024		937

Pollard is contingently liable for outstanding letters of guarantee in the amount of $10,704 at December 31, 2019 (2018 – $1,337). These letters of guarantee are part of Pollard's credit facility and are secured as disclosed in note 13.

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

16. Commitments and contingencies (continued):

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

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

On September 12, 2018, Pollard entered into a lease arrangement for land and building in Lansing, Michigan. The lease commences upon occupancy of space after construction completion, expected in 2020. The lease has a seven year term, with options for two consecutive five year extensions. Annual rent for the lease is approximately $380 per year.

On February 6, 2020, Pollard Games, Inc. entered into an agreement, approved by the courts, to acquire certain fixed assets and intellectual property for a purchase price of $3,766 which were being sold under a bankruptcy process. The transaction is subject to certain closing conditions and is expected to close on March 20, 2020. These assets had previously been used in the operation of a business producing pull-tab tickets for the lottery and charitable gaming business.

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

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

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

17. Revenue and contract balances:

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

Revenue – geographical segment	Year ended December 31, 2019		
	Lotteries and charitable gaming	Diamond Game	Total
Canada	$ 71,883	$ 9,879	$ 81,762
United States	222,559	16,034	238,593
International	77,484	–	77,484
Total	$ 371,926	$ 25,913	$ 397,839

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

Revenue – product lines	Year ended December 31, 2019		
	Lotteries and charitable gaming	Diamond Game	Total
Lottery	$ 309,452	$ –	$ 309,452
Charitable	62,474	–	62,474
Gaming systems	–	25,913	25,913
Total	$ 371,926	$ 25,913	$ 397,839

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

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

17. Revenue and contract balances (continued):

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

Contract balances		December 31, 2019		December 31, 2018
Trade receivables, which are included in accounts receivable	$	50,730	$	27,061
Contract assets, which are included in accounts receivable		3,491		3,128
Contract liabilities		–		857

Contract liabilities		Year ended December 31, 2019		Year ended December 31, 2018
Balance, beginning of year	$	857	$	1,491
Increases due to cash received		–		982
Revenue recognized during the year		(857)		(1,616)
Balance, end of year		–		857
Less current portion		–		(814)
	$	–	$	43

18. Other expenses:

		2019		2018
Loss on equity investment (note 9)	$	3,942	$	2,631
EBITDA support agreement income		(2,000)		(2,000)
Other expenses (income)		13		(167)
	$	1,955	$	464

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

18. Other expenses (continued):

EBITDA support agreement

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

19. Finance costs and finance income:

Finance costs		2019		2018
Foreign exchange loss	$	1,129	$	5,593
Interest		6,415		4,243
	$	7,544	$	9,836

Finance income		2019		2018
Foreign exchange gain	$	3,931	$	881
	$	3,931	$	881

20. Net income per share:

		2019		2018
Net income attributable to shareholders for basic and diluted net income per share	$	22,017	$	14,852
Weighted average number of shares (basic)		25,632,645		25,439,952
Weighted average impact of share options		252,705		247,397
Weighted average number of shares (diluted)		25,885,350		25,687,349
Net income per share (basic)	$	0.86	$	0.58
Net income per share (diluted)	$	0.86	$	0.58

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

21. Personnel expenses:

		2019		2018
Wages and salaries	$	116,277	$	100,622
Benefits and government payroll remittances		18,609		16,760
Profit share		2,838		2,010
Expenses related to defined contribution plans		755		517
Expenses related to defined benefit plans		5,721		5,932
	$	144,200	$	125,841

22. Supplementary cash flow information:

		2019		2018
Change in non-cash operating working capital:				
Accounts receivable	$	(21,573)	$	14,002
Inventories		756		(7,799)
Prepaid expenses and deposits		(607)		(509)
Income taxes		(742)		(531)
Accounts payable and accrued liabilities		464		(1,222)
Contract liabilities		(798)		56
	$	(22,500)	$	3,997

23. Related party transactions:

Pollard Equities Limited and affiliates

During the year ended December 31, 2019, Pollard paid property rent of $3,238 (2018 – $3,187) and $436 (2018 – $528) in plane charter costs to affiliates of Equities. In addition, during the year, Pollard paid Equities $nil (2018 – $421) interest on Pollard's subordinated debt.

During the year, Equities paid Pollard $72 (2018 – $72) for accounting and administration fees.

At December 31, 2019, included in accounts payable and accrued liabilities is an amount owing to Equities and its affiliates for rent, expenses and other items of $456 (2018 – $560). Included within property, plant and equipment and lease liabilities on the consolidated statement of financial position are right-of-use assets and corresponding liabilities for premises leased to Pollard from Equities. As at December 31, 2019, the net book value of the right-of-use assets was $10,803 and the present value of the lease liabilities was $11,787.

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

23. Related party transactions (continued):

Neogames S.à r.l. and affiliates

During the year ended December 31, 2019, Pollard reimbursed operating costs and paid software royalties of $5,728 (2018 – $3,321) to its iLottery partner, which are recorded in cost of sales.

At December 31, 2019, included in accounts payable and accrued liabilities is a net amount owing to Pollard's iLottery partner of $134 (2018 – $940) for reimbursement of operating costs and capital expenditures, and its share of operating profits.

At December 31, 2019, included in restricted cash and accounts payable and accrued liabilities is an amount owing to Pollard's iLottery partner of $2,600 (2018 - $1,566) for funds relating to contractual performance guarantees.

Key management personnel

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

Key management personnel compensation comprised:

		2019		2018
Wages, salaries and benefits	$	3,370	$	3,267
Profit share		15		20
Expenses related to defined benefit plans		614		619
	$	3,999	$	3,906

As at December 31, 2019, the Directors and Named Executive Officers of Pollard, as a group, beneficially owned or exercised control or direction over 17,439,058 common shares of Pollard.

24. Sales to major customers:

For the year ended December 31, 2019, sales to one customer amounted to 11.2 percent of consolidated sales and 10.1 percent to a second customer. In 2018, sales to one customer amounted to 12.7 percent of consolidated sales and 11.1 percent to a second customer.

25. Segmented information:

Pollard has two reportable segments: Lotteries and charitable gaming and Diamond Game, which are Pollard's strategic business units.

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

25. Segmented information (continued):

The strategic business units offer different products and services, and are managed separately. For each of the strategic business units, Pollard's Co–CEO's review internal management reports on a monthly basis.

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

	Year ended December 31, 2019		
	Lotteries and charitable gaming	Diamond Game	Total
Revenues from external customers	$ 371,926	$ 25,913	$ 397,839
Operating costs and expenses	345,929	22,909	368,838
Earnings before income taxes	25,997	3,004	29,001
Total assets	292,456	59,809	352,265

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

	December 31, 2019	December 31, 2018
Property, plant and equipment and goodwill:		
Canada	$ 76,774	$ 66,227
U.S.	81,663	75,046
U.K.	3,460	–
	$ 161,897	$ 141,273

26. Financial instruments:

The fair value of a financial instrument is the estimated amount that Pollard would receive or pay to terminate the instrument agreement at the reporting date.

26. Financial instruments (continued):

The following methods and assumptions were used to estimate the fair value of each type of financial instrument by reference to various market value data and other valuation techniques as appropriate.

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

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

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

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

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

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

Level 3 – valuation techniques with significant unobservable market inputs

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

As at December 31, 2019, the cash and restricted cash recorded at fair value was classified as level one of the fair value hierarchy.

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

27. Financial risk management:

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

Credit risk
Liquidity risk
Currency risk
Interest rate risk

Pollard's risk management policies are established to identify and analyze the risks, to set appropriate risk limits and controls and to monitor risks and adherence to limits. The Audit Committee oversees how management monitors compliance with Pollard's risk management policies and procedures.

The Audit Committee is assisted in its oversight role by Internal Audit, who undertakes regular reviews of risk management controls and utilizes the annual risk assessment process as the basis for the annual internal audit plan.

Credit risk

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

	December 31, 2019	December 31, 2018
Current	$ 50,093	$ 30,929
Past due for 1 to 60 days	2,708	2,647
Past due for more than 60 days	4,600	1,289
Less: Allowance for losses	(188)	(190)
	$ 57,213	$ 34,675

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

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

27. Financial risk management (continued):

Liquidity risk

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

The following table outlines Pollard's maturity analysis of the undiscounted cash flows, including related interest payments, of certain non-current financial liabilities and leases as of December 31, 2019:

		Total	2020	2021	2022	2023	2024
Long-term debt	$	146,060	5,386	6,427	134,247	–	–
Leases		18,052	5,473	4,474	4,021	3,147	937
	$	164,112	10,859	10,901	138,268	3,147	937

Pollard's approach is to ensure, as far as possible, that it will always have sufficient liquidity to meet its liabilities when due. The 2020 requirements for capital expenditures, working capital and dividends are expected to be financed from cash flow provided by operating activities and the unused portion of Pollard's credit facility. Pollard enters into contractual obligations in the normal course of business operations.

Currency risk

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

A 50 basis point strengthening/weakening in the foreign exchange rate between the Canadian and U.S. dollar would decrease/increase the income before income taxes by approximately $36 for year ended December 31, 2019 (2018 – $23). A 50 basis point strengthening/weakening in the foreign exchange rate between the Canadian dollar and Euro would decrease/increase the income before income taxes due to changes in operating cashflow by approximately $81 for year ended December 31, 2019 (2018 – $75).

In addition, translation differences arise when foreign currency monetary assets and liabilities are translated at foreign exchange rates that change over time. As at December 31, 2019, the amount of financial liabilities denominated in U.S. dollars exceeded the amount of financial assets denominated in U.S. dollars by approximately $27,949 (2018 – $36,147).

27. Financial risk management (continued):

A 50 basis point weakening/strengthening in the value of the Canadian dollar relative to the U.S. dollar would result in a decrease/increase in income before taxes of approximately $140 for the year ended December 31, 2019 (2018 – $181).

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

Pollard also uses financial hedges, including foreign currency contracts, to help manage foreign currency risk. At December 31, 2019, Pollard had no outstanding foreign currency contracts.

Interest rate risk

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

A 50 basis point decrease/increase in interest rates would result in an increase/decrease in income before income taxes of approximately $639 for the year ended December 31, 2019 (2018 – $581).

28. Subsequent event:

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 $13,416 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. The purchase price was funded by proceeds from Pollard's credit facility and cash on hand. The acquisition will be accounted for using the acquisition method. The allocation of the purchase price to the identifiable assets and liabilities has not yet been completed.

The Board of Directors of Pollard Banknote Limited

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

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

[2] Lead Director

Senior Management

John Pollard
CO-CHIEF EXECUTIVE OFFICER

Douglas Pollard
CO-CHIEF EXECUTIVE OFFICER

Paul Franzmann
EXECUTIVE VICE PRESIDENT, CORPORATE DEVELOPMENT

Pedro Melo
EXECUTIVE VICE PRESIDENT, INFORMATION TECHNOLOGY

Margaret Proven
EXECUTIVE VICE PRESIDENT, HUMAN RESOURCES

Riva Richard
GENERAL COUNSEL AND EXECUTIVE VICE PRESIDENT, LEGAL AFFAIRS

Robert Rose
EXECUTIVE VICE PRESIDENT, FINANCE AND CHIEF FINANCIAL OFFICER

Jennifer Westbury
EXECUTIVE VICE PRESIDENT, SALES AND CUSTOMER DEVELOPMENT

Robert Young
EXECUTIVE VICE PRESIDENT, OPERATIONS

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