



PINNACLE RENEWABLE HOLDINGS INC.

2017 ANNUAL REPORT



Our mission is to be the world's most reliable producer and supplier of bioenergy products

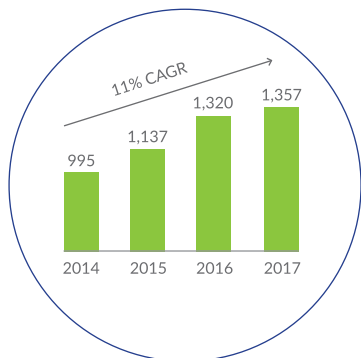
PROFILE

We are one of the world's leading manufacturers and distributors of industrial wood pellets, which are used by global utilities and large-scale power generators as fuel to produce renewable and reliable baseload power. We currently operate seven wood pellet production facilities, with an additional facility now under construction, throughout western Canada that process a wide range of wood fibre (primarily forest product residuals) sourced from forestry industry partners that harvest from sustainably certified forests. Our production facilities are all located on major rail lines allowing for efficient rail transport to one of two shipping terminals on the B.C. coast: our wholly-owned Westview terminal in Prince Rupert, and the Fibreco Terminal at the Port of Vancouver. We take pride in our industry leading health and safety practices.

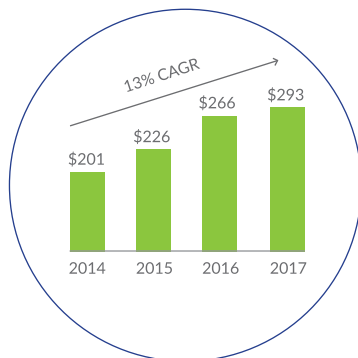


PERFORMANCE HIGHLIGHTS

PRODUCTION
(millions of MT per annum)



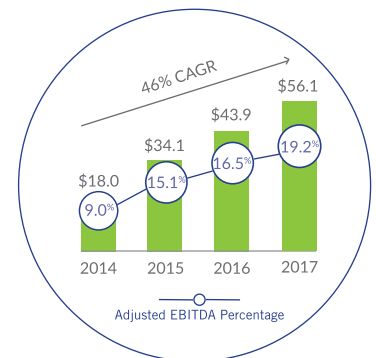
REVENUE
(\$ millions)



ADJUSTED GROSS MARGIN¹
(\$ millions)



ADJUSTED EBITDA¹
(\$ millions)



¹Adjusted Gross Margin and Adjusted EBITDA are Non-IFRS measures. Please refer to page 3 of our Management's Discussion & Analysis for further information.

To our shareholders,

We are pleased to present our fiscal 2017 Annual Report. We had a strong year on all of our key metrics in 2017, with our highest ever wood pellet production and shipment volumes, along with record annual revenue, Adjusted EBITDA and cash flows.

Since implementing our “Owning Safety” culture in fiscal 2014, we have improved our Medical Incident Rate by more than 90 percent from fiscal 2014 to 2017, which was our safest year ever. Our efficient, well-integrated network of production facilities combined with our consistent focus on best practices in production management enabled us to increase same-facility production by 18 percent from fiscal 2014 to fiscal 2017.

Our strong overall performance reflects the growing demand for industrial wood pellets from our customers in Europe, the United Kingdom and Asia, our reliable production capacity and focus on operational efficiencies, and the exceptional performance and commitment of our people.

During fiscal 2017, we entered into four major, long-term off-take contracts with customers. Two of the contracts are with Mitsubishi, whereby our pellets will be supplied to two separate end users in Japan. We also signed off-take contracts with Uniper Benelux NV and RWE Ag, two large utilities in Europe. We ended the year with a contracted backlog of approximately \$3 billion, up 15.4 percent from the end of fiscal 2016.

Our momentum has been building over the past several years, with consistent annual growth in production volumes, revenue and profitability. Our success positioned us to complete our initial public offering and secondary offering of common shares in February 2018. Pinnacle Renewable Holdings Inc. commenced trading on the Toronto Stock Exchange on February 6, 2018 under the symbol “PL”.

We have continued to build on our positive momentum to date in fiscal 2018. Our operations performed well during the first quarter, as we largely offset the impact of rail service disruptions. We generated revenue of \$71 million, an increase of 4.7 percent compared to the first quarter a year ago, reflecting an 8,000 metric ton increase in wood pellet sales volumes and a higher average sales price per metric ton.

As expected, we commenced initial production at our new, wholly-owned Entwistle facility during the first quarter and completed our first unit train shipment to our Westview port facility. We are currently near completion of the commissioning phase for Entwistle and then we’ll gradually ramp up production to reach our targeted annual run-rate of 400,000 metric tons in the second quarter next year. To date, Entwistle is on-time and on-budget. We also commenced construction of the new Smithers facility, which is owned 70 percent by Pinnacle. We expect initial production at Smithers in the fourth quarter this year. We’ll then gradually ramp up production to reach our targeted annual run-rate production of 125,000 metric tons in the third quarter next year. All of the production capacity of these new facilities has been contracted to customers under long-term, take-or-pay agreements and we have secured long-term, fibre supply agreements from our forestry industry partners for both facilities.

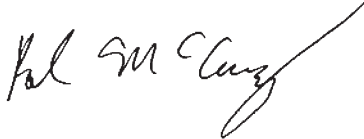
We are off to an excellent start this year with new off-take contracts with customers in Japan. To date in fiscal 2018, we have signed new long-term take-or-pay contracts with: Hanwa Co., Ltd., Sumitomo Corporation, Toyota Tsusho Corporation and Ube Industries Ltd. Similar to our contracts with Mitsubishi last year, each of these new contracts will result in our pellets being supplied to separate end users for renewable power generation. These four new supply agreements increase our current contracted backlog to \$3.8 billion and further diversify our customer base. The contracts commence in late fiscal 2019 through fiscal 2022 and will require us to add more production capacity to meet our growing customer backlog.

Once we have secured long-term, off-take agreements we advance projects in our development funnel for new production facilities. We intend to add production capacity through a combination of the following: increasing production capacity at our existing facilities, advancing the development of new production facilities in our funnel of new growth projects, and potential acquisitions of existing industrial wood pellet production

facilities. We look forward to providing more specific details on our near-term capacity expansion plan, following the completion of our active internal review process.

Our markets have an exceptional growth trajectory and we are well positioned to capitalize with our vertically-integrated platform in western Canada, attractive cost position, strong customer and supplier relationships, robust project development pipeline, a sound balance sheet and enhanced access to capital. Our mission is to be the world's most reliable producer and supplier of bioenergy products. On behalf of our Board and all the Pinnacle team members, we appreciate your support as we continue to advance our growth strategy and build value for our stakeholders.

Sincerely,

Handwritten signature of Robert McCurdy in black ink.

Robert McCurdy
Chief Executive Officer

Handwritten signature of Gregory Baylin in black ink.

Gregory Baylin
Chair of the Board



PINNACLE RENEWABLE HOLDINGS INC.

Management's Discussion & Analysis

Fiscal Year Ended December 29, 2017

March 15, 2018

GENERAL INFORMATION AND CAUTIONARY STATEMENTS

Introduction

The following management's discussion and analysis ("MD&A") dated March 15, 2018 provides information concerning the financial condition and results of operations of Pinnacle Renewable Holdings Inc. (collectively with its consolidated subsidiaries, the "Company", "Pinnacle", "we", "us" or "our"). This MD&A provides the reader with a view and analysis, from the perspective of management, of the Company's financial results for the fourth quarter and the fiscal year ended December 29, 2017. This MD&A should be read in conjunction with our audited consolidated financial statements for the year ended December 29, 2017 including the related notes thereto.

Basis of Presentation

Our audited annual consolidated financial statements and accompanying notes have been prepared in accordance with International Financial Reporting Standards ("IFRS"), as issued by the International Accounting Standards Board ("IASB"), using the accounting policies described therein. All amounts are presented in thousands of Canadian dollars unless otherwise indicated. We manage our business on the basis of one operating and reportable segment.

All references in this MD&A to "Fiscal 2014" are to our 52-week period ended December 26, 2014, references to "Fiscal 2015" are to our 52-week period ended December 25, 2015, references to "Fiscal 2016" are to our 53-week period ended December 30, 2016, references to "Fiscal 2017" are to our 52-week period ended December 29, 2017, references to "Fiscal 2018" are to our 52-week period ended December 28, 2018, and references to "Fiscal 2019" are to our 52-week period ended December 27, 2019. All references in this MD&A to "Q4 2017" are to our 13-week period ended December 29, 2017, and references to "Q4 2016" are to our 14-week period ended December 30, 2016. Our fiscal year is the 52 or 53-week period ending the last Friday of the calendar year. The last 53-week fiscal year occurred in Fiscal 2016.

The audited annual consolidated financial statements and accompanying notes for Fiscal 2017 and this MD&A were reviewed by our Audit Committee and approved by our Board of Directors on March 15, 2018.

Forward-Looking Information

This MD&A contains "forward-looking information" within the meaning of applicable securities laws in Canada. Forward-looking information may relate to our future financial outlook and anticipated events or results and may include information regarding our financial position, business strategy, growth strategies, budgets, operations, financial results, taxes, dividend policy, plans and objectives. Particularly, information regarding our expectations of future results, performance, achievements, prospects or opportunities or the markets in which we operate is forward-looking information. As the context requires, this may include certain targets as disclosed in the prospectus for our initial public offering, which are based on the factors and assumptions, and subject to the risks, as set out therein and herein. See also the "Outlook" section of this MD&A.

In some cases, forward-looking information can be identified by the use of forward-looking terminology such as "plans", "targets", "expects" or "does not expect", "is expected", "an opportunity exists", "budget", "scheduled", "estimates", "outlook", "forecasts", "projection", "prospects", "strategy", "intends", "anticipates", "does not anticipate", "believes", or variations of such words and phrases or state that certain actions, events or results "may", "could", "would", "might", "will", "will be taken", "occur" or "be achieved". In addition, any statements that refer to expectations, intentions, projections or other characterizations of future events or circumstances contain forward-looking information. Statements containing forward-looking information are not historical facts but instead represent management's expectations, estimates and projections regarding future events or circumstances. There can be no assurance that such information will prove to be accurate, as actual results and future events could differ materially from those anticipated in such information.

Many factors could cause our actual results, level of activity, performance or achievements or future events or developments to differ materially from those expressed or implied by the forward-looking statements, including, without limitation, the factors discussed in the "Financial Risk Factors" section of this MD&A and in the "Risk Factors" section

of our prospectus dated January 30, 2018 related to our initial public offering (the “Prospectus”). A copy of the Prospectus can be accessed under the Company’s profile on the System for Electronic Document Analysis and Retrieval (“SEDAR”) at www.sedar.com. The Company cautions that the list of risk factors and uncertainties described herein and in the Prospectus are not intended to represent a complete list of the factors that could affect us. Readers are urged to consider the risks, uncertainties and assumptions carefully in evaluating the forward-looking information and are cautioned to not to place undue reliance on such information.

The forward-looking information contained in this MD&A represents our expectations as of the date of this MD&A (or as the date they are otherwise stated to be made), and are subject to change after such date. However, we disclaim any intention or obligation or undertaking to update or revise any forward-looking information whether as a result of new information, future events or otherwise, except as required under applicable securities laws in Canada.

Non-IFRS Financial Measures

This MD&A makes reference to certain non-IFRS measures. These measures are not recognized measures under IFRS, and do not have a standardized meaning prescribed by IFRS and are therefore unlikely to be comparable to similar measures presented by other companies. Rather, these measures are provided as additional information to complement those IFRS measures by providing further understanding of our results of operations from management’s perspective. Accordingly, these measures should not be considered in isolation nor as a substitute for analysis of our financial information reported under IFRS. We use non-IFRS measures including “EBITDA”, “Adjusted EBITDA”, “Adjusted EBITDA per Metric Ton”, “Adjusted Gross Margin”, “Adjusted Gross Margin per Metric Ton”, “Adjusted Gross Margin Percentage”, and “Free Cash Flow”. These non-IFRS measures are used to provide investors with supplemental measures of our operating performance and thus highlight trends in our core business that may not otherwise be apparent when relying solely on IFRS measures. We also believe that securities analysts, investors and other interested parties frequently use non-IFRS measures in the evaluation of issuers. Our management also uses non-IFRS measures in order to facilitate operating performance comparisons from period to period, to prepare annual operating budgets and forecasts and to determine components of management compensation. As required by Canadian securities laws, we reconcile these non-IFRS measures to the most comparable IFRS measure in the MD&A. For definitions and reconciliations of these non-IFRS measures to the relevant reported measures, see “Key Performance Indicators” and “Selected Consolidated Financial Information”.

COMPANY OVERVIEW, STRATEGY AND OBJECTIVES

Company Overview

Pinnacle is a rapidly growing industrial wood pellet manufacturer and distributor and is the third largest wood pellet producer in the world. We produce renewable fuel for electricity generation in the form of industrial wood pellets, which are used by global utilities and large-scale power generators to produce renewable and reliable baseload power. We are a trusted supplier to our customers, who require reliable, high quality fuel supply to maximize utilization of their facilities. The industrial wood pellet industry is experiencing rapid growth driven by increased European and Asian demand for power sources that reduce carbon emissions in-line with regulatory objectives. Hawkins Wright, a leading, independent industry research body, forecasts that demand for industrial wood pellets will have a compound annual growth rate of 17.7% from 2016 through 2021.

As one of only three large global suppliers, we currently operate seven production facilities with a combined run-rate production capacity in excess of 1.8 million metric tons per annum (“MTPA”), and are well positioned to support growing demand through construction of new capacity. In March 2018, we commenced operations at the Entwistle Facility (as defined herein) (400,000 MTPA) with production from dry fibre, and have recently approved construction of the Smithers Facility (as defined herein) (125,000 MTPA) in partnership with West Fraser Timber Co. Ltd. (“West Fraser”). Our wholly-owned Entwistle Facility will be completing dryer commissioning and ramping up production during Fiscal 2018 and the Smithers Facility is expected to commence production in the fourth quarter of Fiscal 2018. We have entered into long-term take-or-pay contracts with our customers, whereby the buyer has a firm obligation to purchase a fixed quantity of product at specific prices that represent 100% of our production capacity through 2021 and nearly 80% of our production capacity through 2026, on an aggregated basis, including new production capacity from the

Entwistle and Smithers Facilities. As of December 29, 2017 our total Contracted Backlog (as defined herein) was \$3.0 billion.

Strategy and Objectives

Through increasing capacity at our existing production facilities, the construction of our new Entwistle Facility and the Smithers Facility, as well as the addition of other greenfield and brownfield projects, we believe we have an opportunity to grow our industrial wood pellet production proportionately with increasing global demand.

In addition to organic growth opportunities, we may consider acquisition opportunities or other strategic initiatives in Western Canada or in other jurisdictions, such as the U.S. Pacific Northwest, Eastern Canada and the U.S. Southeast, to further diversify our asset base, leverage our strong development and operational expertise and capture increased market share.

The industrial wood pellet market has undergone a significant evolution over the last decade with three large independent suppliers, including us, emerging as global leaders, each having over 1.0 million MTPA of industrial wood pellet production capacity. Pinnacle and these two other suppliers are expected to supply approximately 33% of total global potential demand for industrial wood pellets by 2019 (including under construction and financed projects). The remaining potential demand will be fulfilled by utilities that self-supply for a portion of their fuel supply needs or smaller, independent suppliers with less than 700,000 MTPA of industrial wood pellet production capacity. These smaller, independent suppliers tend to operate one or two production facilities and generally do not own or control their transportation infrastructure. This is generally viewed less favourably by large utilities seeking the certainty of supply in exchange for long-term contracts, which is enhanced by suppliers that have greater control over their logistics chain, diversity of supply, operational capabilities and financial resources. We believe smaller, independent suppliers represent potential acquisition opportunities.

RECENT DEVELOPMENTS

Initial Public Offering

On February 6, 2018, we completed an initial public offering (the “Offering”) of our common shares (the “Common Shares”). The Offering included a treasury offering by us and a secondary offering of Common Shares by certain of our shareholders (the “Selling Shareholders”), at a price of \$11.25 per Common Share. Pursuant to the Offering, we sold 6,223,889 Common Shares for total gross proceeds of approximately \$70 million and the Selling Shareholders sold 7,111,111 Common Shares for total gross proceeds of approximately \$80 million. The Common Shares are listed for trading on the Toronto Stock Exchange (“TSX”) under the symbol “PL”.

The underwriters were granted an over-allotment option (the “Over-Allotment Option”) to purchase up to an additional 2,000,250 Common Shares from certain Selling Shareholders at a price of \$11.25 per Common Share for additional gross proceeds of approximately \$22.5 million. The Over-Allotment Option was exercisable for a period of 30 days from the closing date of the Offering. On February 27, 2018, the underwriters exercised the Over-Allotment Option in full.

In connection with certain pre-closing capital changes effected immediately prior to closing of the Offering, ONCAP II L.P., ONCAP (US) II L.P., ONCAP (US) II-A L.P., ONEX Parallel Investment (ONCAP) L.P. and Biomass EI Ltd. (collectively, the “ONCAP Entities”) converted various shares and convertible debt instruments they held in us in accordance with their terms in exchange for 14,112,787 Common Shares in the aggregate. Subject to applicable laws and certain lock-up arrangements with the underwriters, the ONCAP Entities may purchase or sell Common Shares from time to time.

Market Update

- According to Hawkins Wright’s January 2018 Forest Energy Monitor, year-over-year demand growth for industrial wood pellets as at December 2017 was up 15% in Europe, 42% in South Korea and 54% in Japan.

- The European Parliament, the directly elected parliamentary institution of the European Union (“EU”), voted to accept the Renewable Energy Directive which calls for a renewable energy target of 35% for EU member countries. We expect this will provide further impetus for growth in biomass-based fuel sources within the European power generating portfolio.
- Drax, one of the United Kingdom’s largest power utilities, received subsidy support for its fourth generating unit at the Drax Power Station in the U.K. The effect of the subsidy support is expected to impact this generating unit in 2018/2019, allowing Drax to utilize wood pellets more continuously and at a slightly elevated overall level.
- The Engie plant at Rodenhuize, Belgium has re-started in the first quarter of 2018, off-setting the effect of the delayed start of the Lynemouth power station in the U.K.
- We are currently negotiating with various counterparties to secure long-term take-or-pay contracts in Asia to meet growing demand.

New and Extended Off-take Agreements

During Fiscal 2017, we entered into the following off-take contracts:

- a contract with Mitsubishi Corp. (“Mitsubishi”) to supply 80,000 MTPA of industrial wood pellets to Nippon Paper Ishinomaki Energy Center Ltd., commencing in Fiscal 2018;
- a contract with Uniper Benelux NV to supply 100,000 MTPA of industrial wood pellets commencing in Fiscal 2019;
- a renewal contract with RWE Ag (“RWE”) for annual volumes commencing in 2019 at 120,000 MTPA (as it overlaps with the previous contract with RWE) and increasing over the term of the renewal contract to 480,000 MTPA of industrial wood pellets; and,
- a contract with Mitsubishi to supply 100,000 MTPA of industrial wood pellets to Orix Corporation, commencing in Fiscal 2018, as we continued to advance our sales strategy for growth in the Japanese market.

Our first delivery under an off-take contract signed in Fiscal 2016 with Lynemouth Power Limited (“Lynemouth”) was completed in June 2017. In 2016, Lynemouth began to convert its coal-fired power station in the U.K. to consume industrial wood pellets instead of coal. Our total deliveries of industrial wood pellets to Lynemouth will increase to a full supply of 400,000 MTPA in 2018. The new and renewed contracts are denominated in Canadian Dollars.

New Production Facilities

Entwistle

The Entwistle production facility (the “Entwistle Facility”) is owned 100% by us. The Entwistle Facility is located in Entwistle, Alberta, 95 kilometres west of Edmonton, in close proximity to abundant wood fibre sources, including several major sawmills. The Entwistle Facility commenced initial operations in March 2018 with production from dry fibre. We will complete the construction of the Entwistle Facility in the second quarter of Fiscal 2018, and continue commissioning the facility to utilize a broader range of fibre sources, including shavings, sawdust, bush grind, chips and hog fuel. We will gradually ramp-up the Entwistle Facility to ensure all machine centres are performing optimally and expect to achieve full run-rate production of 400,000 MTPA in the second quarter of Fiscal 2019.

Smithers

The Smithers production facility (the “Smithers Facility”) is owned 70% by us and 30% by West Fraser through a partnership, Smithers Pellet Limited Partnership (“SPLP”), and is located in Smithers, British Columbia (“B.C.”). In the third quarter of Fiscal 2017, we executed agreements with West Fraser relating to various marketing and operating services for the Smithers Facility. In the fourth quarter of 2017, Pinnacle and West Fraser completed the acquisition of the assets of Northern Engineered Wood Products, historically a manufacturer of particle board, for the redevelopment of the Smithers Facility. On February 22, 2018, our Board of Directors and the SPLP board of directors approved the construction of the Smithers Facility.

We have executed long-term agreements with wood fibre suppliers and have initiated engineering activities for the Smithers Facility. The capital cost of the project is anticipated to be \$30 to \$33 million (70% will be attributable to us), which includes the acquisition of the land and operating infrastructure for \$8.4 million. Approximately 79% of capital costs are fixed.

We expect initial pellet production at the Smithers Facility to commence in the fourth quarter of Fiscal 2018. The delay in production commencement from our previous estimate of the third quarter of Fiscal 2018 is due to higher than anticipated snowfall in the recent winter months. At this time, we do not believe this delay will have a material impact on our results. Following commissioning, our management team expects to gradually ramp up the Smithers Facility to ensure all machine centres are performing optimally. Full run-rate production of 125,000 MTPA is anticipated in the third quarter of Fiscal 2019.

Amendment to credit facility

In Q4 2017, we amended our senior secured debt, which consists of an existing term loan, a delayed draw term loan and revolving operating line, to provide additional capacity to fund new growth projects. The amended facility provides up to a \$50 million revolving operating line, a \$200 million term loan and a \$130 million delayed draw term loan. This amended facility has a maturity date of December 13, 2022. Refer to “Senior Credit Facilities” sub-section under “Liquidity and Capital Resources” of this MD&A for discussion of terms.

FINANCIAL HIGHLIGHTS

We refer the reader to the section entitled “Key Performance Indicators” of this MD&A for the definition of the items discussed below and, when applicable, to the section entitled “Selected Consolidated Financial Information” for reconciliations of non-IFRS measures with the most directly comparable IFRS measure.

As noted above under the section entitled “Basis of Presentation”, we highlight to the reader that “Q4 2017” refers to our 13-week period ended December 29, 2017, “Q4 2016” refers to our 14-week period ended December 30, 2016, “Fiscal 2017” refers to our 52-week period ended December 29, 2017, and “Fiscal 2016” refers to our 53-week period ended December 30, 2016. Differences in the duration of our fiscal periods may affect the comparability of our financial results.

Select financial highlights include the following:

| <i>(In millions of Canadian dollars, except Adjusted Gross Margin Percentage)</i> | Q4 2017 | Q4 2016 | Fiscal 2017 | Fiscal 2016 |
|---|----------------|----------------|--------------------|--------------------|
| Revenue | \$73.0 | \$70.9 | \$292.7 | \$266.3 |
| Production costs | \$47.4 | \$46.3 | \$188.4 | \$173.7 |
| Distribution costs | \$9.9 | \$11.1 | \$38.4 | \$39.5 |
| Selling, general and administration expenses | \$4.3 | \$4.1 | \$15.3 | \$12.3 |
| Net profit (loss) and comprehensive income (loss) | \$0.1 | \$2.6 | \$(4.9) | \$5.3 |
| Adjusted Gross Margin | \$15.9 | \$13.5 | \$66.9 | \$53.1 |
| Adjusted Gross Margin Percentage | 21.8% | 19.1% | 22.9% | 19.9% |
| Adjusted EBITDA | \$12.8 | \$11.0 | \$56.1 | \$43.9 |

- Contracted Backlog increased 15.4% to \$3.0 billion at the end of Fiscal 2017 from \$2.6 billion at the end of Fiscal 2016; and

- Free Cash Flow increased 69.3% to \$38.2 million in Fiscal 2017 from \$22.6 million in Fiscal 2016.

SUMMARY OF FACTORS AFFECTING PERFORMANCE

We believe that our performance and future success depends on a number of factors that present significant opportunities. These factors are also subject to a number of inherent risks and challenges, some of which are discussed below. See also the “Financial Risk Factors” section of this MD&A and the risk factors identified in the Prospectus.

Growing Global End Market

Our growth is supported by the increasing global demand for industrial wood pellets resulting from the shift toward renewable, cleaner power generation. This demand is largely driven by the introduction of regulatory frameworks that set targets and create financial incentives for the reduction of global greenhouse gas emissions. The increasing number of power generation plants compatible with industrial wood pellets in jurisdictions with favourable regulatory frameworks could provide stronger revenue growth if we are able to expand our industrial wood pellet production capacity accordingly. Adoption by additional markets of regulatory frameworks and incentive structures in countries that burn significant amounts of coal, such as the U.S. and China, could also significantly increase our revenue growth potential.

We have long-term sales contracts with utilities and large power generators in the U.K., Europe and Asia. The U.K. uses a number of regulatory reforms, including a carbon tax, to encourage development of low-carbon alternatives, which includes biomass. We expect significant future revenue growth and geographic and customer diversification from the developing Japanese market. Japan supports investment in renewables through a feed-in-tariff system which offers twenty-year support for renewable energy power facilities. We are well-positioned geographically to participate in the growth of this developing market from our location in Western Canada. Changes in governments may result in modifications to these laws and regulatory environments that support the growth of our business. To address this risk, we continue to develop relationships with new customers in diverse regions.

Revenues and Costs for Deliveries to Customers

We enter into long-term take-or-pay off-take contracts with reliable counterparties, matching shipping requirements with new production availability. We have 100% of our production capacity contracted through 2021, and nearly 80% of our production capacity contracted through 2026, on an aggregated basis, including production capacity of the Entwistle Facility and the Smithers Facility. Strong demand for industrial wood pellets enables us to obtain price escalation in contracts that should mitigate any increased cost of production and distribution. Revenues and costs for deliveries to customers can vary significantly between periods depending upon the type of contract and timing of shipments. Depending on the specific off-take contract, shipping terms are either Free on Board (“FOB”), whereby the buyer assumes responsibility for the goods as soon as they are shipped, or Cost, Insurance, Freight (“CIF”), whereby the seller assumes responsibility for the goods until the goods are received by the buyer (typically at the receiving port). Under an FOB contract, the customer is responsible for paying all shipping costs directly, so our revenue is not impacted by shipping costs. Under a CIF contract, we procure and pay for shipping costs which include insurance and all other charges up to the port of destination for the customer. These costs are included in the price charged to the customer and as such, are included in revenue and cost of distribution. As well, revenue is impacted by the timing of shipments which can result in material fluctuations in our revenue between periods.

New Development Projects

We have established a well-defined development blueprint for developing, constructing and operating new production facilities and expanding/converting existing production facilities (the “Development Blueprint”), which has led to a strong track record of successful project development. We target the development of new industrial wood pellet production capacity at a capital cost of approximately 4.0x to 5.5x run-rate EBITDA (i.e., the incremental annual earnings, before depreciation and amortization, finance expense and provision for income taxes, we expect to generate from the project). We have been one of the most active developers of industrial wood pellet production capacity and associated infrastructure in recent years which has helped to establish us as one of the leading global suppliers of industrial wood pellets.

Following our Development Blueprint, once we have new committed sales contracts, we construct and commission new production facilities. Our most recently completed greenfield project, the Lavington production facility (the “Lavington Facility”), was constructed on time, under budget and is currently producing volumes in excess of original expectations. We are leveraging our experience from the construction of the Lavington Facility and are currently constructing the Entwistle Facility and developing the Smithers Facility in accordance with our Development Blueprint.

Production

Our efficient, well-integrated network of production facilities and advanced production management practices allow us to ensure reliable production. We continue to increase our efficiency, as illustrated by same-facility production (excluding the Lavington Facility) increases of 18% from Fiscal 2014 compared to Fiscal 2017. The following factors influence our production:

- **Fibre Availability:** Our operating flexibility across our network of mills to process a broad range of forest residuals from logs, bush grind, bark, sawdust, shavings, and chips, enables us to optimize wood fibre supply among multiple locations for efficient processing;
- **Seasonality:** Extreme cold weather can impact equipment performance at our production facilities. Extremely wet weather and high moisture content in wood fibre can slow production and increase wood fibre drying costs. Extreme, prolonged dry weather conditions can lead to fire risk and the potential disruption of wood fibre supply when loggers cannot enter the forests to supply the production facilities. Our extensive long-term contractual relationships with some of the top forest companies in Canada allow us to offset wood fibre shortfalls in these situations. We also manage our inventory levels of logs to mitigate potential production disruptions;
- **Downtime:** The “safety first” culture established by management provides high engagement and reduces downtime related to medical incidents and labour challenges; and
- **Capacity Utilization:** We utilize real-time information gathering to monitor equipment performance and utilize preventative maintenance programs with regularly scheduled production shutdowns to optimize equipment uptime and production throughput. We operate to stringent environmental standards and use specialized equipment and processes to remove particles from production emissions. Real time monitoring of production facility information affords us the opportunity to respond quickly to production disruptions for any reason.

Wood Fibre and Forest Residuals

We are located in a region with a high volume of available, competitively priced and sustainably managed wood fibre ideal for the production of high calorific value industrial wood pellets. We have been successful in extending the terms of wood fibre agreements to support our existing and new production for up to 10 to 15-year terms. We have also expanded the types of wood fibre used in our production facilities and partnered with three of our largest wood fibre suppliers in the ownership of existing and in development production facilities. These partnerships help ensure that our wood fibre suppliers have a vested interest in the economic success of our production facilities. Our wood fibre demand is symbiotic with, rather than in competition with, demand for high-grade wood for use by other forest product industries, such as lumber production. The use of un-merchantable logs, bark and other by-product for industrial wood pellet production indirectly supports other forest-related industries as well as the sustainable management of commercial forests.

Our ability to produce industrial wood pellets is dependent on the availability and cost of wood fibre available within an economic radius of our plants.

Trucking, Rail and Port Logistics

Our production facilities are strategically located in highly concentrated sawmill regions, adjacent to rail lines and on back-haul routes in key wood fibre regions, enabling efficient, cost-effective transportation of industrial wood pellets and providing access to wood fibre supply. If there are rail line or trucking disruptions, mitigating strategies can be deployed. Industrial wood pellets from our production facilities are efficiently transported to the Westview Terminal (as defined herein) at the Port of Prince Rupert in Northern B.C. or the Fibreco Export Inc. terminal at the Port of Vancouver. The availability of alternative ports for shipping helps mitigate our risk. The weather sensitivity of our cargo and occasional port congestion of ships and rail cars can delay our shipment and increase demurrage costs. Conservative

shipping scheduling provides the opportunity for pulling shipments forward and reducing costs when the weather is favourable.

Sustainability

In order to be eligible for financial incentives and subsidies that encourage the use of renewable energy, our customers, major utilities and power generators must comply with sustainability requirements which require that industrial wood pellets be sourced from forest lands that are managed in a manner which is demonstrably sustainable. To meet these sustainability requirements, we must ensure that the procurement of fibre, conversion to wood pellets and delivery to the point of consumption comply with certain carbon intensity targets. Forest practices in our areas of operation, our logistics network, our proximity to Asian markets, and our efficient use of large vessels for longer haul shipping to Europe allow us to meet sustainability requirements and obtain the required certifications.

KEY PERFORMANCE INDICATORS

The measures below are used by management as key performance indicators for our business. Certain measures used by management are not recognized under IFRS. See “Non-IFRS Measures”.

IFRS Measures

Revenue

We primarily earn revenue by supplying industrial wood pellets to our customers under long-term off-take contracts. We refer to the structure of our contracts as “take-or-pay” because they include a firm obligation to take a fixed quantity of product at a stated price and contain provisions that ensure we will be compensated in the case of a customer’s failure to accept all or a part of the contracted volumes or for termination by a customer. Each contract defines the annual volume of industrial wood pellets that a customer is required to purchase and we are required to sell, the fixed price per metric ton (“MT”) for product satisfying a base net calorific value and other technical specifications. These prices are escalated at annual inflation-based adjustments or price escalators.

In addition to our sales of industrial wood pellets under these long-term, take-or-pay contracts, we occasionally sell small quantities of industrial wood pellets under short-term contracts which range in volume and tenor and, in some cases, may be limited to only one shipment. Because each of our contracts is a bilaterally negotiated agreement, the pricing is fixed and does not follow short-term contract market pricing trends. As a result, our revenue is predetermined over the duration of these contracts which ensures a high level of visibility for future revenue. Revenue from the sale of industrial wood pellets is recognized when the risks and rewards of ownership are transferred, there is no continuing managerial involvement to the degree associated with ownership, the amount of revenue can be measured reliably, it is probable the economic benefits will flow to the entity and costs incurred or to be incurred can be measured reliably.

The timing and size of shipments during a month or quarter can result in material fluctuations in our revenue recognition and related profitability between periods.

The vast majority of the industrial wood pellets we supply to our customers are produced at our production facilities. We also fulfill our contractual commitments and take advantage of dislocations in market supply and demand by purchasing from and selling to third-party market participants. In these back-to-back transactions where the risks and rewards of ownership are not immediately transferred to the ultimate purchaser, revenue is recorded only when the industrial wood pellets are delivered to the final customer.

Contracted Backlog

Contracted Backlog represents the revenue to be recognized under existing contracts, assuming deliveries occur as specified in the contracts.

Costs of Production and Distribution

The principal expenses to produce and deliver our industrial wood pellets consist of production and distribution costs.

We have strategically located our production facilities in B.C. and Alberta regions with high quality wood fibre sources. We supply the majority of wood fibre in our production facilities primarily through long-term contracts. Delivered wood fibre costs include the cost of both procuring the fibre and trucking the fibre from the source to our production facilities.

Production costs at our production facilities consist of not only the costs of wood fibre but all the costs of production and maintenance labour and benefits, repairs and maintenance, utilities, plant overhead (property taxes, insurance, facility management), rail transportation and other direct costs. In addition to the industrial wood pellets that we produce at our owned and operated production facilities, we selectively purchase additional quantities of industrial wood pellets from third-party wood pellet producers, most significantly from the Houston production facility (the “Houston Facility”), our minority-owned business held in a partnership, Houston Pellet Limited Partnership (“HPLP”), with Canfor Corporation (“Canfor”) and the Moricetown Band Development Corporation (the “Moricetown Band”). Our current purchase agreement with HPLP expires on December 31, 2018.

Distribution costs include costs incurred at our wholly-owned Westview Terminal (the “Westview Terminal”) and costs paid to Fibreco Export Inc., a third-party terminal operator in Vancouver, Canada. These costs include storage or handling costs while the product remains at port and shipping costs related to the delivery of our product from the ports to our customers. Both the strategic location of our production facilities and our ownership of the Westview Terminal has allowed for the efficient and cost-effective transportation of our industrial wood pellets.

Production costs associated with delivering our industrial wood pellets to our ports, third-party industrial wood pellet purchase costs and depreciation related to assets and intangibles related to the production process are included as a component of inventory. These costs are expensed when inventory is sold. Distribution costs are expensed as incurred.

Gross Margin

Gross Margin is our Revenue less Costs of Production and Distribution.

Selling, General and Administration

We incur selling, general and administrative (“SG&A”) expenses related to our executive, central operations, finance, business and growth development and sales and marketing departments. These costs include salaries and benefits, professional fees and other administrative expenses not directly related to any one particular production facility or the Westview Terminal, including the costs of our internal development team.

Equity Earnings in HPLP

With the exception of a small portion of sales made directly to Kansai Electric Power Co., Inc. (approximately 40,000 MTPA), industrial wood pellets produced at the Houston Facility are sold to our customers. Our investment in the Houston Facility is accounted for on an equity basis as we own 30% of HPLP. The remainder of the investment is held by Canfor and the Moricetown Band.

Non-controlling interests

The Lavington Facility is operated through Lavington Pellet Limited Partnership (“LPLP”), 75% owned by us with the remaining 25% interest held by Tolko Industries (“Tolko”). Our consolidated results include 100% of the results of the Lavington Facility with the 25% interest owned by Tolko disclosed as non-controlling interests. We have an agreement to purchase pellets from LPLP and sell to end customers through Pinnacle until October 2022.

Non-IFRS Measures

Adjusted Gross Margin Percentage

“Adjusted Gross Margin” is defined as gross margin excluding gains and losses on asset disposals and amortization of equipment and intangible assets included in cost of goods sold.

“Adjusted Gross Margin Percentage” is defined as Adjusted Gross Margin as a percentage of revenue.

We use Adjusted Gross Margin Percentage to measure our financial performance. We believe Adjusted Gross Margin Percentage is a meaningful measure because it compares our revenue generating activities to our operating costs for a view of profitability and performance. By calculating Adjusted Gross Margin Percentage we can show the performance trends over time as our sales mix changes. Adjusted Gross Margin Percentage will primarily be affected by our ability to meet targeted production volumes and to control direct and indirect costs associated with procurement and delivery of wood fibre to our production facilities and the production and distribution of industrial wood pellets. Adjusted Gross Margin Percentage as we calculate it may not be comparable to metrics provided by other businesses.

Adjusted EBITDA

“EBITDA” is defined as consolidated net income (loss) before depreciation and amortization, finance expense and provision for income taxes.

“Adjusted EBITDA” is defined as EBITDA excluding non-cash stock compensation expense, asset impairments and disposals, and certain items of income or loss that we characterize as unrepresentative of our ongoing operations. Adjusted EBITDA includes an amount representing our 30% share of HPLP and excludes the non-controlling interests share of LPLP.

We use Adjusted EBITDA to measure our financial performance. Adjusted EBITDA is a supplemental measure used by management and other users of our financial statements including shareholders and lenders, to assess the financial performance of our business without regard to financing methods or capital structure.

We believe Adjusted EBITDA is a useful measure of operating performance as it provides a more relevant picture of operating results by excluding the effects of financing and investing activities which removes the effects of interest, depreciation and amortization costs, expenses that are not reflective of our underlying business performance, and other one-time or non-recurring expenses. We use Adjusted EBITDA to facilitate a comparison of our operating performance on a consistent basis and to provide for a more complete understanding of factors and trends affecting our business.

Free Cash Flow

“Free Cash Flow” is defined as Adjusted EBITDA less maintenance capital expenditures, finance costs, principal repayments and cash taxes paid.

We use Free Cash Flow as a performance metric to compare the cash generating performance of the business from period to period and to compare the cash generating performance for specific periods to the cash distributions (if any) that are expected to be paid to our shareholders. We do not rely on Free Cash Flow as a liquidity measure.

As we intend to distribute dividends on an ongoing basis, and since Adjusted EBITDA is a metric used by many investors and financial analysts to compare issuers on the basis of the ability to generate cash from operations, we believe that, in addition to net cash provided by operations, Adjusted EBITDA is a useful non-IFRS, supplemental measure from which to make adjustments to determine Free Cash Flow. We believe Adjusted EBITDA provides a more relevant picture of operating results in that it excludes the effects of financing and investing activities by removing the effects of interest, depreciation and amortization costs, expenses that are not reflective of underlying business performance, and other one-time or non-recurring income or expenses. However, there are no standard definitions of Adjusted EBITDA or Free Cash Flow prescribed by IFRS and other issuers may calculate similarly described measures differently.

Please note that we have amended our determination of Free Cash Flow from that as disclosed in the Prospectus to exclude an adjustment from Adjusted EBITDA to Free Cash Flow for our distribution to non-controlling interests.

SELECTED CONSOLIDATED FINANCIAL INFORMATION

The following table sets forth selected historical financial information for Q4 2017, Q4 2016, Fiscal 2017, Fiscal 2016, and Fiscal 2015. Such information has been derived from our audited consolidated financial statements and related notes, in each case prepared in accordance with IFRS. The selected consolidated financial information set out below for Q4 2017 and Q4 2016 is unaudited.

| | <u>Q4 2017</u> <u>13 weeks</u> | <u>Q4 2016</u> <u>14 weeks</u> | <u>Fiscal</u> <u>2017</u> <u>52 weeks</u> | <u>Fiscal</u> <u>2016</u> <u>53 weeks</u> | <u>Fiscal</u> <u>2015</u> <u>52 weeks</u> |
|---|-----------------------------------|-----------------------------------|---|---|---|
| (In thousands of Canadian dollars, except per share amounts) | | | | | |
| <u>Consolidated Statements of Operations Data</u> | | | | | |
| Revenue..... | 72,958 | 70,935 | 292,727 | 266,338 | 225,591 |
| Costs and expenses: | | | | | |
| Production..... | 47,377 | 46,278 | 188,414 | 173,693 | 140,327 |
| Distribution..... | 9,925 | 11,079 | 38,421 | 39,474 | 42,053 |
| Selling, general and administration..... | 4,347 | 4,116 | 15,268 | 12,331 | 10,419 |
| Amortization of equipment and intangible assets..... | 5,280 | 5,557 | 21,819 | 21,211 | 17,605 |
| Profit (loss) before finance costs and other (income) expense..... | 6,029 | 3,905 | 28,805 | 19,629 | 15,187 |
| Finance cost (income)..... | 6,120 | (15,004) | 24,251 | 1,000 | 22,366 |
| Other (income) expense..... | (358) | 11,595 | 8,912 | 7,796 | (4,189) |
| Net profit (loss) before income taxes..... | 267 | 7,314 | (4,358) | 10,833 | (2,990) |
| Income tax (expense) recovery: | | | | | |
| Current..... | - | (12) | - | (2) | 1 |
| Deferred..... | (163) | (4,716) | (526) | (5,569) | 1,097 |
| Net profit (loss) and comprehensive income (loss)..... | 104 | 2,586 | (4,884) | 5,262 | (1,892) |
| Net profit (loss) per share attributable to owners | | | | | |
| Basic and diluted – Class A..... | \$(0.01) | \$0.07 | \$0.22 | \$0.11 | \$(0.11) |
| Basic and diluted – Class B..... | \$(0.01) | \$0.07 | \$0.22 | \$0.11 | \$(0.11) |

Statement of Cash Flows Data

| | | | | | |
|---|----------|----------|----------|----------|----------|
| Cash provided by (used in) | | | | | |
| Operating activities before net change in non-cash operating working capital..... | | | | | |
| operating working capital..... | 11,305 | 8,457 | 51,128 | 44,742 | 35,343 |
| Net change in non-cash operating working capital..... | (15,302) | (1,543) | (20,183) | (14,126) | (8,124) |
| Financing activities..... | 41,165 | (10,212) | 48,812 | (20,958) | 25,771 |
| Investing activities..... | (29,786) | (3,812) | (72,682) | (13,250) | (45,640) |
| Foreign exchange gain (loss) on cash position held in foreign currency..... | (69) | 63 | (279) | 68 | 334 |

| | <u>Q4 2017</u> <u>13 weeks</u> | <u>Q4 2016</u> <u>14 weeks</u> | <u>Fiscal</u> <u>2017</u> <u>52 weeks</u> | <u>Fiscal</u> <u>2016</u> <u>53 weeks</u> | <u>Fiscal</u> <u>2015</u> <u>52 weeks</u> |
|---|-----------------------------------|-----------------------------------|---|---|---|
| (In thousands of Canadian dollars, except Adjusted Gross Margin Percentage and metric tons) | | | | | |
| <u>Other Financial Data</u> | | | | | |
| Adjusted EBITDA ⁽¹⁾ | 12,775 | 10,970 | 56,121 | 43,922 | 34,109 |
| Adjusted EBITDA per Metric Ton ⁽¹⁾ | 38.25 | 32.75 | 40.87 | 33.68 | 32.39 |
| Adjusted Gross Margin per Metric Ton ⁽¹⁾ | 47.70 | 40.43 | 48.74 | 40.72 | 42.50 |
| Adjusted Gross Margin Percentage ⁽¹⁾ | 21.8% | 19.1% | 22.9% | 19.9% | 19.9% |
| Maintenance capital expenditures..... | 5,444 | 1,454 | 9,040 | 4,434 | 4,357 |
| Growth capital expenditures..... | 23,691 | 2,358 | 63,016 | 8,916 | 41,551 |
| <u>Operating Data</u> | | | | | |
| Metric tons of industrial wood pellets sold (000s)..... | 334 | 335 | 1,373 | 1,304 | 1,054 |

| | As at Dec 29, 2017 | As at Dec 30, 2016 | As at Dec 25, 2015 |
|--|------------------------------------|-----------------------|-----------------------|
| | (In thousands of Canadian dollars) | | |
| Selected Consolidated Statement Financial Position Data | | | |
| Cash | 18,908 | 12,112 | 15,636 |
| Property, plant and equipment | 238,196 | 175,849 | 187,262 |
| Total assets | 433,645 | 353,511 | 342,697 |
| Term debt and shareholders' debentures (including current portion) | 285,694 | 234,142 | 259,369 |
| Total non-current liabilities | 318,811 | 263,600 | 266,964 |
| Total equity | 35,204 | 37,951 | 33,995 |

Notes:

(1) See "Non-IFRS Measures".

The following table reconciles EBITDA, Adjusted EBITDA and Adjusted EBITDA per Metric Ton to the most directly comparable IFRS financial performance measure:

| | Q4 2017 13 weeks | Q4 2016 14 weeks | Fiscal 2017 52 weeks | Fiscal 2016 53 weeks | Fiscal 2015 52 weeks |
|--|---|---------------------|-------------------------|-------------------------|-------------------------|
| | (In thousands of Canadian dollars, except per Metric Ton amounts) | | | | |
| Net profit (loss) and comprehensive income | | | | | |
| (loss) | 104 | 2,586 | (4,884) | 5,262 | (1,892) |
| Income tax expense (recovery) | 163 | 4,728 | 526 | 5,571 | (1,098) |
| Finance costs excluding shareholders' debentures ⁽¹⁾ | 2,667 | 2,959 | 11,592 | 9,618 | 9,248 |
| Finance costs (income) on shareholders' debentures .. | 3,241 | (17,833) | 12,359 | (8,244) | 11,368 |
| Amortization of equipment and intangible assets ⁽²⁾ | 5,089 | 5,365 | 21,395 | 21,031 | 17,806 |
| EBITDA ⁽⁴⁾ | 11,264 | (2,195) | 40,988 | 33,238 | 35,432 |
| Stock-based compensation expense | 172 | 91 | 237 | 138 | 558 |
| Pinnacle's share of HPLP legal settlement | — | — | — | (4,875) | — |
| Loss on disposal of property, plant and equipment ⁽²⁾ | 478 | 1,687 | 1,049 | 2,353 | 383 |
| Plant curtailment costs ⁽³⁾ | 53 | 687 | 4,626 | 1,591 | — |
| Revaluation (gain) loss on class B and D common shares | (424) | 10,278 | 5,601 | 10,278 | (2,520) |
| Other non-operational adjustments | 1,232 | 422 | 3,620 | 1,199 | 256 |
| Adjusted EBITDA ⁽⁴⁾ | 12,775 | 10,970 | 56,121 | 43,922 | 34,109 |
| Metric tons of industrial wood pellets sold (000s) .. | 334 | 335 | 1,373 | 1,304 | 1,054 |
| Adjusted EBITDA per Metric Ton ⁽⁴⁾ | \$38.25 | \$32.75 | \$40.87 | \$33.68 | \$32.36 |

Notes:

- (1) Finance cost excluding shareholder debentures excludes realized (gain) loss on derivatives and foreign exchange.
(2) Amortization and loss on disposal of property, plant and equipment includes our share of HPLP and excludes the non-controlling interests share of LPLP.
(3) Costs related to the impairment and curtailment of the Quesnel facility, which is being permanently closed.
(4) See “Non-IFRS Measures”.

The following table reconciles Adjusted Gross Margin and Adjusted Gross Margin per Metric Ton to the most directly comparable IFRS financial performance measure:

| | Q4 2017 13 weeks | Q4 2016 14 weeks | Fiscal 2017 52 weeks | Fiscal 2016 53 weeks | Fiscal 2015 52 weeks |
|--|---------------------|---------------------|----------------------------|----------------------------|----------------------------|
| (In thousands of Canadian dollars, except per Metric Ton amounts and Adjusted Gross Margin Percentage) | | | | | |
| Profit (loss) before finance costs and other (income) expense | 6,029 | 3,905 | 28,805 | 19,629 | 15,187 |
| Selling, general and administration..... | 4,347 | 4,116 | 15,268 | 12,331 | 10,419 |
| Amortization | 5,280 | 5,557 | 21,819 | 21,211 | 17,605 |
| Gross Margin | 15,656 | 13,578 | 65,892 | 53,171 | 43,211 |
| Gross Margin Percentage | 21.5% | 19.1% | 22.5% | 20.0% | 19.2% |
| Equity earnings in HPLP..... | 255 | 172 | 1,381 | 5,675 | 1,510 |
| Pinnacle’s share of income in HPLP legal settlement..... | — | — | — | (4,875) | — |
| Non-controlling interests..... | 20 | (207) | (353) | (866) | 77 |
| Adjusted Gross Margin⁽¹⁾ | 15,931 | 13,543 | 66,920 | 53,105 | 44,798 |
| Metric tons of industrial wood pellets sold (000s)..... | 334 | 335 | 1,373 | 1,304 | 1,054 |
| Adjusted Gross Margin per Metric Ton⁽¹⁾ | \$47.70 | \$40.43 | \$48.74 | \$40.72 | \$42.50 |
| Adjusted Gross Margin Percentage⁽¹⁾ | 21.8% | 19.1% | 22.9% | 19.9% | 19.9% |

Notes:

- (1) See “Non-IFRS Measures”.

CONTRACTED BACKLOG

We enter into long-term, take-or-pay off-take contracts with large and well capitalized counterparties including power generators such as Drax, RWE and Mitsubishi, or their affiliates. As of December 29, 2017, we had approximately \$3.0 billion of product sales in Contracted Backlog.

“Contracted Backlog” represents the revenue to be recognized under existing contracts assuming deliveries occur as specified in the contracts. As a result of customer preferences or logistics management, there can be movement in the timing of deliveries that may result in revenue being recognized in either a preceding or following interim fiscal period. Our expected future industrial wood pellet sales under our Contracted Backlog as of December 29, 2017, is as follows (in millions):

| | |
|---|----------------|
| Fiscal 2018..... | \$ 355 |
| Fiscal 2019 and thereafter..... | 2,646 |
| Total product sales under Contracted Backlog | \$3,001 |

RESULTS OF OPERATIONS

Analysis of Results for Q4 2017 to Q4 2016

The following section provides an overview of our financial performance in Q4 2017 compared to Q4 2016. The following discussion of variances reflect one less week of operations in Q4 2017 compared to Q4 2016.

| <u>Thousands except per MT amounts</u> | <u>Q4 2017</u> | <u>Q4 2016</u> | <u>Q4 2017</u> |
|---|------------------|------------------|--------------------|
| | <u>13 Weeks</u> | <u>14 Weeks</u> | <u>vs. Q4 2016</u> |
| MT's of industrial wood pellets sold | 334 | 335 | (1) |
| Revenue | \$ 72,958 | \$ 70,935 | \$ 2,023 |
| Costs and expenses | | | |
| Production..... | 47,377 | 46,278 | 1,099 |
| Distribution..... | 9,925 | 11,079 | (1,154) |
| Selling, general and administration | 4,347 | 4,116 | 231 |
| Amortization..... | 5,280 | 5,557 | (277) |
| | 66,929 | 67,030 | (101) |
| Profit before finance (income) costs and other (income) expenses | 6,029 | 3,905 | 2,124 |
| Finance (income) cost..... | 6,120 | (15,004) | 21,124 |
| Other (income) expense..... | (358) | 11,595 | (11,953) |
| | 5,762 | (3,409) | 9,171 |
| Net profit before income taxes | 267 | 7,314 | (7,047) |
| Income tax (expense) recovery | | | |
| Current..... | - | (12) | 12 |
| Deferred..... | (163) | (4,716) | 4,553 |
| Income Taxes..... | (163) | (4,728) | 4,565 |
| Net profit and comprehensive income | \$ 104 | \$ 2,586 | \$ (2,482) |

Revenue

Revenue for Q4 2017 totaled \$73.0 million, an increase of 2.9%, or \$2.0 million, compared to \$70.9 million for Q4 2016. This increase was primarily a result of an increase in the average sales price per MT reflecting an improved contract mix on higher priced U.K. and European contracts in Q4 2017 compared to Q4 2016. Sales volumes were comparable between the two periods.

Production

Production costs were \$47.4 million for Q4 2017, an increase of \$1.1 million from \$46.3 million for Q4 2016, primarily due to an increase in fibre costs. Production volumes were comparable between the two periods.

Distribution

Distribution costs were \$9.9 million for Q4 2017, a decrease of \$1.2 million compared to \$11.1 million for Q4 2016, primarily as a result of increased shipments through our lower cost Westview Terminal.

Selling, general and administration

Selling, general and administration expenses increased \$0.2 million from \$4.1 million for Q4 2016 to \$4.3 million for Q4 2017. Non-recurring portions of SG&A expenses include certain professional fees incurred in connection with the Offering in Q4 2017 of \$0.6 million and certain legal fees related to a damage claim we are pursuing against one of our equipment suppliers in Q4 2017 of \$0.2 million. In Q4 2016, legal fees related to this claim were \$0.3 million. Excluding the above non-recurring items, SG&A expenses decreased \$0.3 million from Q4 2016 to Q4 2017.

Amortization

There was no significant change in amortization expense from Q4 2016 to Q4 2017. During Q4 2017, the majority of additions to property, plant and equipment related to construction in progress for the Entwistle and Smithers Facilities. Construction in progress is not subject to amortization until the assets are available for use. The Entwistle and Smithers Facilities have planned production commencement dates in the first and fourth quarters of Fiscal 2018, respectively. Additions to property, plant and equipment other than construction in progress in Q4 2017 included those related to the optimization of the pelleters and drying system at our Lavington Facility, and contributed to an increase in amortization expense in Q4 2017. This was offset by write-downs of property, plant and equipment related to the shutdown of the Quesnel facility.

Finance (income) cost

In Q4 2016, finance income was \$15.0 million and in Q4 2017 finance cost was \$6.1 million, resulting in a variance of \$21.1 million. Finance income in Q4 2016 was primarily related to a \$21.3 million gain from the revaluation of shareholders' debentures on modification, offset by interest on the revolver loan, term debt, delayed draw loan and debentures, and other finance costs. There was no modification of shareholders' debentures in Q4 2017.

Other (income) expense

In Q4 2016, other expense was \$11.6 million and in Q4 2017 other income was \$0.4 million, resulting in a variance of \$12.0 million. Other expense in Q4 2016 related to revaluation loss of the Class B and Class D common shares. Other income in Q4 2017 was not significant.

Income taxes

Income tax expense was \$0.2 million in Q4 2017, a decrease of \$4.5 million from \$4.7 million in Q4 2016, due to the decreases in net profit before income taxes.

Net profit and comprehensive income

Net profit and comprehensive income was \$0.1 million in Q4 2017, a decrease of \$2.5 million from \$2.6 million in Q4 2016, primarily due to a non-recurring \$21.3 million gain recorded in Q4 2016 from the revaluation of shareholders' debentures, offset by a \$11.6 million loss recorded in Q4 2016 from the revaluation of Class B and D common shares.

Adjusted Gross Margin Percentage

| Thousands except per MT amounts | Q4 2017 | Q4 2016 | Q4 2017 |
|---|------------------|------------------|--------------------|
| | 13 Weeks | 14 Weeks | vs. Q4 2016 |
| Profit (loss) before finance costs and other income (expenses) | \$ 6,029 | \$ 3,905 | \$ 2,124 |
| Selling, general and administration | 4,347 | 4,116 | 231 |
| Amortization | 5,280 | 5,557 | (277) |
| Equity earnings in HPLP | 255 | 172 | 83 |
| Non-controlling interests | 20 | (207) | 227 |
| Adjusted Gross Margin | \$ 15,931 | \$ 13,543 | \$ 2,388 |
| Adjusted Gross Margin per MT of industrial wood pellets sold | \$ 47.70 | \$ 40.43 | \$ 7.27 |
| Adjusted Gross Margin percentage of Revenue | 21.8% | 19.1% | 2.7% |

Adjusted Gross Margin Percentage increased to 21.8% for Q4 2017 (\$47.70/MT), up from 19.1% in Q4 2016 (\$40.43/MT), primarily due to higher average sales prices and lower distribution costs in Q4 2017 as discussed above, partially offset by increases in production costs.

Adjusted EBITDA

| Thousands except per MT amounts | Q4 2017 | Q4 2016 | Q4 2017 vs Q4 2016 |
|---|-----------------|------------------|-----------------------|
| Total MT's of industrial wood pellets sold | 334 | 335 | (1) |
| Net profit and comprehensive income for the year | \$104 | \$2,586 | \$(2,482) |
| Income tax expense | 163 | 4,728 | (4,565) |
| Finance costs (income) excluding shareholder debentures (note 1) | 3,241 | (17,833) | 21,074 |
| Finance costs on shareholder debentures | 2,667 | 2,959 | (292) |
| Amortization of equipment and intangible assets (note 2) | 5,089 | 5,365 | (276) |
| EBITDA | \$11,264 | \$(2,195) | \$13,459 |
| <i>EBITDA Adjustments</i> | | | |
| Stock-based compensation expense | 172 | 91 | 81 |
| Loss on disposal of PP&E (note 2) | 478 | 1,687 | (1,209) |
| Plant curtailment costs | 53 | 687 | (634) |
| Revaluation of Class B and Class D common shares | (424) | 10,278 | (10,702) |
| Other items (note 3) | 1,232 | 422 | 810 |
| Total Adjustments | 1,511 | 13,165 | (11,654) |
| Adjusted EBITDA | \$12,775 | \$10,970 | \$1,805 |
| Adjusted EBITDA per MT of industrial wood pellets sold | \$38.25 | \$32.75 | \$5.50 |

Notes:

- (1) Finance cost excluding shareholder debentures excludes realized (gain) loss on derivatives and foreign exchange.
- (2) Amortization and loss on disposal of PP&E includes our share of HPLP and excludes the non-controlling interest's share of LPLP.
- (3) Other items include deduction for the non-controlling interest's share of LPLP as well as non-recurring items such as legal fees related to pursuing a damage claim and, in 2017, fees related to financing activities.

Adjusted EBITDA increased \$1.8 million to \$12.8 million in Q4 2017, up from \$11.0 million in Q4 2016. This increase was due to higher sales prices and lower distribution costs as discussed above. The increase was offset by higher production costs, as well as higher SG&A costs due to inflation adjustments on employees' salaries and increased headcount.

Analysis of Results for Fiscal 2017 compared to Fiscal 2016

The following section provides an overview of our financial performance during Fiscal 2017 compared to Fiscal 2016. The following discussion of variances reflect one fewer week of operations in Fiscal 2017 compared to Fiscal 2016.

| Thousands except per MT amounts | 2017 52 weeks | 2016 53 Weeks | 2017 vs. 2016 |
|---|--------------------------|--------------------------|--------------------------|
| MT's of industrial wood pellets sold | 1,373 | 1,304 | 69 |
| Revenue | \$292,727 | \$266,338 | \$26,389 |
| Costs and expenses | | | |
| Production..... | 188,414 | 173,693 | 14,721 |
| Distribution..... | 38,421 | 39,474 | (1,053) |
| Selling, general and administration..... | 15,268 | 12,331 | 2,937 |
| Amortization..... | 21,819 | 21,211 | 608 |
| | 263,922 | 246,709 | 17,213 |
| Profit (loss) before finance costs and other (income) expenses | 28,805 | 19,629 | 9,176 |
| Finance Cost..... | 24,251 | 1,000 | 23,251 |
| Other expense..... | 8,912 | 7,796 | 1,116 |
| | 33,163 | 8,796 | 24,367 |
| Net profit (loss) before income taxes | (4,358) | 10,833 | (15,191) |
| Income tax (expense) recovery | | | |
| Current..... | - | (2) | 2 |
| Deferred..... | (526) | (5,569) | 5,043 |
| Income Taxes..... | (526) | (5,571) | 5,045 |
| Net profit (loss) and comprehensive income (loss) | \$(4,884) | \$5,262 | \$(10,146) |

Revenue

Revenue increased to \$292.7 million for Fiscal 2017, an increase of 9.9%, or \$26.4 million, compared to \$266.3 million in Fiscal 2016. This increase was primarily due to an additional 69,000 MT of industrial wood pellets sold in Fiscal 2017, as well as an increase in the average sales price per MT reflecting an improved contract mix on higher priced U.K. and European contracts in Fiscal 2017 compared to Fiscal 2016.

Production

Production costs were \$188.4 million for Fiscal 2017, an increase of \$14.7 million compared to \$173.7 million in Fiscal 2016, reflecting increased production volumes.

Distribution

Distribution costs were \$38.4 million in Fiscal 2017, a decrease of \$1.1 million from \$39.5 million in Fiscal 2016 primarily as a result of increased shipments through our lower cost Westview Terminal.

Selling, general and administration

SG&A expenses increased \$3.0 million from \$12.3 million for Fiscal 2016 to \$15.3 million for Fiscal 2017. This increase was primarily due to inflation adjustments on employees' salaries, increased employee headcount, certain professional fees incurred in connection with the Offering and higher legal costs. Non-recurring portions of SG&A expenses include certain professional fees incurred in connection with the Offering in Fiscal 2017 of \$1.9 million and certain legal fees related to a damage claim we were pursuing against one of our equipment suppliers in Fiscal 2017 of \$1.0 million. In Fiscal 2016, legal fees related to this claim were \$0.6 million. Excluding the above non-recurring items, SG&A expenses increased \$0.7 million from Fiscal 2016 to Fiscal 2017.

Amortization

There was no significant change in amortization expense from Fiscal 2016 to Fiscal 2017. The majority of additions to property, plant and equipment during Fiscal 2017 related to construction in progress for the Entwistle and Smithers Facilities. Construction in progress is not subject to amortization until the assets are available for use. The Entwistle and Smithers production facilities have planned production commencement dates in the first and fourth quarters of 2018, respectively.

Finance cost

Finance costs were \$24.3 million in Fiscal 2017, an increase of \$23.3 million compared to \$1.0 million in Fiscal 2016. This increase was primarily related to a non-recurring gain of \$21.3 million on modification of debentures in Fiscal 2016. In addition, the Company recognized a loss on revaluation of fair value of derivatives on US dollar foreign exchange forward contracts during Fiscal 2017. The corresponding revaluation in Fiscal 2016 resulted in a gain.

Other expense

Other expense increased \$1.1 million from \$7.8 million for Fiscal 2016 to \$8.9 million for Fiscal 2017. The increase was primarily due to:

- an increase of \$3.0 million in production facility curtailment costs from \$1.6 million in Fiscal 2016 to \$4.6 million in Fiscal 2017 as a result of the curtailment of our Quesnel facility while we evaluated the long-term viability of this facility. The shutdown of the Quesnel facility was due to the lack of fibre as several of the sawmills near the Quesnel facility shut down operations;
- a decrease of \$4.7 million in the revaluation loss on Class B and Class D common shares from \$10.3 million for Fiscal 2016 to \$5.6 million in Fiscal 2017; and
- non-recurring income in Fiscal 2016 of \$4.9 million related to our share of recovery from a legal settlement.

Remaining changes in other expense were not significant.

Income taxes

Income taxes were \$0.6 million for Fiscal 2017, a decrease of \$5.0 million from \$5.6 million for Fiscal 2016. This change was due to the Company incurring a net loss before income taxes for Fiscal 2017.

At the end of Fiscal 2017, the Company had \$96.4 million of unused non-capital loss carry forwards expiring between 2032 and 2037 to reduce future taxable income. At the end of Fiscal 2016, the Company had \$115.4 million of unused non-capital loss carry forwards.

Net profit (loss) and comprehensive income (loss)

Net loss and comprehensive loss was \$4.9 million in Fiscal 2017, compared with a net profit and comprehensive income of \$5.3 million in Fiscal 2016. The variance was primarily due to a non-recurring \$21.3 million gain recorded in Fiscal 2016 from the revaluation of shareholders' debentures, a non-recurring income in Fiscal 2016 of \$4.9 million related to Pinnacle's share of recovery from a legal settlement, offset by a \$4.7 million decrease in revaluation loss on Class B and D common shares from Fiscal 2016 to Fiscal 2017.

Adjusted Gross Margin Percentage

| Thousands except per MT amounts | 2017 52 weeks | 2016 53 Weeks | 2017 vs. 2016 |
|---|------------------|------------------|------------------|
| Profit (loss) before finance costs and other income (expenses) .. | \$28,805 | \$19,629 | \$9,176 |
| Selling, general and administration..... | 15,268 | 12,331 | 2,937 |
| Amortization..... | 21,819 | 21,211 | 608 |
| Equity earnings in HPLP..... | 1,381 | 5,675 | (4,294) |
| Our Share of Income in HPLP legal settlement..... | - | (4,875) | 4,875 |
| Non-controlling interest | (353) | (866) | 513 |
| Adjusted Gross Margin | \$66,920 | \$53,105 | \$13,815 |
| Adjusted Gross Margin per MT of industrial wood pellets sold | \$48.74 | \$40.72 | \$8.02 |
| Adjusted Gross Margin percentage of Revenue | 22.9% | 19.9% | 3.0% |

Adjusted Gross Margin Percentage was 22.9% for Fiscal 2017, up from 19.9% for Fiscal 2016, reflecting higher average sales prices and lower distribution costs in Fiscal 2017 as discussed above, partially offset by increases in production costs.

Adjusted EBITDA

| Thousands except per MT amounts | 2017 52 weeks | 2016 53 Weeks | 2017 vs. 2016 |
|--|------------------|------------------|-------------------|
| Total MT's of industrial wood pellets sold | 1,374 | 1,304 | 70 |
| Net profit (loss) and comprehensive income (loss) for the year..... | \$(4,884) | \$5,262 | \$(10,146) |
| Income tax expense..... | 526 | 5,571 | (5,045) |
| Finance costs (income) on shareholder debentures..... | 12,359 | (8,244) | 20,603 |
| Finance costs excluding shareholder debentures (note 1)..... | 11,592 | 9,618 | 1,974 |
| Amortization of equipment and intangible assets (note 2) | 21,395 | 21,031 | 364 |
| EBITDA | 40,988 | 33,238 | 7,750 |
| <i>EBITDA Adjustments</i> | | | |
| Stock-based compensation expense..... | 237 | 138 | 99 |
| Pinnacle's share of HPLP legal settlement..... | - | (4,875) | 4,875 |
| Loss on disposal of PP&E (note 2)..... | 1,049 | 2,353 | (1,304) |
| Plant curtailment costs and impairment loss..... | 4,626 | 1,591 | 3,035 |
| Revaluation of Class B and Class D shares..... | 5,601 | 10,278 | (4,677) |
| Other items (note 3) | 3,620 | 1,199 | 2,421 |
| Total Adjustments..... | 15,133 | 10,684 | 4,449 |
| Adjusted EBITDA | \$56,121 | \$43,922 | \$12,199 |
| Adjusted EBITDA per MT of industrial wood pellets sold | \$40.87 | \$33.68 | \$7.19 |

Notes:

- (1) Finance cost excluding shareholder debentures excludes realized (gain) loss on derivatives and foreign exchange.
- (2) Amortization and loss on disposal of PP&E includes our share of HPLP and excludes the non-controlling interest's share of LPLP.
- (3) Other items include deduction for the non-controlling interest's share of LPLP as well as non-recurring items such as legal fees related to pursuing a damage claim and, in 2017, fees related to financing activities.

Adjusted EBITDA was \$56.1 million (\$40.87/MT) in Fiscal 2017, an increase of 27.8% from \$43.9 million (\$33.68/MT) in Fiscal 2016. This \$12.2 million increase was due to higher sales prices, higher sales volume, and lower

distribution costs as discussed above. The increase was offset by higher production costs, as well as higher SG&A costs due to inflation adjustments on employees' salaries and increased headcount.

Free Cash Flow

| All numbers in thousands | 2017 | 2016 | 2017 |
|--|-------------------|-----------------|--------------------|
| | 52 weeks | 53 Weeks | vs. 2016 |
| Net profit (loss) and comprehensive income (loss) | \$ (4,884) | \$ 5,262 | \$ (10,146) |
| Income tax expense | 526 | 5,571 | (5,045) |
| Finance costs excluding shareholder debentures ⁽¹⁾ | 11,592 | 9,618 | 1,974 |
| Finance costs (income) on shareholder debentures..... | 12,359 | (8,244) | 20,603 |
| Amortization of equipment and intangible assets ⁽²⁾ | 21,395 | 21,031 | 364 |
| EBITDA | 40,988 | 33,238 | 7,750 |
| Stock-based compensation expense | 237 | 138 | 99 |
| HPLP legal settlement | - | (4,875) | 4,875 |
| Loss on disposal of PP&E ⁽³⁾ | 1,049 | 2,353 | (1,304) |
| Plant curtailment costs..... | 4,626 | 1,591 | 3,035 |
| Revaluation of Class B and Class D shares..... | 5,601 | 10,278 | (4,677) |
| Other items ⁽⁴⁾ | 3,620 | 1,199 | 2,421 |
| Adjusted EBITDA ⁽⁵⁾ | 56,121 | 43,922 | 12,199 |
| Maintenance capital expenditures ⁽⁶⁾ | (9,040) | (4,434) | (4,606) |
| Interest and finance costs, net ⁽⁷⁾ | (7,425) | (8,539) | 1,114 |
| Cash taxes paid ⁽⁸⁾ | - | - | - |
| Mandatory amortization ⁽⁹⁾ | (1,600) | (8,370) | 6,770 |
| Free Cash Flow ⁽¹⁰⁾ | \$38,056 | \$22,579 | \$15,477 |

Notes:

- (1) Finance cost excluding shareholder debentures excludes realized (gain) loss on derivatives and foreign exchange.
- (2) Amortization of PP&E includes our share of HPLP and excludes the non-controlling interest's share of LPLP.
- (3) Loss on disposal of PP&E includes our share of HPLP and excludes the non-controlling interest's share of LPLP.
- (4) Other items include deduction for the non-controlling interest's share of LPLP as well as non-recurring items such as legal fees related to pursuing a damage claim and fees related to financing activities.
- (5) See definition of Adjusted EBITDA in the section entitled "Key Performance Indicators" and reconciliation of Adjusted EBITDA to net income in "Selected Consolidated Financial Information".
- (6) "Maintenance capital expenditures" refers to cash expenditures to maintain long-term operating capacity or net income. Annual maintenance capital expenditure allows for the maintenance of long-term operating capacity or net income. Upon commissioning of the Entwistle Facility and the Smithers Facility, we anticipate these facilities to require \$3.6 million in annual maintenance capital expenditures.
- (7) Reflect post-Offering capital structure, and therefore exclude interest and financing costs on historical credit facilities described under "Description of Material Indebtedness — The Credit Agreement". We have repaid certain of our credit facilities upon the Offering. Refer to the section entitled "Subsequent Events".
- (8) In recent years, we have accumulated significant net operating losses that will shield future earnings from taxes. As at December 29, 2017 and December 30, 2016, we had unused non-capital loss carryforwards of \$96.4 million and \$115.4 million, respectively. We do not anticipate a requirement to pay income tax before 2020.
- (9) There was no mandatory amortization for the period from the first quarter to the third quarter of Fiscal 2017 of the Term Credit Facility and of the Delayed Draw Term Credit Facility as described under "Description of Material Indebtedness — The Credit Agreement" in the Prospectus. On December 13, 2017, we amended our credit facilities. Refer to the section entitled "Liquidity and Capital Resources – Senior Credit Facilities" in this MD&A for details of the amended credit facilities.
- (10) See definition of Free Cash Flow in "Non-IFRS Measures".

SUMMARY OF CONSOLIDATED RESULTS AND CERTAIN PERFORMANCE MEASURES

The following table summarizes the results of our operations for the last eight quarters. This unaudited quarterly information has been prepared in accordance with IFRS. ⁽¹⁾

| Thousands except per MT and per share amounts | 2017 | | | | 2016 | | | |
|---|----------------|------------------|----------------|----------------|----------------|----------------|----------------|------------------|
| | Q4 | Q3 | Q2 | Q1 | Q4 | Q3 | Q2 | Q1 |
| | 13 Weeks | 13 Weeks | 13 Weeks | 13 Weeks | 14 Weeks | 13 Weeks | 13 Weeks | 13 Weeks |
| MT's of industrial wood pellets sold | 334 | 387 | 332 | 320 | 335 | 321 | 349 | 299 |
| Revenue | \$72,958 | \$82,366 | \$69,556 | \$67,847 | \$70,935 | \$65,322 | \$70,293 | \$59,788 |
| Costs and expenses | | | | | | | | |
| Production | 47,377 | 51,628 | 44,863 | 44,546 | 46,278 | 41,437 | 46,282 | 39,696 |
| Distribution | 9,925 | 11,568 | 7,868 | 9,060 | 11,079 | 9,484 | 10,737 | 8,174 |
| Selling, general and administration | 4,347 | 4,222 | 3,493 | 3,206 | 4,116 | 2,867 | 2,784 | 2,564 |
| Amortization | 5,280 | 5,365 | 5,570 | 5,604 | 5,557 | 5,067 | 5,549 | 5,038 |
| | 66,929 | 72,783 | 61,794 | 62,416 | 67,030 | 58,855 | 65,352 | 55,472 |
| Profit (loss) before finance costs and other (income) expenses | 6,029 | 9,583 | 7,762 | 5,431 | 3,905 | 6,467 | 4,941 | 4,316 |
| Finance Cost ⁽²⁾ | 6,120 | 6,469 | 5,835 | 5,827 | (15,004) | 5,555 | 5,080 | 5,369 |
| Other (income) expense ⁽³⁾⁽⁴⁾ | (358) | 9,146 | 131 | (7) | 11,595 | (4,201) | 190 | 212 |
| | 5,762 | 15,615 | 5,966 | 5,820 | (3,409) | 1,354 | 5,270 | 5,581 |
| Net profit (loss) before income taxes | 267 | (6,032) | 1,796 | (389) | 7,314 | 5,113 | (329) | (1,265) |
| Income tax (expense) recovery | | | | | | | | |
| Current | — | — | — | — | (12) | 10 | — | — |
| Deferred | (163) | 2 | (469) | 104 | (4,716) | (1,309) | 106 | 350 |
| Income Taxes | (163) | 2 | (469) | 104 | (4,728) | (1,299) | 106 | 350 |
| Net profit (loss) and comprehensive income (loss) | \$104 | \$(6,030) | \$1,327 | \$(285) | \$2,586 | \$3,814 | \$(223) | \$(915) |
| Net Profit (loss) and comprehensive income (loss) attributable to: | | | | | | | | |
| Owners of the Company | 124 | (6,371) | 1,234 | (224) | 2,379 | 3,444 | (308) | (1,119) |
| Non-controlling interests | (20) | 341 | 93 | (61) | 207 | 370 | 85 | 204 |
| Net profit (loss) and comprehensive income (loss) | \$104 | \$(6,030) | \$1,327 | \$(285) | \$2,586 | \$3,814 | \$(223) | \$(915) |
| Net income (loss) attributable to owners | | | | | | | | |
| Net income (loss) attributable to owners | 124 | (6,371) | 1,234 | (224) | 2,379 | 3,444 | (308) | (1,119) |
| Cumulative preferred dividends .. | (409) | (309) | (309) | (310) | (310) | (309) | (312) | (323) |
| | \$(285) | \$(6,680) | \$925 | \$(534) | \$2,069 | \$3,135 | \$(620) | \$(1,442) |
| Net profit (loss) per share attributable to owners | | | | | | | | |
| Basic and diluted – Class A | \$(0.01) | \$(0.23) | \$0.03 | \$(0.01) | \$0.07 | \$0.11 | \$(0.02) | \$(0.05) |
| Basic and diluted – Class B | \$(0.01) | \$(0.23) | \$0.03 | \$(0.01) | \$0.07 | \$0.11 | \$(0.02) | \$(0.05) |

Notes:

- (1) Factors that impact the comparability of the quarters include the following: (a) the cost of producing industrial wood pellets during the winter is typically greater than that during the summer due to the higher moisture content of raw materials which results in higher drying costs and the increased costs of maintaining operating equipment due to lower ambient temperatures; and (b) net profit (loss) is also impacted by fluctuations in Canadian dollar exchange rates from the revaluation of the Company's outstanding U.S. dollar forward exchange contracts.
- (2) In Q4 2016, a \$21.3 million (before-tax) gain was recognized on the modification of terms of shareholders' debentures.
- (3) Class B and Class D common shares, which are classified as liabilities are subject to fair value adjustments. Revaluation gains and losses were recognized as follows: in the third quarter of Fiscal 2017, a loss of \$6.0 million (before-tax), and in Q4 2016, a loss of \$10.3 million (before-tax).
- (4) In the third quarter of Fiscal 2016, a \$4.9 million (before-tax) gain was recognized from our share of a legal settlement.

The following table summarizes the results of our operations for the last eight quarters based on non-IFRS measures.

Adjusted Gross Margin Percentage

| Thousands except per MT amounts | 2017 | | | | 2016 | | | |
|--|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|-----------------|
| | Q4 | Q3 | Q2 | Q1 | Q4 | Q3 | Q3 | Q4 |
| | 13 Weeks | 13 Weeks | 13 Weeks | 13 Weeks | 14 Weeks | 13 Weeks | 13 Weeks | 13 Weeks |
| Profit (loss) before finance costs and other income (expenses)..... | \$6,029 | \$9,583 | \$7,762 | \$5,431 | \$3,905 | \$6,467 | \$4,941 | \$4,316 |
| Selling, general and administration..... | 4,347 | 4,222 | 3,493 | 3,206 | 4,116 | 2,867 | 2,784 | 2,564 |
| Amortization..... | 5,280 | 5,365 | 5,570 | 5,604 | 5,557 | 5,067 | 5,549 | 5,038 |
| Equity earnings in HPLP | 255 | 544 | 265 | 317 | 172 | 4,915 | 174 | 414 |
| Pinnacle's Share of Income in HPLP legal settlement... | — | — | — | — | — | (4,875) | — | — |
| Non-controlling interests..... | 20 | (341) | (93) | 61 | (207) | (370) | (85) | (204) |
| Adjusted Gross Margin | \$15,931 | \$19,373 | \$16,997 | \$14,619 | \$13,543 | \$14,071 | \$13,363 | \$12,128 |
| Adjusted Gross Margin per MT of industrial wood pellets sold | 47.70 | 50.06 | 51.20 | 45.68 | 40.43 | 43.83 | 38.29 | 40.56 |
| Adjusted Gross Margin percentage of Revenue..... | 21.8% | 23.5% | 24.4% | 21.5% | 19.1% | 21.5% | 19.0% | 20.3% |

Adjusted EBITDA

| Thousands except per MT amounts | 2017 | | | | 2016 | | | |
|---|----------------|------------------|-----------------|-----------------|-----------------|-----------------|-----------------|----------------|
| | Q4 | Q3 | Q2 | Q1 | Q4 | Q3 | Q2 | Q1 |
| Total MT's of industrial wood pellets sold | 334 | 387 | 332 | 320 | 335 | 321 | 349 | 299 |
| Net profit (loss) and comprehensive income (loss) for the year | \$104 | \$(6,030) | \$1,327 | \$(285) | \$2,586 | \$3,814 | \$(223) | \$(915) |
| Income tax expense (recovery) | 163 | (2) | 469 | (104) | 4,728 | 1,299 | (106) | (350) |
| Finance costs excluding shareholder debentures (note 1) | 2,667 | 3,176 | 2,613 | 3,136 | 2,959 | 2,412 | 1,955 | 2,292 |
| Finance costs (income) on shareholder debentures | 3,241 | 3,167 | 3,218 | 2,733 | (17,833) | 3,335 | 3,206 | 3,048 |
| Amortization of equipment and intangible assets (note 2)..... | 5,089 | 5,267 | 5,537 | 5,502 | 5,365 | 5,242 | 5,456 | 4,968 |
| EBITDA | 11,264 | 5,578 | 13,164 | 10,982 | (2,195) | 16,102 | 10,288 | 9,043 |
| <i>EBITDA Adjustments</i> | | | | | | | | |
| Stock-based compensation expense | 172 | 21 | 22 | 22 | 91 | 50 | 51 | (54) |
| Pinnacle's share of HPLP legal settlement..... | — | — | — | — | — | (4,875) | — | — |
| Loss on disposal of PP&E (note 2) | 478 | 366 | 146 | 59 | 1,687 | 235 | 265 | 166 |
| Plant curtailment costs | 53 | 3,571 | 506 | 496 | 687 | 629 | 275 | — |
| Revaluation of Class B and Class D shares | (424) | 6,025 | — | — | 10,278 | — | — | — |
| Other items..... | 1,232 | 1,211 | 580 | 597 | 422 | 158 | 263 | 356 |
| Total Adjustments | 1,511 | 5,171 | 1,254 | 1,174 | 13,165 | (3,803) | 854 | 468 |
| Adjusted EBITDA | 12,775 | \$16,772 | \$14,418 | \$12,156 | \$10,970 | \$12,299 | \$11,142 | \$9,511 |
| Adjusted EBITDA per MT of industrial wood pellets sold | \$38.25 | \$43.34 | \$43.43 | \$37.99 | \$32.75 | \$38.31 | \$31.93 | \$31.81 |

Notes:

- (1) Finance cost excluding shareholder debentures excludes realized (gain) loss on derivatives and foreign exchange.
(2) Amortization and loss on disposal of PP&E includes our share of HPLP and excludes the non-controlling interest's share of LPLP.

LIQUIDITY AND CAPITAL RESOURCES

Overview

Our principal uses of funds are for operating expenses, capital expenditures, debt service requirements and dividends. We believe that cash generated from operations, together with amounts available under our amended credit agreement, will be sufficient to meet our operating expenses, capital expenditures, debt service and dividend requirements. In addition, we believe that our capital structure provides us with significant financial flexibility to pursue our future growth strategies. See “Growth Strategies” in the Prospectus for further details.

However, our ability to fund operating expenses, capital expenditures, and future debt service and dividend requirements will depend on, among other things, our future operating performance, which will be affected by general economic, financial and other factors, including factors beyond our control. See “Summary of Factors Affecting Performance” and “Risk Factors” in this MD&A for additional information. We review investment opportunities in the normal course of our business and may make select investments to implement our business strategy when suitable opportunities arise.

Historically, the funding for any such investments has come from cash flow from operating activities and/or our credit facilities. We believe our delayed draw facility under our amended credit agreement, together with the proceeds from the Offering, will be sufficient to finance the Entwistle Facility and Smithers Facility.

Non-cash Working Capital

“Non-cash working capital” is defined as the sum of accounts receivable, inventories, and other current assets, less accounts payable and accrued liabilities, and other current liabilities. Non-cash working capital excludes cash, the current portion of our long-term debt including the revolving credit facility and therefore provides our management and investors with a clear understanding of the efficiency of our operational working capital needs. Our need for non-cash working capital is highly dependent on the timing of shipments, particularly at the end of a period as a total shipment can be valued as much as \$12 million. Shipment timing impacts accounts receivable and finished industrial wood pellet inventories. Payment terms differ for each contract, but we typically receive an initial payment equal to 90% of the total value of a shipment 12 to 15 days after the shipment leaves the port, with the balance received after the vessel fully discharges its cargo to the customer. Less significantly, non-cash working capital is impacted by wood fibre inventory changes due to the accumulation of wood fibre in winter months and increases in whole log volumes and values as we diversify our wood fibre sources and create supply stock piles.

Senior Credit Facilities

As at December 29, 2017, our credit facilities consisted of \$180 million of term debt, \$130 million of committed delayed draw with \$20 million drawn and \$50 million of committed revolver, with \$22 million drawn. All facilities mature on December 16, 2022.

Advances under the facilities are available as Canadian dollar Prime-Based Loans, Banker’s Acceptances (“BA”) from the BA Lenders in Canadian dollars, BA Equivalent Loans from the Non-BA Lenders in Canadian dollars, US dollar Base Rate Loans, and LIBOR Loans in US dollars. Interest accrues daily and is payable monthly at the applicable Bank Prime, BA, US Base or LIBOR rates plus a margin. The margin varies based on the ratio of Senior Debt to Adjusted EBITDA with a minimum margin of 1.50% and 2.50% for Prime/US Base and BA/LIBOR loans, respectively and a maximum margin of 3.00% and 4.00%, respectively.

At December 29, 2017, the \$180 million term loan and the revolver loan were in Canadian dollar Prime loans at 5.70% and the \$22 million delayed draw term loan was in a Canadian dollar BA loan at 4.86%. At December 30, 2016, the \$160 million term loan was in a Canadian dollar BA loan at 4.42% and the revolver loan was in a Canadian dollar Prime loan at 5.20%. At December 29, 2017, we had issued letters of credit totaling \$0.5 million (2016 - \$0.4 million).

EBITDA and Adjusted EBITDA are defined in the Facility agreement and used in the calculation of debt covenants and interest rate margins. The primary debt covenants are the Total Funded Debt to Adjusted EBITDA and Fixed Charge Coverage Ratio. As at December 29, 2017 and December 30, 2016, the Company was in compliance with all debt covenants.

The debt is secured by a first-ranking security interest on all present and after-acquired assets of the Company's subsidiary, Pinnacle Renewable Energy Inc.

The credit facilities have authorized credit and repayment terms as follows:

a) Revolver loan

We may borrow up to \$50 million (2016 - \$50 million) under the revolver loan with a maximum of \$5 million (2016 - \$5 million) for letters of credit. The revolver loan is to be used for operating purposes and is expected to be repaid within the year, and therefore has been presented as a current liability.

b) Term loan

We may borrow up to \$200 million (2016 - \$160 million) under the non-revolving term loan and as at December 29, 2017 had borrowed \$180 million (2015 - \$160 million). We are required to make principal payments on the term loan in installments on the last day of each fiscal quarter as follows: (i) \$2 million on March 31, 2018 to December 31, 2018, inclusive, (ii) \$2.5 million on March 31, 2019 to December 31, 2019, inclusive, (iii) \$4 million on March 31, 2020 to December 31, 2020, inclusive and (iv) \$5 million on March 31, 2021 to December 31, 2021, inclusive (v) \$6 million on March 31, 2022 to September 30, 2022. The remaining balance is due on December 13, 2022.

c) Delayed draw term loan

The Company may borrow up to \$130 million (2016 - \$90 million) under the non-revolving delayed draw term loan and at December 29, 2017 had borrowed \$20 million (2016 - \$nil). Advances under this loan may be made in multiple advances and are available to be drawn until December 31, 2019. The Company is required to make quarterly principal installments equal to (i) 2.0% of the principal amount of the loan for each repayment date occurring during or before December 31, 2020, (ii) 2.50% of the principal amount of the loan for each repayment date occurring after December 31, 2020 but during or before December 31, 2021, and (iii) 3.0% of the principal amount of the loan for each repayment date occurring after December 31, 2021 but during or before September 30, 2022. The remainder of the drawn amount is due on December 13, 2022.

All the credit facilities require mandatory loan prepayments by us of principal and interest if certain events occur.

CASH FLOWS

Analysis of cash flows for Q4 2017 compared to Q4 2016

| All numbers in thousands | Q4 2017 | Q4 2016 | Q4 2017 vs. Q4 2016 |
|---|-----------------|------------------|------------------------|
| Cash flow from operations before net change in non-cash working capital | \$11,305 | \$8,457 | \$2,848 |
| Net change in non-cash operating working capital | (15,302) | (1,543) | (13,759) |
| Financing activities | 41,165 | (10,212) | 51,377 |
| Investing activities | (29,786) | (3,812) | (25,974) |
| Other | (69) | 63 | (132) |
| Change in cash..... | \$7,313 | \$(7,047) | \$14,360 |
| Cash at beginning of period..... | 11,595 | 19,159 | (7,564) |
| Cash at end of period | \$18,908 | \$12,112 | \$6,796 |

Cash flow from operations before net change in non-cash working capital

Cash flow from operations before net change in non-cash working capital increased \$2.8 million to \$11.3 million for Q4 2017, up from \$8.5 million for Q4 2016, reflecting the higher adjusted gross margin in Q4 2017 compared to Q4 2016.

Net change in non-cash working capital

The \$15.3 million increase in non-cash working capital in Q4 2017 reflected an increase in accounts receivable related to the timing of certain shipments at period-end and the \$1.5 million increase in non-cash working capital in Q4 2016 reflected an increase in inventory.

Financing activities

In Q4 2017, financing activities provided \$41.2 million of cash primarily from the amendment of credit facilities as the Company funded the construction of the Entwistle and Smithers Facilities. In Q4 2016, financing activities used \$10.2 million as the Company paid down its credit facilities.

Investing activities

Cash used for investing activities relates primarily to the acquisition and construction of property, plant and equipment. In Q4 2017, cash used for property, plant and equipment was \$29.8 million. The increase during Fiscal 2017 represents the additional cash used for the construction of the Entwistle and Smithers Facilities. In Q4 2016, cash used for property, plant and equipment was \$3.8 million.

Analysis of cash flows for Fiscal 2017 compared to Fiscal 2016

| All numbers in thousands | Fiscal 2017 52 weeks | Fiscal 2016 53 weeks | Fiscal 2017 vs. 2016 |
|---|---------------------------------|---------------------------------|---------------------------------|
| Cash flow from operations before net change in non-cash working capital | \$51,128 | \$44,742 | \$6,386 |
| Net change in non-cash operating working capital | (20,183) | (14,126) | (6,057) |
| Financing activities | 48,812 | (20,958) | 69,770 |
| Investing activities | (72,682) | (13,250) | (59,432) |
| Other | (279) | 68 | (347) |
| Change in cash | <u>\$6,796</u> | <u>\$(3,524)</u> | <u>\$10,320</u> |
| Cash at beginning of period | <u>\$12,112</u> | <u>\$15,636</u> | <u>\$(3,524)</u> |
| Cash at end of period | <u>\$18,908</u> | <u>\$12,112</u> | <u>\$6,796</u> |

Cash flow from operations before net change in non-cash working capital

Cash flow from operations before net change in non-cash working capital provided \$51.1 million of cash for Fiscal 2017 and \$44.7 million for Fiscal 2016. This \$6.4 million increase in cash is primarily due to the increase in profitability as noted above.

Net change in non-cash working capital

The \$20.2 million increase in non-cash working capital in Fiscal 2017 was largely due to an increase in accounts receivable from higher sales and partially offset by an increase in deferred revenue. The \$14.1 million increase in non-cash working capital in Fiscal 2016 was largely due to an increase in accounts receivable as a result of higher sales, somewhat offset by an increase in accounts payable and accrued liabilities due to higher shipping cost accruals.

Financing activities

Financing activities provided \$48.8 million of cash for Fiscal 2017 and used \$21.0 million for Fiscal 2016. This \$69.8 million increase in cash is primarily due to an amendment to our credit facilities in Q4 2017 to support the construction of the Entwistle and Smithers Facilities in 2017 as discussed above.

Investing activities

Investing activities used \$72.7 million of cash for Fiscal 2017 and \$13.3 million for Fiscal 2016. This \$59.4 million increase was primarily related to the construction of the Entwistle and Smithers Facilities in Fiscal 2017.

OUTLOOK

We believe that we have an opportunity to significantly grow our revenue and underlying profitability over the next several years as a result of our current production facility development projects as well as contracted price increases in most of our off-take agreements. In addition, we believe that as the potential demand for industrial wood pellets continues to grow globally, we are positioned to grow our production platform at a similar rate through a combination of expansion projects at existing production facilities and new greenfield and brownfield growth projects.

Our strategies to realize on these opportunities are described in more detail under “Growth Strategies” in the Prospectus and can be summarized as follows:

- continue to realize production and operating efficiencies in our existing production facilities to expand EBITDA per Metric Ton;
- grow our business through the completion and operational execution of the Entwistle Facility, Smithers Facility and other greenfield project opportunities throughout North America;
- expand production capacity at existing production facilities;
- make potential accretive acquisitions of industrial wood pellet producers in Canada or the United States;
- capture a disproportionate share of opportunities in the growing Asian marketplace as a result of our proximity to this market which results in shipping cost advantages and longstanding relationship with customers in this region; and
- continue to improve gross margins through further efficiencies in our sourcing and production processes.

Our operations have experienced rail disruptions during the first quarter of Fiscal 2018 due to weather and capacity-related operational challenges facing our rail service provider. We have been able to mitigate some of our exposure to this issue through active management of our operations. Our estimate of \$61 to \$65 million in Adjusted EBITDA for Fiscal 2018 contained in the Prospectus remains unchanged.

CONTRACTUAL OBLIGATIONS AND OFF-BALANCE SHEET ARRANGEMENTS

The following table summarizes the contractual obligations and off-balance sheet arrangements at December 29, 2017 for each of the next five fiscal years and thereafter:

| (In millions of dollars) | 2018 | 2019 | 2020 | 2021 | 2022 | Thereafter | Total |
|---------------------------------|-------------|-------------|-------------|-------------|--------------|-------------------|--------------|
| Term loan..... | 6.0 | 9.5 | 14.5 | 24.0 | 146.0 | – | 200.0 |
| Finance lease..... | 0.6 | 0.5 | 0.6 | – | – | – | 1.7 |
| Operating lease..... | 8.5 | 8.4 | 7.0 | 5.2 | 3.2 | 22.2 | 54.5 |
| Total contractual obligations.. | 15.1 | 18.4 | 22.1 | 29.2 | 149.2 | 22.2 | 256.2 |

The obligations under the senior credit facilities are discussed in the “Liquidity and Capital Resources” section of this MD&A.

We have rail car leases of varying terms with Wells Fargo Rail Corporation, Interstate Commodities Inc., NuRail Canada ULC, TrinityRail Canada Inc., Midwest Railcar Corporation, Southwest Rail Industries Inc., and American Railcar Leasing LLC. Termination of these rail car lease arrangements could impact our distribution costs.

We enter into letters of credit to facilitate the throughput of industrial wood pellets through terminals and to secure expenditures on potential future capital projects. We have issued \$0.5 million letters of credit as at December 29, 2017 and \$0.4 million letters of credit as at December 30, 2016.

We have made commitments to customers and suppliers with respect to minimum volumes for sales, shipping, storage and loading and fibre purchases. These contracts are in the normal course of business and cover periods of up to fifteen years in the future. Failure to meet contractual terms other than as a result of a force majeure event as defined under the various agreements could result in various payments required by us. We expect to meet our commitments in the normal course of operations.

We have capital commitments of \$22.5 million at December 29, 2017 related to the construction of our facilities.

Other than those items disclosed here and elsewhere in this MD&A and our Consolidated Financial Statements, we do not have any material contractual obligations, off-balance sheet arrangements or commitments as at December 29, 2017 and December 30, 2016.

FINANCIAL RISK FACTORS

We are exposed to a number of risks as a result of holding financial instruments including credit risk, liquidity risk and market risk. Our Risk Management Committee manages risk related to counterparty credit risk and market risk such as foreign exchange.

Credit risk

Credit risk is the risk of financial loss to us if a counterparty to a financial instrument fails to meet its contractual obligations. Financial instruments that are subject to credit risk include cash and accounts receivable. We manage our credit risk on cash by using major Canadian chartered banks for all cash deposits. The cash balance at December 29, 2017 is \$18.9 million (2016 - \$12.1 million).

We manage our credit risk on accounts receivable by reviewing individual sales contracts considering the length of the contract and assessing the credit quality of the counterparty. Board approval is required for contracts over \$5.0 million. The significant majority of our sales are contracted with large utility customers. The accounts receivable balance at December 29, 2017 is \$41.3 million (2016 - \$24.7 million).

Liquidity risk

Liquidity risk is the risk that we will not be able to meet our respective obligations as they come due. We manage liquidity requirements through frequent monitoring of cash inflows and outflows, preparation of regular cash flow forecasting and our available credit facilities.

Refer to Note 23 to the Consolidated Financial Statements for details of the contractual maturities of financial liabilities excluding future interest and shareholders' debentures and common and preferred shares at December 29, 2017 and December 30, 2016.

At December 29, 2017, we have available liquidity of \$44.3 million (2016 - \$51.4 million) from our debt facilities and forecasts sufficient liquidity throughout Fiscal 2018. We expect to finance our operations and cash flows from our current available resources and without further support from our shareholders and lenders. However, to the extent that additional cash resources are required due to unforeseen circumstances, we anticipate support from our shareholders and lenders, although there can be no guarantees.

Market risk

Market risk is that the change in market prices such as foreign exchange rates will affect our net profit (loss) and that the future cash flows of a financial instrument will fluctuate due to changes in market prices.

With respect to costs of distribution, we mitigate the market risk of fluctuations in shipping costs by entering into long-term, fixed-price shipping contracts with reputable shippers matching the terms and volumes of our CIF off-take contracts for which we are responsible for managing shipping. We enter into these long-term shipping contracts at the same time as we enter long-term sales contracts, ensuring matching the terms and tenure between both contracts. Certain of our off-take contracts include pricing adjustments for volatility in fuel prices, which allows us to pass the majority of the fuel price risk associated with shipping through to our customers.

Foreign currency

Our functional and reporting currency is the Canadian dollar. Our sales, operating and capital expenditures are primarily denominated and settled in Canadian dollars. We have exposure to the US dollar on our shipping costs, rail car leases and some capital purchases. We mitigate our exposure to the US dollar on our shipping costs by invoicing the shipping portion in US dollars and with a contract with our major shipping provider with a fixed US dollar to Canadian dollar exchange rate. We mitigate the remaining exposure by entering into a series of US dollar forward contracts matching the amount and timing of the estimated US dollar expenditures.

These contracts are simultaneously settled on a gross tax basis as the Company exchanges US dollars into Canadian dollars at predetermined rates. We do not apply hedge accounting to its US dollar forward contracts. Refer to Note 23 to the Consolidated Financial Statements for outstanding notional amounts of the US dollar forward contracts and their contractual maturities.

Interest rate

We are exposed on interest rate risk through our debt facility including our revolver, term loan and delayed draw term loan which are subject to variable lending rates. Currently, we do not use financial instruments to manage this risk. A 1% change in interest rates would increase or decrease interest expense by \$1.8 million (2016 - \$1.6 million).

Our objective when managing our capital structure is to maintain a strong financial position and to provide returns with sufficient liquidity to undertake further growth for the benefit of our shareholders.

Refer to Note 23 to the Consolidated Financial Statements for the composition of our capital.

There were no changes to our approach to capital management during the year.

We are subject to certain financial covenants in our debt obligations. Refer to Note 9 to the Consolidated Financial Statements for details. Our strategy is to ensure we remain in compliance with all of our existing covenants so as to ensure continuous access to required debt to fund growth. We review results and forecasts to monitor our compliance.

Disclosure Controls & Procedures and Internal Control Over Financial Reporting

As we recently became a reporting issuer, we intend to file abbreviated CEO and CFO certifications in respect of our first interim period ending after becoming a reporting issuer.

CRITICAL ACCOUNTING ESTIMATES AND ACCOUNTING STANDARDS ADOPTED BUT NOT EFFECTIVE

Critical Accounting Estimates and Judgments

The preparation of consolidated financial statements in accordance 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 assumptions are continuously evaluated and are based on management's best judgments and experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Revisions to accounting estimates are recognized in the period in which the estimates are revised and in any future periods affected. Actual results may differ from these estimates.

The following discusses the most significant accounting judgments and estimates that we have made in the preparation of our consolidated financial statements:

Valuation of Non-financial Assets and certain Class B and Class D common shares

Non-financial assets including goodwill, intangible assets and property, plant & equipment are evaluated for impairment on an annual basis and certain Class B and Class D common shares held by management are adjusted to fair value on an annual basis.

We prepare our estimate of our enterprise value ("EV") as the basis for the valuation of non-financial assets and certain Class B and Class D common shares. The EV is based on the weighted average of the outputs of a discounted cash flow ("DCF") and an Adjusted EBITDA multiplier model. The DCF is weighted at 50%, with a 25% weighting applied to each of Fiscal 2018 and 2019 forecasted Adjusted EBITDA.

The EV determination is dependent on a number of assumptions including forecasted revenue, earnings, cash flows, discount rates (using our weighted average cost of capital), assumed selling prices, operating cost changes, production volumes, foreign exchange rates, capital expenditures, and trading multiples for comparative companies in relative industries and other factors including the inclusion of the Entwistle Facility for the Class B and Class D common share valuation only. This valuation process is subjective and requires management to exercise judgment in making assumptions about future results including revenue, Adjusted EBITDA and cash flows.

Impairment losses on non-financial assets (if any) are recognized in net profit (loss). Impairment losses for non-financial assets, other than goodwill, are reversed in future periods if the circumstances that led to impairment no longer exist. The reversal is limited to restoring the carrying value amount such that it does not exceed the carrying amount that would have been determined, net of amortization, had no impairment loss been recognized.

Changes in the fair value of certain Class B and Class D common shares are also recognized in net profit (loss) on an annual basis.

Our share capital has been reorganized upon closing of the Offering, after which the Class B and Class D common shares no longer exist.

Inventory

Wood fibre inventory is inherently difficult to measure and value because of the estimates and assumptions management uses to determine the volume in cubic metres of wood fibre stockpiles, the conversion rates to convert cubic metres to oven dried tons by wood fibre type and identification of obsolete and unusable wood fibre stockpiles. As well, wood fibre stockpiles are not zeroed out on a recurring basis, are significant in volume, size and complexity which can be highly variable depending on the type of wood fibre in the stockpiles, and there is no reliable industry standard for consistently measuring and valuing wood fibre inventory.

Inventories of wood fibre, finished industrial wood pellets, supplies and spare parts are measured at the lower of cost and net realizable value. The cost of inventories is based on the weighted average cost principle, and includes all direct costs incurred in production and conversion including raw materials, labour and direct overhead and other costs incurred in bringing the inventories to their existing condition and location. The cost of manufactured inventories includes production overhead based on normal operating capacity. Costs that do not contribute to bringing inventories to their present condition and location, such as storage and administration overhead, are excluded from the cost of inventories and expensed as incurred.

We estimate net realizable value as the amount finished industrial wood pellet inventories are expected to be sold for, less estimated costs for completion and costs necessary to make the sale. In determining net realizable value, factors such as obsolescence and damage, aging of, and future potential demand for, the inventory, selling prices, and contractual arrangements with customers are considered. A change to these assumptions could impact the inventory valuation and

have a resulting impact on gross profits. Inventories are written down to net realizable value when their cost is not deemed to be recoverable. When circumstances that previously caused inventories to be written down below cost no longer exist, including when there is clear evidence of an increase in selling price, the amount of the write-down previously recorded is reversed.

Decommissioning liabilities

We have certain decommissioning liabilities related to the operations of the Westview Terminal, the plants at Lavington, Armstrong, and Williams Lake, and the use of rail cars. The measurement of decommissioning liabilities requires management to make assumptions and estimates with respect to the anticipated timing and amount of cash flows required to settle the obligations, as well as the discount rates used in measuring these provisions.

Accounts receivable

Accounts receivable are measured at cost. We evaluate accounts receivable for impairment to determine if an allowance for doubtful accounts is required. A specific allowance is recorded against customer receivables based on the evaluation of the customers' credit worthiness and knowledge of their financial condition. When a receivable is considered permanently uncollectible, the receivable is written off against the allowance account. Historically, we have experienced insignificant amount of bad debt.

Stock-Based Compensation

Stock-based compensation expense requires the use of estimates in the Black-Scholes option pricing model. The classification of stock options as an equity-settled or cash-settled plan is influenced by judgment in determining the expected settlement of the option.

Income Taxes

Income taxes, which requires judgment to determine when deferred income tax assets are recognized based on various factors including our history of losses.

Significant Accounting Standards Adopted and Issued But Not Effective

Accounting standards adopted in Fiscal 2017

In January 2016, the IASB issued amendments to IAS 7 Statements of Cash Flows that require additional disclosures about changes to an entity's financing liabilities arising from both cash and non-cash flow items. These changes are effective for annual periods on or after January 1, 2017. We implemented these amendments and provide disclosure in our Consolidated Financial Statements.

Accounting standards issued but not yet effective

The IASB has issued the following standards that are not yet effective and are relevant to us.

IFRS 15 — Revenue from Contracts with Customers

IFRS 15, Revenue from Contracts with Customers, was issued in May 2014 by the IASB as a replacement for IAS 18, Revenue. The Standard establishes a single, principles based five-step model to be applied to all contracts with customers and provide useful information to users of financial statements about the nature, timing, and uncertainty of revenue and cash flows arising from a contract with a customer. The Standard is effective for annual periods beginning on or after January 1, 2018. We have completed an assessment of the potential impact of the adoption of IFRS 15 on the Consolidated Financial Statements and this standard will not materially impact us.

IFRS 9 — Financial Instruments

IFRS 9, Financial Instruments, was issued in July 2014 by the IASB as a replacement for IAS 39, Financial Instruments: Recognition and Measurement. The Standard includes requirements for recognition and measurement,

impairment, derecognition, and general hedge accounting. The Standard is effective for annual periods beginning on or after January 1, 2018. We have completed our assessment on the potential impact of the adoption of IFRS 9 on the Consolidated Financial Statements and determined that this standard will not materially impact us.

IFRS 16 — Leases

IFRS 16, Leases, was issued in January 2016 by the IASB as a replacement for IAS 17, Leases. The Standard introduces a single, on-balance sheet accounting model for lessees. A lessee recognizes a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are optional exemptions for short-term leases and leases of low value items. The Standard is effective for annual periods beginning on or after January 2019. The extent of the impact of adoption of IFRS 16 has not yet been determined but conceptually will result in significant operating leases recorded on our statement of financial position.

RELATED PARTY TRANSACTIONS

HPLP transactions

HPLP is owned 30% by us and 70% by non-related third parties. We purchase industrial wood products from HPLP and earn revenue from sales of fibre and distribution fees. We manage and administer the business affairs of HPLP and charge a management fee. These transactions are at negotiated amounts with the non-related third parties.

The amounts receivable and payable to us are unsecured and non-interest bearing.

LPLP transactions

LPLP is owned 75% by us and 25% by a non-related third party. We purchase industrial wood products from LPLP and earn revenue from sales of fibre at negotiated prices with the non-related third party. We manage and administer the business affairs of LPLP.

The amounts receivable and payable to us are unsecured and non-interest bearing.

SPLP transactions

On October 4, 2017, we entered into a limited partnership with a non-related third party for the acquisition and development of a wood pellet facility. SPLP is owned 70% by us and 30% by a non-related third party. On October 13, 2017, we contributed \$5.6 million and the non-related third party contributed \$2.4 million for the purchase of land, plant and equipment, and intangible assets. On March 2, 2018, we and the non-related third party made further contributions of \$2.1 million and \$0.9 million, respectively.

Parent and ultimate controlling entity

Prior to the Offering, we were controlled by the ONCAP Entities who owned approximately 60% of the Company. The ONCAP Entities are ultimately controlled by Onex Corporation. Our remaining shareholders were former owners or current employees. During Fiscal 2017, we paid a monitoring fee to ONCAP Management Partners L.P. of \$0.5 million (2016 - \$0.5 million).

Upon the completion of our initial public offering on February 6, 2018, the ONCAP Entities own 42.9% of the Company, and the monitoring fee to ONCAP Management Partners L.P. has been discontinued.

Minority shareholder in PRHI

During Fiscal 2017, we paid market rent for the Williams Lake facility in the amount of \$0.2 million to a corporation controlled by the controlling shareholder of one of our minority shareholders, Beckman Holdings Inc., resulting from a lease agreement entered into in the normal course of business and on the same terms accorded to unrelated third parties.

See Note 21 to the Consolidated Financial Statements for additional details on related party transactions.

SHARE CAPITAL

Share Information Prior to Pre-Closing Capital Changes

Prior to the completion of the pre-closing capital changes undertaken in connection with the Offering (the “Pre-Closing Capital Changes”), our share capital consisted of the following:

- Unlimited Class A common participating, voting shares, without par value, which provide the holders an additional preferred return of 7.5% on returns upon a liquidation that is in excess of three times the invested capital.
- Unlimited Class B common participating, voting shares, without par value.
- Unlimited Class C common participating, voting shares, without par value.
- Unlimited Class D common participating, voting shares, without par value.
- Unlimited Class E preferred participating, voting shares without par value accrue cumulative dividends at 14% for the first five years after the share issuance date; thereafter dividends will be fixed and will not increase. Rate will decrease to 10% when certain operational targets are achieved, which occurred in 2014.
- Unlimited Class F preferred participating, non-voting shares without par value, accrue cumulative dividends at 4.5%. Redeemable at the option of the Company for the issuance amount plus all dividends accrued or declared and unpaid. A mandatory redemption occurs on an initial public offering for the issuance amount.
- Unlimited Class G preferred participating, non-voting shares without par value, accrue cumulative dividends at 4.5%. Redeemable at the option of the Company for the issuance amount plus all dividends accrued or declared and unpaid. A mandatory redemption occurs on an initial public offering for the issuance amount plus all dividends accrued or declared unpaid.
- Unlimited Class H preferred participating, non-voting shares without par value, accrue cumulative dividends at 3.5% and pay cash dividends at 1.5%. Redeemable at the option of the Company for the issuance amount plus all dividends accrued or declared and unpaid. A mandatory redemption occurs on an initial public offering for the issuance amount plus all dividends accrued or declared unpaid or November 30, 2020.

In summary, our issued share capital was as follows:

| As at | December 29, 2017 |
|--|----------------------------|
| Common shares | |
| 25,000,000 Class A common shares | \$25,000,000 |
| 4,500,000 Class B common shares..... | 4,500,000 |
| 5,500,000 Class B common shares presented as a liability..... | — |
| 1,000,000 Class D common shares presented as a liability | — |
| | <u>\$29,500,000</u> |
| Preferred shares | |
| 500,000 Class E preferred shares | \$500,000 |
| 19,000,000 Class F preferred shares | 19,000,000 |
| 8,600,000 Class G preferred shares..... | 8,505,000 |
| 5,004,000 Class H preferred shares presented as a liability..... | — |
| | <u>\$28,005,000</u> |

Current Share Information

In connection with the closing of the Offering, we simplified our share structure, as follows:

| Shares Outstanding prior to completion of the Pre-Closing Capital Changes | Shares Outstanding immediately following the Pre-Closing Capital Changes |
|--|---|
| 25,000,000 Class A common share | 5,831,730 common shares |
| 4,500,000 Class B common shares | 1,049,711 common shares |
| 5,500,000 Class B common shares presented as a liability | 1,282,980 common shares |
| 1,000,000 Class D common shares presented as a liability | 254,592 common shares |
| 500,000 Class E preferred shares | 36,719 common shares |
| 19,000,000 Class F preferred shares | 2,274,553 common shares |
| 8,600,000 Class G preferred shares | 982,341 common shares |
| 5,004,000 Class H preferred shares presented as a liability | 457,785 common shares |
| | |
| Upon closing of the Offering | |
| Convertible debenture payable – converted | 14,076,068 common shares |
| Share options – exercised and sold | 432,853 common shares |
| Treasury shares – issued | 6,223,889 common shares |
| | |
| Total | 32,903,221 common shares |

As of March 15, 2018, we had 32,903,221 Common Shares issued and outstanding and no preferred shares issued and outstanding. As of March 15, 2018, an aggregate of 1,694,983 options to acquire Common Shares are outstanding.

SUBSEQUENT EVENTS

We completed the Offering on February 6, 2018 and listed our Common Shares on the TSX. The Offering included a treasury offering of 6,223,889 Common Shares for gross proceeds of approximately \$70 million and a secondary offering of 7,111,111 of Common Shares from certain shareholders for gross proceeds of approximately \$80 million. Upon closing of the Offering, we received aggregate net proceeds of \$37.6 million which is net of underwriting fees of \$3.9 million and the repayment of our \$28.6 million subordinated debentures. We did not receive any of the proceeds from the secondary offering.

Prior to the completion of the Offering, the ONCAP Entities were our controlling parent. Upon completion of the Offering, the ONCAP Entities own 14,112,787 or 42.9% of the issued and outstanding Common Shares.

On February 27, 2018, the underwriters exercised the Over-Allotment Option, which was a secondary offering for \$22.5 million, from which we did not receive any proceeds.

Use of Proceeds from the Offering

The following table provides a comparison of our planned use of proceeds from the Offering, as previously disclosed in our Prospectus, and our actual use of proceeds as of the date of this MD&A.

There were no material variances from our planned use of proceeds and our actual use of proceeds as of the date of this MD&A.

(In thousands of Canadian dollars)

| Intended use | Planned (approximate) | Actual incurred (approximate) | Variances |
|--|----------------------------------|--|------------------|
| Funding for the construction of the Entwistle Facility and the Smithers Facility | \$35,000 | \$35,000 | — |
| Repayment of certain existing subordinated shareholder debt | \$28,580 | \$28,577 | \$(3) |
| General corporate expenses | \$2,588 | \$2,591 | \$3 |
| Total net proceeds from treasury offering | \$66,168 | \$66,168 | — |

Additional Information

Additional information relating to the Company is available on SEDAR at www.sedar.com. The Company's Common Shares are listed for trading on the TSX under the symbol "PL".

As at and for the years ended
December 29, 2017 and December 30,
2016

Consolidated Financial Statements



Pinnacle.
RENEWABLE HOLDINGS INC.



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INDEPENDENT AUDITORS' REPORT

To the Shareholders of Pinnacle Renewable Holdings Inc.

We have audited the accompanying consolidated financial statements of Pinnacle Renewable Holdings Inc., which comprise the consolidated statements of financial position as at December 29, 2017 and December 30, 2016, the consolidated statements of comprehensive income (loss), changes in equity and cash flows for the years then ended, and notes, comprising a summary of significant accounting policies and other explanatory information.

Management's Responsibility for the Consolidated Financial Statements

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

Auditors' Responsibility

Our responsibility is to express an opinion on these consolidated financial statements based on our audits. We conducted our audits in accordance with Canadian generally accepted auditing standards. Those standards require that we comply with ethical requirements and plan and perform the audit to obtain reasonable assurance about whether the consolidated financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the consolidated financial statements. The procedures selected depend on our judgment, including the assessment of the risks of material misstatement of the consolidated financial statements, whether due to fraud or error. In making those risk assessments, we consider internal control relevant to the entity's preparation and fair presentation of the consolidated financial statements 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. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of accounting estimates made by management, as well as evaluating the overall presentation of the consolidated financial statements. We believe that the audit evidence we have obtained in our audits is sufficient and appropriate to provide a basis for our audit opinion.



Opinion

In our opinion, the consolidated financial statements present fairly, in all material respects, the consolidated financial position of Pinnacle Renewable Holdings Inc. as at December 29, 2017 and December 30, 2016, and its consolidated financial performance and its consolidated cash flows for the years then ended in accordance with International Financial Reporting Standards.

KPMG LLP

March 15, 2018
Vancouver, Canada

**PINNACLE RENEWABLE HOLDINGS INC.**

Consolidated Statements of Financial Position
(Expressed in thousands of Canadian dollars)

| As at | December 29, 2017 | December 30, 2016 |
|---|-------------------|-------------------|
| Assets | | |
| Current assets | | |
| Cash and cash equivalents | \$ 18,908 | \$ 12,112 |
| Accounts receivable (note 4) | 41,253 | 24,746 |
| Inventory (note 5) | 17,709 | 20,422 |
| Other current assets | 3,392 | 4,460 |
| | 81,262 | 61,740 |
| Property, plant and equipment (note 6) | 238,196 | 175,849 |
| Investment in Houston Pellet Limited Partnership (note 7) | 8,916 | 8,210 |
| Other long-term assets | 51 | 228 |
| Goodwill and intangible assets (note 8) | 105,220 | 107,484 |
| | \$ 433,645 | \$ 353,511 |
| Liabilities | | |
| Current liabilities | | |
| Revolver loan (note 9) | \$ 22,000 | \$ 7,100 |
| Accounts payable and accrued liabilities | 35,653 | 42,185 |
| Current portion of term debt (note 9) | 6,000 | 1,600 |
| Other current liabilities | 15,977 | 1,075 |
| | 79,630 | 51,960 |
| Term debt (note 9) | 190,813 | 155,570 |
| Shareholders' debentures payable (note 10) | 88,881 | 76,972 |
| Common and preferred shares classified as liabilities (note 11) | 25,992 | 19,765 |
| Other long-term liabilities (note 12) | 3,457 | 2,151 |
| Deferred income taxes (note 18) | 9,668 | 9,142 |
| | 398,441 | 315,560 |
| Equity | | |
| Common shares (note 13) | 29,500 | 29,500 |
| Preferred shares (note 13) | 28,005 | 28,005 |
| Contributed surplus (note 16) | 4,332 | 4,095 |
| Equity component of convertible debentures (note 10) | 35,213 | 35,213 |
| Deficit | (75,419) | (70,182) |
| Total equity (deficit) attributable to: Owners of the Company | 21,631 | 26,631 |
| Non-controlling interests (note 14) | 13,573 | 11,320 |
| | 35,204 | 37,951 |
| | \$ 433,645 | \$ 353,511 |
| Total liabilities and equity | | |

Commitments (note 25)
Contingencies (note 26)
Subsequent events (note 29)

See accompanying notes to the consolidated financial statements

APPROVED BY THE BOARD

s/Gregory Baylin
Director, Gregory Baylin

s/Hugh MacDiarmid
Director, Hugh MacDiarmid

**PINNACLE RENEWABLE HOLDINGS INC.**

Consolidated Statements of Comprehensive Income (Loss)

(Expressed in thousands of Canadian dollars)

| Fiscal year ended | December 29, 2017 | December 30, 2016 |
|--|-------------------|-------------------|
| Revenue (notes 27 and 28) | \$ 292,727 | \$ 266,338 |
| Costs and expenses (note 15) | | |
| Production | 188,414 | 173,693 |
| Distribution | 38,421 | 39,474 |
| Selling, general and administration | 15,268 | 12,331 |
| Amortization of equipment and intangible assets | 21,819 | 21,211 |
| | 263,922 | 246,709 |
| Profit (loss) before undernoted items | 28,805 | 19,629 |
| Equity earnings in Houston Pellet Limited Partnership (note 7) | 1,381 | 5,675 |
| Loss on disposal of property, plant and equipment | (1,049) | (1,966) |
| Plant impairment loss and curtailment costs (note 6) | (4,626) | (1,591) |
| Revaluation loss on class B and D common shares (note 11) | (5,601) | (10,278) |
| Finance costs excluding shareholders' debentures (note 17a) | (11,892) | (9,244) |
| Finance (costs) income on shareholders' debentures (note 17b) | (12,359) | 8,244 |
| Other income | 983 | 364 |
| | (33,163) | (8,796) |
| Net profit (loss) before income taxes | (4,358) | 10,833 |
| Income tax (expense) (note 18) | | |
| Current | - | (2) |
| Deferred | (526) | (5,569) |
| | (526) | (5,571) |
| Net profit (loss) and comprehensive income (loss) for the year | \$ (4,884) | \$ 5,262 |
| Net profit (loss) and comprehensive income (loss) attributable to: | | |
| Owners of the Company | \$ (5,237) | \$ 4,396 |
| Non-controlling interests | 353 | 866 |
| Net profit (loss) and comprehensive income (loss) for the year | \$ (4,884) | \$ 5,262 |
| Net profit (loss) per share attributable to owners (note 19): | | |
| Basic and diluted - Class A | \$ (0.22) | \$ 0.11 |
| Basic and diluted - Class B | \$ (0.22) | \$ 0.11 |
| Weighted average of number of shares outstanding (thousands): | | |
| Class A - Basic and diluted | 25,000 | 25,000 |
| Class B - Basic and diluted | 4,500 | 4,500 |

See accompanying notes to the consolidated financial statements

**PINNACLE RENEWABLE HOLDINGS INC.**

Consolidated Statements of Equity

(Expressed in thousands of Canadian dollars)

| | Common shares (note 13) | Preferred shares (note 13) | Contributed surplus (note 16) | Convertible debentures equity (note 10) | Deficit | Non- controlling Interests (note 14) | Total equity |
|---|-------------------------------|----------------------------------|-------------------------------------|--|--------------------|---|------------------|
| Balance, December 25, 2015 | \$ 29,500 | \$ 29,005 | \$ 3,957 | \$ 26,319 | \$ (65,540) | \$ 10,754 | \$ 33,995 |
| Net profit and comprehensive income for the year | - | - | - | - | 4,396 | 866 | 5,262 |
| Stock-based compensation (note 16) | - | - | 138 | - | - | - | 138 |
| Investment by non-controlling interest | - | - | - | - | - | 500 | 500 |
| Cash distributions to non-controlling interest | - | - | - | - | - | (800) | (800) |
| Shares repurchased | - | (1,000) | - | - | - | - | (1,000) |
| Dividends | - | - | - | - | (144) | - | (144) |
| Adjustment to convertible debentures equity on modification (note 10) | - | - | - | 8,894 | (8,894) | - | - |
| Balance, December 30, 2016 | \$ 29,500 | \$ 28,005 | \$ 4,095 | \$ 35,213 | \$ (70,182) | \$ 11,320 | \$ 37,951 |
| Net profit (loss) and comprehensive income (loss) for the year | - | - | - | - | (5,237) | 353 | (4,884) |
| Cash distributions to non-controlling interest | - | - | - | - | - | (500) | (500) |
| Investment by non-controlling interest | - | - | - | - | - | 2,400 | 2,400 |
| Stock-based compensation (note 16) | - | - | 237 | - | - | - | 237 |
| Balance, December 29, 2017 | \$ 29,500 | \$ 28,005 | \$ 4,332 | \$ 35,213 | \$ (75,419) | \$ 13,573 | \$ 35,204 |

See accompanying notes to the consolidated financial statements

**PINNACLE RENEWABLE HOLDINGS INC.**

Consolidated Statements of Cash Flows
(Expressed in thousands of Canadian dollars)

| Fiscal year ended | December 29, 2017 | December 30, 2016 |
|--|-------------------|-------------------|
| Cash provided by (used in) | | |
| Operating activities | | |
| Net profit (loss) for the year | \$ (4,884) | \$ 5,262 |
| Finance costs excluding shareholders' debentures | 11,892 | 9,244 |
| Finance costs (income) on shareholders' debentures | 12,359 | (8,244) |
| | 19,367 | 6,262 |
| Items not involving cash | | |
| Amortization of property, plant and equipment (note 6) | 18,904 | 18,242 |
| Amortization of intangible assets (note 8) | 2,915 | 2,971 |
| Equity earnings in Houston Pellet Limited Partnership (note 7) | (1,381) | (5,675) |
| Loss on disposal on property, plant and equipment | 1,049 | 1,966 |
| Impairment loss on property, plant and equipment (note 6) | 3,245 | - |
| Stock-based compensation | 237 | 138 |
| Inventory write-down | - | 75 |
| Loss on disposal of shares | - | 572 |
| Revaluation loss of class B and D common shares (note 11) | 5,601 | 10,278 |
| Income tax expense | 526 | 5,571 |
| Other | (10) | (243) |
| Distributions from Houston Pellet Limited Partnership | 675 | 4,575 |
| Income tax received | - | 10 |
| | 51,128 | 44,742 |
| Net change in non-cash operating working capital (note 20) | (20,183) | (14,126) |
| | 30,945 | 30,616 |
| Financing activities | | |
| Issuance of revolver loan | 14,900 | 7,100 |
| Issuance of term debt | 180,000 | 161,786 |
| Repayment of term debt | (160,000) | (178,690) |
| Issuance of delayed draw loan | 20,000 | - |
| Issuance of Class D common shares | 550 | - |
| Shareholders' debentures payable | - | 5,266 |
| Investment from non-controlling interest | 2,400 | 500 |
| Distributions to non-controlling interest | (500) | (800) |
| Payment of finance leases | (198) | (99) |
| Finance costs paid | (8,340) | (16,021) |
| | 48,812 | (20,958) |
| Investing activities | | |
| Purchase of intangible assets | (651) | - |
| Purchase of property, plant and equipment (note 20) | (72,056) | (13,350) |
| Proceeds from sale of property, plant and equipment | 25 | 100 |
| | (72,682) | (13,250) |
| Foreign exchange gain (loss) on cash position held in foreign currency | (279) | 68 |
| Increase (decrease) in cash | 6,796 | (3,524) |
| Cash position, beginning of year | 12,112 | 15,636 |
| Cash position, end of year | \$ 18,908 | \$ 12,112 |

See accompanying notes to consolidated financial statements



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

1. Reporting entity

Pinnacle Renewable Holdings Inc. (the “Company”), was incorporated on December 6, 2010 under the laws of the Province of British Columbia and is domiciled in Canada. The Company’s registered office is at 350 - 3600 Lysander Lane, Richmond, British Columbia.

The Company is primarily involved in the manufacture and sale of wood pellets for both industrial electrical power generation and home heating consumption in North America, Asia and Europe. The Company operates facilities at various locations in the Province of British Columbia including Quesnel, Armstrong, Williams Lake, Burns Lake, Meadowbank, Houston and Lavington. The Company also owns and operates the Westview port facility at Prince Rupert for the storage, handling and loading of the Company's and third party wood pellets. The Company is currently constructing a plant in Entwistle, Alberta and has started development of a plant in Smithers, British Columbia.

Subsequent to December 29, 2017, the Company completed an Initial Public Offering and Secondary Offering and became a listed entity in Canada (see note 29).

2. Basis of preparation

a) Statement of compliance and basis of measurement

These consolidated financial statements have been prepared in accordance with International Financial Reporting Standards (“IFRS”) and its interpretations issued by the International Accounting Standards Board (“IASB”). The consolidated financial statements were authorized for issue by the Board of Directors on March 15, 2018.

These consolidated financial statements have been prepared on the historical cost convention except for certain financial liabilities and derivative instruments which are stated at fair value with changes in fair value recognized in net profit (loss).

b) Basis of consolidation

The consolidated financial statements include the accounts of the Company’s wholly-owned subsidiaries, its majority-owned subsidiaries and its ownership in its equity investment as follows:

| | Country of residence | Economic ownership | Voting % | Method of accounting |
|--------------------------------------|----------------------|--------------------|----------|----------------------|
| Pinnacle Renewable Energy Inc. | Canada | 100% | 100% | Consolidated |
| Pinnacle Pellet Houston Inc. | Canada | 100% | 100% | Consolidated |
| Houston Pellet Inc. | Canada | 33% | 33% | Equity |
| Houston Pellet Limited Partnership | Canada | 30% | 30% | Equity |
| Lavington Pellet Inc. | Canada | 75% | 75% | Consolidated |
| Lavington Pellet Limited Partnership | Canada | 75% | 75% | Consolidated |
| Smithers Pellet Inc. | Canada | 70% | 70% | Consolidated |
| Smithers Pellet Limited Partnership | Canada | 70% | 70% | Consolidated |



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

2. Basis of preparation (continued)

c) Functional currency

These consolidated financial statements are presented in Canadian dollars, which is the Company's functional currency as it is the primary economic environment in which it operates.

d) Use of estimates and judgments

The preparation of 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 and liabilities, earnings and expenses. Actual results could differ from those estimates.

Estimates and underlying assumptions are reviewed on an ongoing basis. Revisions to estimates are recognised prospectively.

Judgments

Information about judgments made in applying accounting policies that have the most significant effects on the amounts recognised in the consolidated financial statements is included in the following notes:

Note 8 – Goodwill: determination of appropriate cash generating units; and,

Note 25 – Commitments, Leases: whether an arrangement contains a lease.

Assumptions about estimation uncertainties

Information about assumptions and estimation uncertainties that have a significant risk of resulting in a material adjustment to the carrying amounts of assets and liabilities within the year ending December 29, 2017 is included in the following notes:

Note 5 – measurement of net realizable value of inventory: key fibre volume measurement assumptions;

Note 8 – impairment test of goodwill: key assumptions underlying recoverable amounts;

Note 10 – determination of the fair value of debt and equity components of convertible debentures on the basis of significant unobservable inputs;

Note 11 – determination of the fair value of common shares classified as liabilities on the basis of significant unobservable inputs;

Note 12 – Recognition and measurement of provisions: key assumptions about the likelihood and magnitude of an outflow of resources; and,

Note 18 – recognition of deferred tax assets: availability of future taxable profit against which tax losses carried forward can be used.



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

3. Significant accounting policies

The accounting policies set out below have been applied consistently to all periods presented in these consolidated financial statements. All accounting policies have been applied consistently by the Company, its subsidiaries and associates.

Certain comparative amounts in the consolidated statements of net profit (loss) have been reclassified to conform with the current year's presentation.

a) Subsidiaries

The Company's determination of its subsidiaries is based on its control of entities that are subject to consolidation and reflects its continuing power to determine their strategic operating, investing and financing policies without the co-operation of others, in a manner that would earn the Company the right and ability to obtain future economic benefits from these entities and exposes the Company to the related risks. The financial statements of subsidiaries are included in the consolidated financial statements from the date that control commences until the date that control ceases.

b) Non-controlling interests

For non wholly owned controlled subsidiaries, the net assets attributable to the outside equity shareholders are presented as non-controlling interests in the equity section of the consolidated statement of financial position. Profit or loss for the period that is attributable to non-controlling interests is calculated based on the ownership of the minority shareholders in the subsidiary.

c) Investment in associates (equity accounted investees)

Associates are those entities in which the Company has significant influence, but does not control the strategic financing, investing and operating policies. Significant influence is presumed to exist when the Company holds between 20 and 50 percent of the voting power of another entity. Investments in associates are accounted for initially at cost and subsequently using the equity method, whereby the investment is adjusted for post-acquisition earnings and equity transactions, from the date that significant influence commences until the date that significant influence ceases. When the Company's share of losses exceeds its interest in an equity accounted investee, the carrying amount of that interest, including any long-term investments, is reduced to nil, and the recognition of further losses is discontinued except to the extent that the Company has an obligation to fund the investee's operations or has made payments on behalf of the investee.

d) Transactions eliminated on consolidation

Inter-company balances and transactions as well as any unrealized income and expenses arising from Inter-company transactions are eliminated in the consolidated financial statements. Unrealized gains arising from transactions with equity accounted investees are eliminated against the investment to the extent of the Company's interest in the investee. Unrealized losses are eliminated in the same way as unrealized gains, but only to the extent that there is no evidence of impairment.



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

3. Significant accounting policies (continued)

e) Foreign currency translation

Transactions in foreign currencies are translated to the functional currency at exchange rates on the dates of transactions. Monetary assets and liabilities denominated in foreign currencies at the reporting date are translated to the functional currency at the exchange rate on that date. Non-monetary assets and liabilities denominated in foreign currencies are translated at historic rates. Foreign currency differences arising on translation are recognized in net profit (loss).

f) Cash and cash equivalents

Cash and cash equivalents include cash in bank accounts and deposits with original maturities of three months or less from the date of acquisition.

g) Accounts receivable

Accounts receivable are measured at cost. The Company evaluates accounts receivable for impairment to determine if an allowance for doubtful accounts is required. A specific allowance is recorded against customer receivables based on the evaluation of the customers' credit worthiness and knowledge of their financial condition. The provision expense is included in selling, general and administration cost in net profit (loss). When a receivable is considered permanently uncollectible, the receivable is written off against the allowance account.

h) Inventory

Inventories of fibre, finished wood pellets, supplies and spare parts are measured at the lower of cost and net realizable value. The cost of inventories is based on the weighted average cost principle, and includes all direct costs incurred in production and conversion including raw materials, labour and direct overhead and other costs incurred in bringing the inventories to their existing condition and location. The cost of manufactured inventories includes production overhead based on normal operating capacity. Costs that do not contribute to bringing inventories to their present condition and location, such as storage and administration overhead, are excluded from the cost of inventories and expensed as incurred.

The Company estimates net realizable value as the amount inventories are expected to be sold for less estimated costs for completion and costs necessary to make the sale. In determining net realizable value, factors such as obsolescence and damage, aging of, and future demand for, the inventory, selling prices, and contractual arrangements with customers are considered. A change to these assumptions could impact the inventory valuation and resulting impact on gross margins. Inventories are written down to net realizable value when their cost is not deemed to be recoverable. When circumstances that previously caused inventories to be written down below cost no longer exist, including when there is clear evidence of an increase in selling price, the amount of the write-down previously recorded is reversed.



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

3. Significant accounting policies (continued)

i) Property, plant and equipment

Property, plant and equipment are stated at cost less accumulated amortization and any impairment losses. Cost consists of expenditures directly attributable to the acquisition of the asset. The cost of self-constructed assets includes the cost of materials and direct labour, any other costs directly attributable to bringing the assets to working condition for their intended use, the costs of dismantling and removing the items and restoring the site on which they are located and borrowing costs on qualifying assets. Costs are capitalized when economic benefits associated with that asset are probable and cost can be measured reliably. Borrowing costs that are directly attributable to the acquisition, construction or production of a qualifying asset are capitalized. All other repairs and maintenance costs are expensed as incurred.

Amortization is provided over the estimated useful lives on a straight-line basis starting when the asset is available for use. Construction in progress is not subject to amortization until the assets are put into use. Leased assets are amortized over the shorter of their lease term and their useful lives, unless it is reasonably certain the Company will obtain ownership by the end of the lease term. Land is not amortized. Amortization is recorded over the following terms:

| Asset | Term |
|--|---|
| Buildings and related assets | 20 years |
| Production machinery and other equipment | 3-20 years |
| Mobile equipment | 5 years |
| Leasehold improvements | Shorter of the lease term and the useful life |

When components of an asset have significantly different useful lives than the primary asset, the components are amortized separately. Residual values, useful lives and methods of amortization are reviewed annually and adjusted prospectively. Gains and losses on the disposal or retirement of property, plant and equipment are determined by comparing net proceeds from disposal with the carrying amount of the asset and are recognized in profit (loss).

j) Leases

Leases where the Company has assumed substantially all the risks and rewards of ownership are classified as finance leases. Finance leases are capitalized at the lease commencement date at the lower of fair value of the leased asset and present value of the minimum lease payments. Subsequent to initial recognition, the leased asset is accounted for in accordance with the accounting policy applicable to its underlying nature.

Leases in which a significant portion of the risks and rewards are retained by the lessor are classified as operating leases. Payments under operating leases are recognized in the Company's net profit (loss).



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

3. Significant accounting policies (continued)

k) Goodwill

Goodwill represents the excess of the cost of a business acquisition over the fair value of the acquired identifiable net assets at the date of acquisition.

l) Intangible assets

Intangible assets are recorded at their fair values at the date of acquisition. For all limited life intangible assets, amortization is provided for on a straight-line basis over their estimated useful lives as follows:

| Asset | Estimated useful life |
|------------------------|-----------------------|
| Customer relationships | 9 years |
| Supply agreements | 9 years |
| Other | 5 years |

Residual values, useful lives and methods of amortization are reviewed periodically and adjusted prospectively.

m) Impairment

Non-financial assets

At each reporting date, the Company reviews the carrying amounts of its non-financial assets (other than inventories and deferred tax assets) to determine whether there is any indication of impairment. If any such indication exists, then the asset's recoverable amount is estimated. Goodwill is tested annually for impairment.

For impairment testing, assets are grouped together into the smallest group of assets that generates cash inflows from continuing use that are largely independent of the cash inflows of other assets or cash generating units ("CGU"). Goodwill arising from a business combination is allocated to CGUs or groups of CGUs that are expected to benefit from the synergies of the combination

The recoverable amount of an asset or CGU is the greater of its value in use and its fair value less costs to sell. Value in use is based on the estimated future cash flows, 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 or CGU.

An impairment loss is recognized if the carrying amount of an asset or CGU exceeds its recoverable amount. Impairment losses are recognised in net profit (loss). They 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 of goodwill is not reversed. For other assets, an impairment loss is reversed only to the extent that the asset's carrying amount does not exceed the carrying amount that would have been determined, net of depreciation or amortisation, if no impairment loss had been recognized.



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

3. Significant accounting policies (continued)

m) Impairment (continued)

Financial assets

Financial assets not carried at fair value through profit (loss), including an interest in an equity investee, are assessed at each reporting date to determine whether there is objective evidence of impairment. An impairment loss in respect of a financial asset measured at amortized cost is calculated as the difference between the carrying amount and the present value of the estimated future cash flows discounted at the asset's original effective interest rate. When an event occurs after the impairment was recognized that causes the amount of impairment loss to decrease, the decrease in impairment loss is recognized in net profit (loss).

n) Income taxes

Income tax expense comprises current and deferred income taxes. Tax is recognized in the consolidated statement of net profit (loss), except to the extent that it relates to a business combination or items recognized directly in equity, in which case the tax effect is also recognized in equity.

Current income tax expense or recovery is based on the expected tax payable or receivable on the taxable income or loss using the enacted or substantively enacted tax rate applicable to that profit or loss.

Deferred income taxes are recorded using the asset and liability method of income tax allocation. Under this method, deferred income tax is recognized on the temporary differences between the carrying amounts of assets and liabilities for financial reporting purposes and the amounts used for taxation purposes. Deferred income tax is measured at tax rates expected to be applied to the temporary differences when they reverse, based on the laws that have been enacted or substantively enacted by the reporting date. The effect of a change in the income tax rates is included in net profit (loss) in the period in which the rate change occurs.

Deferred income tax assets are recognized only to the extent that it is probable that future taxable profit will be available to utilize the tax losses, tax credit carry-forwards and deductible temporary differences.

Deferred tax assets and liabilities are offset if there is a legally enforceable right to offset current tax liabilities and assets and they relate to taxes levied by the same tax authority on the same taxable entity or on different tax entities, if there is intention to settle current tax liabilities and assets on a net basis, otherwise tax assets and liabilities will be realized simultaneously.

o) Provisions

A provision is a liability of uncertain timing or amount and is generally recognized when the Company has a present legal or constructive obligation as a result of a past significant event, it is probable that payment will be made to settle the obligation and the payment can be estimated reliably. Provisions are determined by discounting the expected future cash flows at a pre-tax rate that reflects current market assessments of the time value of money and the risks specific to the liability. The unwinding of the discount is recognized as a finance cost.



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

3. Significant accounting policies (continued)

p) Decommissioning liabilities

Legal or contractual obligations to retire tangible long-lived assets are recorded in the period in which they are incurred with a corresponding increase in asset value. These include assets leased under operating leases. The liability is accreted over the life of the asset to fair value and the increase in asset value is depreciated over the remaining useful life of the asset. Decommissioning liabilities are discounted at the risk-free rate in effect at the reporting date.

q) Revenue recognition

Revenue from finished wood pellet sales is measured at the fair value of the consideration received or receivable (net of returns, trade discounts and volume rebates) and when the risks and rewards of ownership are transferred to the customer, which is generally when the product is loaded on the shipping vessel. Revenue is recognized when persuasive evidence exists, usually in the form of an executed sales agreement, that significant risks and rewards of ownership have been transferred to the buyer and there is no continuing management involvement with the goods, collection of the relevant consideration is probable, the revenue can be measured reliably, and associated costs and possible return of goods can be estimated reliably, all of which generally precede products being loaded.

Amounts charged to customers for shipping and handling are recognized as revenue, and shipping and handling costs incurred by the Company are reported as a component of distribution costs.

r) Financial instruments

Non-derivative financial instruments

Non-derivative financial instruments consist of cash, trade and other receivables, loans and borrowings, trade and other payables, debentures payable, and common and preferred shares classified as liabilities. Non-derivative financial instruments are recognized initially at fair value plus, for instruments not at fair value through net profit (loss), any directly attributable transaction costs.

Subsequent to initial recognition, non-derivative financial instruments are measured as described below:

- Loans and receivables – Loans and receivables are non-derivative financial assets with fixed or determinable payments that are not quoted in an active market. These are measured at amortized cost using the effective interest method, less any impairment losses. The effective interest method is used to recognize the total costs of or profit from a financial instrument over the life of the instrument. Cash and cash equivalents and accounts receivable are included in this category.
- Financial liabilities at fair value through net profit (loss) – An instrument is classified at fair value through net profit (loss) if it is held for trading or is designated as such upon initial recognition. Financial instruments at fair value through net profit are measured at fair value, and changes therein are recognized in net profit (loss), with attributable transaction costs being recognized in net profit (loss) when incurred. The management held Class B and Class D common shares liability is included in this category.



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

3. Significant accounting policies (continued)

r) Financial instruments (continued)

- Financial liabilities measured at amortized cost – Financial liabilities not classified as fair value through net profit (loss) are recorded at amortized cost using the effective interest rate method. Accounts payable and accrued liabilities, revolver loan and term debt, and shareholders' debentures payable are included in this category. Deferred financing costs relating to the issuance of financial liabilities measured at amortized costs are recorded as a reduction to the cost of the related debt which is amortized to net profit (loss) using the effective interest rate method.

Derivative financial instruments

The Company uses derivative financial instruments in the normal course of its operations as a means to manage its foreign exchange and interest rate risk. Foreign currency forward contracts may be used to limit exposure on U.S. dollar sales. Interest rate swaps may be used to fix a portion of the floating rate debt. The Company's policy is not to utilize derivative financial instruments for trading or speculative purposes.

The Company's derivative financial instruments are not designated as hedges for accounting purposes. Consequently, such derivatives for which hedge accounting is not applied are carried on the consolidated statement of financial position at fair value, with changes in fair value (realized and unrealized) being recognized in net profit (loss). The fair value of the derivatives is determined with reference to period-end market trading prices for derivatives with comparable characteristics.

Embedded derivatives are separated from the host contract and accounted for separately if the economic characteristics and risks of the host contract and the embedded derivative are not closely related, a separate instrument with the same terms as the embedded derivative would meet the definition of a derivative, and the combined instrument is not measured through net profit (loss). Separable embedded derivatives are measured at fair value with changes recognized immediately through net profit (loss).

Compound financial instruments

Compound financial instruments include convertible debentures that are convertible to Class C common shares at the option of the holder. The liability of the compound financial instrument is initially recognized at the fair value of a similar liability that does not have an equity conversion option. The equity component is initially recognized at its estimated fair value using an option valuation model. Any directly attributable transaction costs are allocated to the liability and equity components in proportion to their initial carrying amounts.

Subsequent to initial recognition, the liability component is measured at amortized cost using the effective interest rate method. The interest is recognized in the Company's net profit (loss).



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

3. Significant accounting policies (continued)

s) Finance costs

Finance costs consist of borrowing costs, unwinding of discounts on non-financial assets and liabilities, changes in the fair value of financial assets and liabilities at fair value through net profit (loss), impairment losses recognized on financial assets, foreign exchange gains (losses), and gains (losses) on derivatives. Borrowing costs that are not directly attributable to the acquisition, construction or production of a qualifying asset are recognized in net profit (loss) using the effective interest method. Qualifying assets are those that take a substantial period of time to be made ready for their intended use and generally those that are related to major developments or construction projects. Foreign exchange gains and losses are reported on a net basis.

t) Business combinations

The Company uses the acquisition method to account for business combinations. All identifiable assets, liabilities and contingent liabilities acquired are recorded at the date of acquisition at their respective fair values. One of the most significant estimates relates to the determination of the fair value of these assets and liabilities. Longer term assets, which may include land, buildings and equipment, are independently appraised or estimated based on similar appraisals. When intangible assets are identified, depending on the type of intangible asset and the complexity of determining its fair value, an independent external valuation expert develops the fair value, using appropriate valuation techniques which are generally based on a forecast of the total expected future net cash flows. These evaluations are linked closely to the assumptions made by management regarding the future performance of the assets concerned and any changes in the discount rate applied. Acquisition-related costs are expensed as incurred through net profit (loss).

u) Share capital

Common shares are classified as equity. If there are features within the common shares that create a liability upon triggering events outside of the Company's control, the common shares are presented as a liability.

Preferred shares are classified as equity if they are non-redeemable, or redeemable only at the Company's option, and any dividends are discretionary. Dividends thereon are recognized as distributions within equity. Otherwise, preferred shares are classified as liabilities and dividends recorded as interest expense.

Incremental costs directly attributable to the issue of share capital classified as equity and stock-based payments are recognized as a deduction from equity, net of any tax effects for those shares presented as equity, and as a finance cost for those shares presented as liabilities.

v) Stock-based compensation

The Company has a stock option plan as described in Note 16. Compensation expense is recognized based on the fair value at the grant date over the vesting period. The expense is adjusted to reflect the number of awards for which the related service and non-market vesting conditions are expected to be met, such that the amount ultimately recognized as an expense is based on the number of awards that do meet the related service and non-market performance conditions at the vesting date.



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

3. Significant accounting policies (continued)

w) Earnings per share

The Company calculates basic net profit (loss) per share by dividing net profit (loss) attributable to owners by the weighted average number of common shares outstanding and calculates diluted net profit (loss) per share under the treasury stock method. Under the treasury stock share method, diluted net profit (loss) is calculated by considering the dilution that would occur if stock options or other convertible instruments were converted into shares.

x) Accounting standards adopted in 2017

In January 2016, the IASB issued amendments to IAS 7 *Statements of Cash Flows* that require additional disclosures about changes to an entity's financing liabilities arising from both cash and non-cash flow items. These changes are effective for annual periods on or after January 1, 2017. The Company implemented these amendments and provides disclosure in these consolidated financial statements.

y) Accounting standards issued but not yet effective

The IASB has issued the following standards that are not yet effective and are relevant to the Company.

IFRS 15 – Revenue from Contracts with Customers

IFRS 15, Revenue from Contracts with Customers, was issued in May 2014 by the IASB as a replacement for IAS 18, Revenue. The Standard establishes a single, principles based five-step model to be applied to all contracts with customers and provide useful information to users of financial statements about the nature, timing, and uncertainty of revenue and cash flows arising from a contract with a customer. The Standard is effective for annual periods beginning on or after January 1, 2018. The Company has completed an assessment of the potential impact of the adoption of IFRS 15 on its consolidated financial statements and this standard will not materially impact the Company.

IFRS 9 – Financial Instruments

IFRS 9, Financial Instruments, was issued in July 2014 by the IASB as a replacement for IAS 39, Financial Instruments: Recognition and Measurement. The Standard includes requirements for recognition and measurement, impairment, derecognition, and general hedge accounting. The Standard is effective for annual periods beginning on or after January 1, 2018. The Company has completed its assessment on the potential impact of the adoption of IFRS 9 on its consolidated financial statements and this standard will not materially impact the Company.

IFRS 16 – Leases

IFRS 16, Leases, was issued in January 2016 by the IASB as a replacement for IAS 17, Leases. The Standard introduces a single, on-balance sheet accounting model for lessees. A lessee recognizes a right-of-use asset representing its right to use the underlying asset and a lease liability representing its obligation to make lease payments. There are optional exemptions for short-term leases and leases of low value items. The Standard is effective for annual periods beginning on or after January 2019. The extent of the impact of adoption of IFRS 16 has not yet been determined but conceptually will result in significant operating leases recorded on the Company's statement of financial position.



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

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(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

4. Accounts receivable

| As at | December 29, 2017 | December 30, 2016 |
|---|-------------------|-------------------|
| Trade accounts receivable | \$ 14,503 | \$ 17,189 |
| Other receivables | 25,965 | 6,454 |
| Amounts receivable from related parties (note 21) | 785 | 1,103 |
| | \$ 41,253 | \$ 24,746 |

Included in other receivables is \$14,590 (2016 - \$5,046) of accrued sales which were invoiced in early January.

5. Inventory

| As at | December 29, 2017 | December 30, 2016 |
|--------------------------|-------------------|-------------------|
| Wood pellets | \$ 6,479 | \$ 7,900 |
| Fibre | 6,764 | 8,639 |
| Supplies and spare parts | 4,466 | 3,883 |
| | \$ 17,709 | \$ 20,422 |

The measurement of inventory involves the use of assumptions and estimates including volume measurement of fibre inventory by external surveyors, conversion factors, composition, contamination estimates and other factors. Management has assessed that, considering the sources of uncertainty; valuation of fibre inventory is expected to be reasonably accurate within +/- 10%.

The above inventory balances include adjustments to measurement estimates and to net realizable value which results in write-ups and write-downs. In the year ended December 29, 2017, inventory reflects a net write-up of \$594 (2016 - write-down of \$1,464). These adjustments are included in production costs in net profit (loss).

**PINNACLE RENEWABLE HOLDINGS INC.**

Notes to the Consolidated Financial Statements

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(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

6. Property, plant and equipment

| | Land and buildings | Machinery and other equipment | Construction in progress | Leasehold improvements | Total |
|---|-----------------------|-------------------------------------|-----------------------------|---------------------------|-------------------|
| Balance, beginning of fiscal year | \$ 45,933 | \$ 108,550 | \$ 3,204 | \$ 18,162 | \$ 175,849 |
| Additions | 6,632 | 3,004 | 75,934 | - | 85,570 |
| Amortization | (2,928) | (14,787) | - | (1,189) | (18,904) |
| Disposals and retirements | - | (1,058) | - | (16) | (1,074) |
| Impairment loss | (1,000) | (2,245) | - | - | (3,245) |
| Transfer from construction in progress | 725 | 9,625 | (10,721) | 371 | - |
| Balance, December 29, 2017 | \$ 49,362 | \$ 103,089 | \$ 68,417 | \$ 17,328 | \$ 238,196 |
| Cost | \$ 66,654 | \$ 183,483 | \$ 68,417 | \$ 22,590 | \$ 341,144 |
| Accumulated amortization | (17,292) | (80,394) | - | (5,262) | (102,948) |
| Balance, December 29, 2017 | \$ 49,362 | \$ 103,089 | \$ 68,417 | \$ 17,328 | \$ 238,196 |

| | Land and buildings | Machinery and other equipment | Construction in progress | Leasehold improvements | Total |
|---|-----------------------|-------------------------------------|-----------------------------|---------------------------|-------------------|
| Balance, beginning of fiscal year | \$ 49,898 | \$ 117,726 | \$ 738 | \$ 18,900 | \$ 187,262 |
| Additions | - | 879 | 10,604 | - | 11,483 |
| Amortization | (2,880) | (14,195) | - | (1,167) | (18,242) |
| Disposals and retirements | (2,544) | (2,110) | - | - | (4,654) |
| Transfer from construction in progress | 1,459 | 6,250 | (8,138) | 429 | - |
| Balance, December 30, 2016 | \$ 45,933 | \$ 108,550 | \$ 3,204 | \$ 18,162 | \$ 175,849 |
| Cost | \$ 59,297 | \$ 170,908 | \$ 3,204 | \$ 22,219 | \$ 255,628 |
| Accumulated amortization | (13,364) | (62,358) | - | (4,057) | (79,779) |
| Balance, December 30, 2016 | \$ 45,933 | \$ 108,550 | \$ 3,204 | \$ 18,162 | \$ 175,849 |

See note 20 for supplemental cash flow information.

During the year ended December 29, 2017, capitalized borrowing costs related to construction in progress amounted to \$940 (2016 - nil) with an average capitalization rate of 4.8% for 2017.

On September 25, 2017, the Company made the decision to permanently close its Quesnel plant due to current market conditions, principally due to regional fibre availability. The Company reviewed the assets of the Quesnel plant to determine the recoverable value and recognized an impairment loss of \$3,245. As at December 29, 2017, the Quesnel plant has a net book value of \$802 (2016 - \$5,085). In 2017, the Company expensed \$1,381 (2016 - \$1,591) to maintain the assets while the Company evaluates its future action.

**PINNACLE RENEWABLE HOLDINGS INC.**

Notes to the Consolidated Financial Statements

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7. Investment in Houston Pellet Limited Partnership (“Houston Pellet LP”)

Houston Pellet LP manufactures wood pellets for sale to external customers and the Company. The investment in Houston Pellet LP has been accounted for under the equity basis. The following table summarizes the financial information of Houston Pellet LP and reconciles the Company’s carrying value and its share of net profit (loss):

| Percentage ownership interest | 30% | 30% |
|--|--------------------------|-------------------|
| As at | December 29, 2017 | December 30, 2016 |
| Current assets | \$ 17,616 | \$ 15,595 |
| Non-current assets | 8,544 | 8,885 |
| Current liabilities | (2,516) | (3,189) |
| Net assets | \$ 23,644 | \$ 21,291 |
| Company's share of net assets | 7,093 | 6,387 |
| Goodwill | 1,823 | 1,823 |
| Investment in Houston Pellet LP | \$ 8,916 | \$ 8,210 |

| Fiscal year ended | December 29, 2017 | December 30, 2016 |
|--|--------------------------|-------------------|
| Revenue | \$ 30,750 | \$ 28,501 |
| Expense | (24,503) | (22,785) |
| Amortization | (1,337) | (1,762) |
| Gain on settlement of legal claims | - | 16,250 |
| Loss on disposal of property and equipment | (308) | (1,288) |
| Net Profit | 4,602 | 18,916 |
| Company's share of net profit | \$ 1,381 | \$ 5,675 |

On June 28, 2016, Houston Pellet LP settled various legal claims with a logistics terminal located in Northern British Columbia related to unloading, storage, handling and shipping services for wood pellets manufactured by Houston Pellet LP. Settlement funds of \$16,250 were paid to Houston Pellet LP in the third quarter of 2016. Certain machinery and equipment involved in the settlement were impaired resulting in approximately \$800 in impairment charges recorded by Houston Pellet LP.



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8. Goodwill and Intangible Assets

| | Goodwill | Customer relationships | Supply agreements | Other | Total |
|--|------------------|------------------------|-------------------|---------------|-------------------|
| Balance, December 25, 2015 | \$ 97,482 | \$ 7,261 | \$ 5,274 | \$ 438 | \$ 110,455 |
| Additions | - | - | - | - | - |
| Amortization | - | (1,696) | (1,231) | (44) | (2,971) |
| Balance, December 30, 2016 | 97,482 | 5,565 | 4,043 | 394 | 107,484 |
| Additions | - | - | 651 | - | 651 |
| Amortization | - | (1,663) | (1,209) | (43) | (2,915) |
| Balance, December 29, 2017 | \$ 97,482 | \$ 3,902 | \$ 3,485 | \$ 351 | \$ 105,220 |
| At December 30, 2016 | | | | | |
| Cost | \$ 97,482 | \$ 15,000 | \$ 10,900 | \$ 779 | \$ 124,161 |
| Accumulated amortization | - | (9,435) | (6,857) | (385) | (16,677) |
| Net book value at December 30, 2016 | \$ 97,482 | \$ 5,565 | \$ 4,043 | \$ 394 | \$ 107,484 |
| At December 29, 2017 | | | | | |
| Cost | \$ 97,482 | \$ 15,000 | \$ 11,551 | \$ 779 | \$ 124,812 |
| Accumulated amortization | - | (11,098) | (8,066) | (428) | (19,592) |
| Net book value at December 29, 2017 | \$ 97,482 | \$ 3,902 | \$ 3,485 | \$ 351 | \$ 105,220 |

The Company as a whole is identified as the CGU to which goodwill has been assigned. The recoverable amount of the Company represents its enterprise value which is a weighted average of the Company's discounted future cash flows and a valuation determined on market based earnings multiples. The discounted cash flow is based on the Company's long-term forecast from 2018 – 2022 including the estimated impact of future capital projects and a terminal value calculated at a perpetual growth rate of 2.5% (2016 - 2.5%) beyond 5 years. The estimate of future cash flows requires management to make assumptions based on existing customer and supplier contracts, future production levels and operating and capital costs. The discount rate applied in 2017 ranged from 10.3% - 12.8% (2016 - 10.1% to 12.6%) and is based on the Company's estimate of its cost of capital. The market based earnings multiples are those of current multiples of comparable companies in the pellet, renewable energy and forestry sectors.

Changes in any of the assumptions or estimates used in determining the recoverable value could impact the impairment analysis. Based on management's analysis, no impairment of goodwill was identified in 2017 or 2016.



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

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9. Revolver loan and term debt

| As at | December 29, 2017 | December 30, 2016 |
|--------------------------------|-------------------|-------------------|
| Revolver loan (a) | \$ 22,000 | \$ 7,100 |
| Non-revolving loans | | |
| Term loan (b) | 180,000 | 160,000 |
| Delayed draw term loan (c) | 20,000 | - |
| | 222,000 | 167,100 |
| Less: | | |
| Current portion | (6,000) | (1,600) |
| Revolver loan shown as current | (22,000) | (7,100) |
| Deferred financing costs | (3,187) | (2,830) |
| | \$ 190,813 | \$ 155,570 |

On December 13, 2017, the Company amended its senior secured debt (existing term loan, delayed draw term loan, and revolving operating line). The amended facility from nine lenders through a syndicated loan agreement provides up to a \$50,000 revolving operating line, a \$200,000 term loan, and a \$130,000 delayed draw term loan (the "Facility"). The Facility has a maturity date of December 13, 2022.

Advances under the Facility are available as Canadian dollar Prime-Based Loans, Banker's Acceptances ("BA") from the BA Lenders in Canadian dollars, BA Equivalent Loans from the Non-BA Lenders in Canadian dollars, US dollar Base Rate Loans, and LIBOR Loans in US dollars. Interest accrues daily and is payable monthly at the applicable Bank Prime, BA, US Base or LIBOR rates plus a margin. The margin varies based on the ratio of Senior Debt to Adjusted EBITDA with a minimum margin of 1.50% and 2.50% for Prime/US Base and BA/LIBOR loans, respectively and a maximum margin of 3.00% and 4.00%, respectively.

At December 29, 2017, the \$180,000 term loan and the revolver loan were in Canadian dollar Prime loans at 5.70% and the \$22,000 delayed draw term loan was in a Canadian dollar BA loan at 4.86%. At December 30, 2016, the \$160,000 term loan was in a Canadian dollar BA loan at 4.42% and the revolver loan was in a Canadian dollar Prime loan at 5.20%. At December 29, 2017, the Company had issued letters of credit totaling \$530 (2016 - \$405).

EBITDA and Adjusted EBITDA are defined in the Facility agreement and used in the calculation of debt covenants and interest rate margins. The primary debt covenants are the Total Funded Debt to Adjusted EBITDA and Fixed Charge Coverage Ratio. As at December 29, 2017 and December 30, 2016, the Company was in compliance with all debt covenants.

The debt is secured by a first-ranking security interest on all present and after-acquired assets of the Company's subsidiary, Pinnacle Renewable Energy Inc.

In the fiscal year ended December 29, 2017, unamortized deferred financing fees in the amount of \$496 (2016 - \$346) pertaining to the previous senior secured debt facility were expensed in net profit (loss) at the date of the amendment. Transaction costs pertaining to the amended Facility had been deferred in the amount of \$1,331 (2016 - \$1,896) and are being amortized in net profit (loss).



PINNACLE RENEWABLE HOLDINGS INC.

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9. Revolver loan and term debt (continued)

Aggregate minimum payments for each of the next five fiscal years for the term loan are as follows:

| | | |
|-------|----|---------|
| 2018 | \$ | 6,000 |
| 2019 | | 9,500 |
| 2020 | | 14,500 |
| 2021 | | 24,000 |
| 2022 | | 146,000 |
| Total | \$ | 200,000 |

The Facility has authorized credit and repayment terms as follows:

a) Revolver loan

The Company may borrow up to \$50,000 (2016 - \$50,000) under the revolver loan with a maximum of \$5,000 (2016 - \$5,000) for letters of credit. The revolver loan is to be used for operating purposes and is expected to be repaid within the year, and therefore has been presented as a current liability.

b) Term loan

The Company may borrow up to \$200,000 (2016 - \$160,000) under the non-revolving term loan and as at December 29, 2017 had borrowed \$180,000 (2015 - \$160,000). The Company is required to make principal payments on the term loan in installments on the last day of each fiscal quarter as follows: (i) \$2,000 on March 31, 2018 to December 31, 2018, inclusive, (ii) \$2,500 on March 31, 2019 to December 31, 2019, inclusive, (iii) \$4,000 on March 31, 2020 to December 31, 2020, inclusive and (iv) \$5,000 on March 31, 2021 to December 31, 2021, inclusive (v) \$6,000 on March 31, 2022 to September 30, 2022. The remaining balance is due on December 13, 2022.

c) Delayed draw term loan

The Company may borrow up to \$130,000 (2016 - \$90,000) under the non-revolving delayed draw term loan and at December 29, 2017 had borrowed \$20,000 (2016 - \$nil). Advances under this loan may be made in multiple advances and are available to be drawn until December 31, 2019. The Company is required to make quarterly principal installments equal to (i) 2.0% of the principal amount of the loan for each repayment date occurring during or before December 31, 2020, (ii) 2.50% of the principal amount of the loan for each repayment date occurring after December 31, 2020 but during or before December 31, 2021, and (iii) 3.0% of the principal amount of the loan for each repayment date occurring after December 31, 2021 but during or before September 30, 2022. The remainder of the drawn amount is due on December 13, 2022.



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10. Shareholders' debentures payable

| As at | December 29, 2017 | December 30, 2016 |
|--|-------------------|-------------------|
| Convertible debentures at face value | \$ 60,000 | \$ 60,000 |
| Accrued interest debentures at face value | 49,570 | 49,570 |
| Effective interest rate adjustment on convertible debentures | (48,364) | (56,361) |
| | 61,206 | 53,209 |
| Subordinated debentures at face value | 15,000 | 15,000 |
| Accrued interest on subordinated debentures | 13,571 | 9,535 |
| | 28,571 | 24,535 |
| | 89,777 | 77,744 |
| Less: current interest payable in other current liabilities | (896) | (772) |
| | \$ 88,881 | \$ 76,972 |

The ONCAP entities ("ONCAP") collectively own 60% of the Company and is the Company's controlling parent. ONCAP holds convertible debentures totaling \$60,000 which were issued on May 6, 2011. Interest was payable on the debentures in quarterly installments of 14.00% for the first five years subject to reinvestment noted below; thereafter, interest payments and accruals are not charged. The interest decreased to 10.00% as of February 16, 2014 as a result of the Company having shipped 30,000 MTs of pellets from Westview. ONCAP agreed to re-invest any interest otherwise payable into interest debentures and thus all scheduled interest payments have been capitalized to accrued interest

On issuance on May 6, 2011, the convertible debentures were bifurcated between debt and equity based on their estimated fair values. The debt fair value was determined to be \$33,681 and the equity fair value \$26,319. The debt was being accreted to its face value of \$60,000 on maturity at May 6, 2019 using an effective interest rate of approximately 15.87%. The inputs used in the Black Scholes option model included an exercise price of \$1, an underlying share price of \$1, a risk free interest rate of 3.20%, volatility of 31.2% and a life of 8 years.

On November 29, 2016, the Company and ONCAP modified the convertible debenture agreement by extending the maturity date to January 31, 2022. No interest is charged over this additional 21 months. This modification resulted in a substantial modification to the convertible debentures resulting in an extinguishment of the existing debentures and an issuance of new debentures for accounting purposes. The fair value of the debt decreased by \$21,298 resulting in a gain recorded in the statement of net profit (loss). The fair value of the equity conversion feature increased by \$8,894 which was recorded by transfer from the equity portion of the convertible debentures to deficit. The fair value of the debt was determined using a nominal interest rate of 14% determined based on the change in the Company's credit risk since the debt was originally issued and the change in benchmark interest rates over the same period and translated into an effective rate of 14.75%. The fair value of the conversion feature was determined using a Black Scholes option pricing model with an exercise price of \$1, an underlying share price of \$1.39 (consistent with the Company's valuation done for the Class B shares), a risk free interest rate of 0.95%, volatility of 31.2% and a life of 5.18 years.

ONCAP and other minority shareholders also hold subordinated debentures totaling \$15,000 with an 18.00% interest rate. On an annual basis prior to the interest payment date in April, each lender can elect to have 5/18th of the interest payment paid in cash with the remaining interest reinvested. If no election is made, the total interest amount is reinvested. These debentures mature on January 31, 2022.



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11. Common and preferred share classified as liabilities

| As at | | December 29, 2017 | December 30, 2016 |
|--------------------------|-----------------------------------|-------------------|-------------------|
| Class B common shares | 5,500,000 shares; cost of \$5,500 | \$ 17,215 | \$ 12,540 |
| Class D common shares | 1,172,414 shares; cost of \$1,550 | 3,646 | 2,170 |
| Class H preferred shares | 5,004,000 shares; cost of \$5,055 | 5,131 | 5,055 |
| | | \$ 25,992 | \$ 19,765 |

The Company's management holds Class B and Class D common shares. These shares contain features that may require future settlement in cash and Class D shares have a put right enabling shareholders to put their Class D shares to the Company on death or disability at the greater of cost or fair value. Therefore, 5,500,000 of the Class B shares are measured at fair value and all of the Class D shares are measured at the greater of cost or fair value. The fair value measurements for these classes of shares, which are presented as a liability, are dependent on the underlying fair value of the enterprise as a whole, using estimates consistent with the Goodwill Impairment testing (see note 8). Based on this estimate, the fair value of Class B common shares has increased to \$3.13/share as of December 29, 2017 (2016 - increased to \$2.28/share). The value of Class D common shares has increased to \$3.11/share (2016 - increased to \$2.17/share). The resulting revaluation loss of \$5,601 is recorded in net profit (loss) (2016 - loss of \$10,278).

Class H preferred shares accrue dividends at 4.5% (see note 13) and 3.0% is paid quarterly. The difference of 1.5% is added to their carrying value. During 2016, the Company altered its authorized share structure by authorizing an unlimited number of Class H preferred shares without par value. In connection with the retirement of an employee, 5,004,000 Class H shares were issued in exchange for 5,000,000 Class B shares and 1,000,000 Class F shares. The aggregate fair market value of the shares exchanged, less a discount of 10%, was \$5,004. The Class B shares and Class F shares exchanged were cancelled and a loss of \$572 recognized.

12. Other long-term liabilities

| As at | | December 29, 2017 | December 30, 2016 |
|----------------------------------|--|-------------------|-------------------|
| Decommissioning liabilities | | \$ 2,192 | \$ 1,854 |
| Derivative financial instruments | | 218 | - |
| Other | | 1,047 | 297 |
| | | \$ 3,457 | \$ 2,151 |

The Company has certain decommissioning liabilities related to the operations of the Westview Port, the plants at Lavington, Armstrong, and Williams Lake and the use of rail cars. During 2016, the Company re-estimated the decommissioning liabilities for Lavington Plant based on additional facts and circumstances to more accurately reflect the expected future costs.

| As at | December 30, 2016 | Change in Provision | Change in Discounted Amount | December 29, 2017 |
|-----------------------------------|-------------------|---------------------|-----------------------------|-------------------|
| Plants | \$ 607 | - | \$ 138 | \$ 745 |
| Port Facility | 997 | - | 173 | 1,170 |
| Rail cars | 250 | - | 27 | 277 |
| Total decommissioning liabilities | \$ 1,854 | - | \$ 338 | \$ 2,192 |



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12. Other long-term liabilities (continued)

Plants

The construction and operation of the Lavington plant requires a provision to be set up for the eventual demolition and removal of the plant to restore the operating site to its original condition in accordance with the land lease agreement. The initial term of the land lease expires on December 31, 2019 and renews automatically for an indefinite number of five year periods until terminated. Due to the long-term nature of the liability, there is significant uncertainty regarding eventual costs required to restore the site to its original condition and a \$700 decommissioning cost was provided as management's best estimate. The decommissioning cost was discounted at 2.26% (2016 – 2.31%) which is the Government of Canada long-term bond yield risk-free rate. In addition, provisions have been provided for personal property and fixtures removal for the plants at Armstrong and Williams Lake at the end of their lease terms in accordance with the Company's lease agreements.

Port Facility

In accordance with the associated lease agreement with the Prince Rupert Port Authority, the Company has an obligation to dismantle certain aspects of the Westview port facility at the end of the lease term. The lease term is 21 years ending September 30, 2033 with an option to extend for 10 years. The Company included a provision for the dismantling costs of \$1,200 which is management's best estimate. The discount rate of 2.26% (2016 – 2.31%) which is the Government of Canada long-term bond yield risk-free rate.

Rail cars

Rail cars are leased under various agreements which require the rail cars to be restored to their original condition at the end of the lease term and prior to their return to the lessor.



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13. Shareholders' equity

a) The authorized share capital of the Company consists of the following:

- Unlimited Class A common participating, voting shares, without par value
- Class A common shares issued share in the residual assets of the Company and they provide the holders an additional preferred return of 7.5% on returns upon a liquidation that are in excess of 3 times the invested capital.
- Unlimited Class B common participating, voting shares, without par value
- Unlimited Class C common participating, voting shares, without par value
- Unlimited Class D common participating, voting shares, without par value
- Unlimited Class E preferred participating, voting shares without par value accrue cumulative dividends at 14% for the first five years after the share issuance date; thereafter dividends will be fixed and will not increase. Rate will decrease to 10% when certain operational targets are achieved, which occurred in 2014.
- Unlimited Class F preferred participating, non-voting shares without par value, accrue cumulative dividends at 4.5%. Redeemable at the option of the Company for the issuance amount plus all dividends accrued or declared and unpaid. A mandatory redemption occurs on an initial public offering for the issuance amount plus all dividends accrued or declared unpaid.
- Unlimited Class G preferred participating, non-voting shares without par value, accrue cumulative dividends at 4.5%. Redeemable at the option of the Company for the issuance amount plus all dividends accrued or declared and unpaid. A mandatory redemption occurs on an initial public offering for the issuance amount plus all dividends accrued or declared unpaid.
- Unlimited Class H preferred participating, non-voting shares without par value, accrue cumulative dividends at 5.0%. Redeemable at the option of the Company for the issuance amount plus all dividends accrued or declared and unpaid. A mandatory redemption occurs on an initial public offering for the issuance amount plus all dividends accrued or declared unpaid or November 30, 2020.

b) The issued share capital of the Company consists of the following:

| As at | December 29, 2017 | December 30, 2016 |
|---|-------------------|-------------------|
| Common shares | | |
| 25,000,000 Class A shares | \$ 25,000 | \$ 25,000 |
| 4,500,000 Class B shares | 4,500 | 4,500 |
| 5,500,000 Class B shares presented as a liability (note11) | - | - |
| 1,172,414 Class D shares presented as a liability (note11) | - | - |
| | \$ 29,500 | \$ 29,500 |
| Preferred shares | | |
| 500,000 Class E shares | 500 | 500 |
| 19,000,000 Class F shares | 19,000 | 19,000 |
| 8,600,000 Class G shares | 8,505 | 8,505 |
| 5,004,000 Class H shares presented as a liability (note 11) | - | - |
| | \$ 28,005 | \$ 28,005 |



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14. Non-controlling Interests

The following table summarizes the non-controlling financial information relating to Lavington Pellet Limited Partnership (LPLP) and Smithers Pellet Limited Partnership (SPLP) before inter-company eliminations:

| Fiscal year ended | December 29, 2017 | | | December 30, 2016 | | |
|---|-------------------|-------------|-----------|-------------------|-------------|-----------|
| | LPLP 25% | SPLP 30% | Total | LPLP 25% | SPLP 30% | Total |
| Current assets | \$ 8,703 | \$ 1,828 | \$ 10,531 | \$ 7,300 | - | \$ 7,300 |
| Non-current assets | 40,610 | 9,417 | 50,027 | 42,191 | - | 42,191 |
| Current liabilities | (3,650) | (3,245) | (6,895) | (3,667) | - | (3,667) |
| Non-current liabilities | (970) | - | (970) | (542) | - | (542) |
| Net assets | \$ 44,693 | \$ 8,000 | \$ 52,693 | \$ 45,282 | - | \$ 45,282 |
| Net assets attributable to NCI | \$ 11,173 | \$ 2,400 | \$ 13,573 | \$ 11,320 | - | \$ 11,320 |
| Revenue | \$ 42,015 | - | \$ 42,015 | \$ 38,378 | - | \$ 38,378 |
| Net income | 1,412 | - | 1,412 | 3,464 | - | 3,464 |
| Net income allocated to NCI | \$ 353 | - | \$ 353 | \$ 866 | - | \$ 866 |
| Cash flows from operating activities | \$ 3,365 | \$ - | \$ 3,365 | \$ 4,965 | - | \$ 4,965 |
| Cash flows from investing activities | (2,117) | (6,400) | (8,517) | (1,759) | - | (1,759) |
| Cash flows from financing activities | (2,020) | 8,000 | 5,980 | (1,200) | - | (1,200) |
| Net increase (decrease) in cash and cash equivalents | \$ (772) | \$ 1,600 | \$ 828 | \$ 2,006 | - | \$ 2,006 |

15. Expenses by nature and function

Included in production, distribution and selling, general and administrative costs are the following employee benefit expenses ⁽¹⁾:

| Fiscal year ended | December 29, 2017 | December 30, 2016 |
|-------------------------------------|-------------------|-------------------|
| Production | \$ 16,527 | \$ 17,045 |
| Distribution | 2,972 | 2,455 |
| Selling, general and administration | 7,964 | 6,985 |

(1) Employee benefit expense for the year ended December 29, 2017 includes stock-based compensation of \$237 (2016 - \$138). (note 16)

Amortization of equipment and intangibles allocated by function are as follows:

| Fiscal year ended | December 29, 2017 | December 30, 2016 |
|-------------------------------------|-------------------|-------------------|
| Production | \$ 14,145 | \$ 13,031 |
| Distribution | 3,824 | 3,842 |
| Selling, general and administration | 3,850 | 4,338 |
| | \$ 21,819 | \$ 21,211 |



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

16. Stock based compensation

The Company has a stock option plan (the “Plan”) under which the Board of Directors may grant options to Directors, officers, employees and consultants of the Company at a price not less than the market value of the shares on the day of the grant and for a term not exceeding 10 years. A total of 9,045,000 Class D common shares (2016 - 9,045,000) have been reserved for issuance under the Plan. Options granted vest at a rate of 20% per year from the date of grant.

Details of options issued and outstanding are as follows:

| | Number of options | Weighted average exercise price (\$) | Remaining life (years) |
|--------------------------------|-------------------|--------------------------------------|------------------------|
| Outstanding, December 25, 2015 | 7,775,000 | 1.00 | 6.2 |
| Options forfeited/cancelled | (997,000) | 1.00 | 4.5 |
| Options granted | - | - | - |
| Outstanding, December 30, 2016 | 6,778,000 | 1.00 | 5.3 |
| Options forfeited/cancelled | - | - | - |
| Options granted | 1,200,000 | 3.19 | 9.8 |
| Outstanding, December 29, 2017 | 7,978,000 | 1.33 | 5.1 |

The number of options exercisable at December 29, 2017 was 6,446,782 (2016 – 5,932,497). 1,200,000 options were issued in the year ended December 29, 2017 (2016 – nil). The 2017 grant date value was calculated using the Black-Scholes option pricing model using a weighted average share price and exercise price of \$3.19, an expected volatility rate of 33.11%, which was based on comparable entities, a 1.9% expected risk-free rate and a nil dividend yield. A total of \$237 (2016 - \$138) in stock-based compensation expense was recognized for the year ended December 29, 2017. Contributed surplus on the statement of financial position relates to accrued stock based compensation.

17. Finance costs

a) Finance costs excluding shareholders’ debentures

| Fiscal year ended | December 29, 2017 | December 30, 2016 |
|--|-------------------|-------------------|
| Interest on revolver loan, term debt and delayed draw loan | \$ 7,425 | \$ 8,539 |
| Fair value (gain)/loss on derivatives | 1,566 | (1,374) |
| Realized (gain)/loss on derivatives | (135) | (327) |
| Unrealized (gain)/loss on foreign exchange | (268) | 402 |
| Realized loss on foreign exchange | 436 | 155 |
| Amortization of deferred financing fees | 1,094 | 866 |
| Other | 1,774 | 983 |
| | \$ 11,892 | \$ 9,244 |

b) Finance costs on shareholders’ debentures

| Fiscal year ended | December 29, 2017 | December 30, 2016 |
|--|-------------------|-------------------|
| Interest on debentures (note 10) | \$ 12,359 | \$ 13,054 |
| Gain on modification of debentures (note 10) | - | (21,298) |
| | \$ 12,359 | \$ (\$8,244) |



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

18. Income taxes

The reconciliation of statutory income tax rates to the Company's effective tax rate is as follows:

| Fiscal year ended | December 29, 2017 | December 30, 2016 |
|--|-------------------|-------------------|
| Income tax recovery (expense) at statutory rates | \$ 1,133 | \$ (2,817) |
| (Increase) decrease related to | | |
| Permanent differences and other | (1,298) | (2,754) |
| Change in tax rates | (361) | - |
| | (526) | (5,571) |
| Classified as | | |
| Current | - | (2) |
| Deferred | (526) | (5,569) |
| Income tax expense | \$ (526) | \$ (5,571) |

The Company's deferred income tax assets and liabilities are comprised of the following:

| Deferred tax assets | Non-capital losses | Provisions | Transaction costs | Other | Total |
|-----------------------------------|--------------------|---------------|-------------------|---------------|------------------|
| Balance, December 30, 2016 | \$ 30,014 | \$ 588 | \$ 637 | \$ 54 | \$ 31,293 |
| Increase (decrease) to earnings | (3,979) | 263 | 776 | 103 | (2,837) |
| Balance, December 29, 2017 | \$ 26,035 | \$ 851 | \$ 1,413 | \$ 157 | \$ 28,456 |

| Deferred tax liabilities | Property, plant and equipment | Convertible debentures | Intangible assets | Deferred financing costs | Other | Total |
|--|-------------------------------|------------------------|-------------------|--------------------------|----------------|--------------------|
| Balance, December 30, 2016 | \$ (22,407) | \$ (14,337) | \$ (2,601) | \$ (739) | \$ (351) | \$ (40,435) |
| Increase (decrease) | 213 | 1,607 | 687 | (449) | 253 | 2,311 |
| Balance, December 29, 2017 | \$ (22,194) | \$ (12,730) | \$ (1,914) | \$ (1,188) | \$ (98) | \$ (38,124) |
| Net deferred tax liability at December 30, 2016 | | | | | | \$ (9,142) |
| Net deferred tax liability at December 29, 2017 | | | | | | \$ (9,668) |

At December 29, 2017, the Company has \$96,425 (2016 - \$115,439) of unused non-capital loss carry forwards expiring between 2032 and 2037 to reduce future taxable income.

During 2017, the province of British Columbia increased its general corporate tax rate from 11% to 12%. As at December 29, 2017, this rate change is substantively enacted and the Company recognized a \$361 income tax expense for the fiscal year ended December 29, 2017.



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

19. Earnings per share

Net profit (loss) per share has been calculated as follows:

| | December 29, 2017 | December 30, 2016 |
|---|-------------------|-------------------|
| Net profit (loss) for the year attributable to owners | \$ (5,237) | \$ 4,396 |
| Cumulative preferred dividends | (1,242) | (1,254) |
| | \$ (6,479) | \$ 3,142 |
| Weighted average shares (thousands) | | |
| Class A | 25,000 | 25,000 |
| Class B | 4,500 | 4,500 |
| Basic and diluted net income (loss) per share | | |
| Class A | \$ (0.22) | \$ 0.11 |
| Class B | \$ (0.22) | \$ 0.11 |

For 2016, adjustments for the convertible debentures would include removing the gain on modification of \$21,298, making the impact of conversion anti-dilutive. For options, the average fair value of the common shares approximated the exercise price, such that any additional shares under the treasury stock method are not material.

20. Supplemental cash flow information

| Fiscal year ended | December 29, 2017 | December 30, 2016 |
|--|-------------------|-------------------|
| Accounts receivable | \$ (16,526) | \$ (18,312) |
| Inventory | 2,713 | (5,902) |
| Other current assets | 181 | (2,414) |
| Accounts payable and accrued liabilities | (20,733) | 12,529 |
| Other current liabilities | 14,182 | (27) |
| Net increase in working capital | \$ (20,183) | \$ (14,126) |

| Fiscal year ended | December 29, 2017 | December 30, 2016 |
|--|-------------------|-------------------|
| PPE additions during the year (note 6) | \$ 85,570 | \$ 11,483 |
| PPE additions from prior year paid during the year | 1,792 | 3,713 |
| PPE additions in accounts payable | (15,306) | (1,846) |
| Purchase of property, plant, and equipment | \$ 72,056 | \$ 13,350 |



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

21. Related party transactions

Parent and ultimate controlling entity

The Company is controlled by ONCAP who effectively owns 60% of the Company. ONCAP is ultimately controlled by Onex Corporation. The Company's remaining shareholders are former owners or current employees of the Company. During 2017, the Company paid a monitoring fee to ONCAP of \$500 (2016 - \$500). The monitoring fee will continue until the earlier of one shareholder owning all the shares of the Company or an initial public offering.

Minority shareholder

During the year, the Company paid rent on a plant facility to a minority shareholder in the amount of \$240 (2016 - \$240). This amount is set-out in a lease agreement entered into in the normal course of business and on the same terms accorded to unrelated third parties.

Key management personnel compensation

The Company's key management consists of the Chief Executive Officer, Chief Financial Officer, President and Chief Operating Officer, Senior Vice President of Operations, and Senior Vice President of Sales and Logistics.

Aggregate compensation of the Company's key management was as follows:

| Fiscal year ended | December 29, 2017 | December 30, 2016 |
|--------------------------------|-------------------|-------------------|
| Base compensation and benefits | \$ 1,344 | \$ 1,431 |
| Annual bonus | 429 | 331 |
| Stock-based compensation | 218 | 202 |
| | \$ 1,991 | \$ 1,964 |

Houston Pellet LP

Houston Pellet LP is owned 30% by the Company and 70% by non-related third parties. The Company purchases industrial wood products from Houston Pellet LP and earns revenue from sales of fibre and distribution fees. The Company manages and administers the business affairs of Houston Pellet LP and charges a management fee. These transactions are at negotiated amounts between the Company and the non-related third parties.

| Fiscal year ended | December 29, 2017 | December 30, 2016 |
|-------------------|-------------------|-------------------|
| Purchases | \$ 24,030 | \$ 21,715 |
| Revenue | 3,560 | 3,271 |
| Management fee | 639 | 728 |

| As at | December 29, 2017 | December 30, 2016 |
|--------------------|-------------------|-------------------|
| Amounts receivable | \$ 785 | \$ 1,103 |
| Amounts payable | 2,715 | 2,676 |

The amounts receivable and payable to the Company are unsecured and non-interest bearing.



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

21. Related parties (continued)

Lavington Pellet LP

Lavington Pellet LP is owned 75% by the Company and 25% by a non-related third party. The Company purchases industrial wood products from Lavington Pellet LP and earns revenue from sales of fibre at negotiated prices between the Company and the non-related third party. The Company manages and administers the business affairs of Lavington Pellet LP.

| Fiscal year ended | December 29, 2017 | December 30, 2016 |
|-------------------|-------------------|-------------------|
| Purchases | \$ 42,015 | \$ 38,378 |
| Revenue | 556 | 354 |

| As at | December 29, 2017 | December 30, 2016 |
|--------------------|-------------------|-------------------|
| Amounts receivable | \$ 491 | \$ 282 |
| Amounts payable | 4,839 | 2,760 |

The amounts receivable and payable to the Company are unsecured and non-interest bearing.

Smithers Pellet LP

On October 4, 2017, the Company entered into a limited partnership with a non-related third party for the acquisition and development of a wood pellet facility. Smithers Pellet LP is owned 70% by the Company and 30% by a non-related third party. On October 13, 2017, the Company contributed \$5,600 and the non-related third party contributed \$2,400 for the purchase of land, plant and equipment and intangible assets

22. Financial instruments

The carrying values of cash, accounts receivable, accounts payable and accrued liabilities and Class H preferred shares classified as liabilities are measured at amortized cost and approximate the fair values of these financial instruments due to their short terms to maturity. The revolver loan, term debt, and shareholders' debentures payable are measured at amortized cost and their fair value at December 29, 2017 was \$356,954 (2016 - \$298,352).

Derivative instruments, Class B common shares classified as liabilities and Class D common shares are carried at fair value. Financial instruments carried at fair value through net profit (loss) require classification of items within a hierarchy that prioritizes the inputs to fair value measurement. The three levels of the fair value hierarchy are:

- Level 1 – Unadjusted quoted prices in active markets for identical assets or liabilities;
- Level 2 – Inputs other than quoted prices that are observable for the asset or liability, either directly or indirectly;
- Level 3 – Inputs that are not based on observable market data.

**PINNACLE RENEWABLE HOLDINGS INC.**

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

22. Financial instruments (continued)

The following table summarizes the Company's financial instruments measured at fair value at December 29, 2017 and December 30, 2016 and shows the fair value at which they have been classified:

| | Fair value hierarchy level | December 29, 2017 | December 30, 2016 |
|---|-------------------------------|-------------------|-------------------|
| Derivative financial instruments asset (liability) | Level 1 | \$ (474) | \$ 1,092 |
| Financial liabilities measured at fair value | | | |
| Class B common shares | Level 3 | 17,215 | 12,540 |
| Class D common shares | Level 3 | 3,646 | 2,170 |
| | | \$ 20,861 | \$ 14,710 |

The following table summarizes the fair value of the derivative financial instruments included in the statements of financial position:

| As at | December 29, 2017 | December 30, 2016 |
|-----------------------------|-------------------|-------------------|
| Other current assets | \$ - | \$ 864 |
| Other long-term assets | - | 228 |
| Other current liabilities | 256 | - |
| Other long-term liabilities | 218 | - |
| | \$ 474 | \$ 1,092 |

For the year ended December 29, 2017, the Company recognized a loss of \$1,431 (2016 – gain of \$1,701) on its derivative financial instruments in its net profit (loss) (note 17).

The fair value of Class B common shares and Class D common shares are determined on the same basis as the recoverable amount prepared for goodwill impairment testing (see note 8). This fair value determination requires significant management assumptions and accordingly these are classified as Level 3. The fair value of Class B shares was determined to be \$3.13/share on December 29, 2017 (2016 - \$2.28/share). The value of Class D shares was determined to be \$3.11/share on December 29, 2017 (2016 - \$2.17/share).

The following table shows reconciliation from the opening balances to the closing balances for Level 3 fair values:

| | |
|-------------------------------------|------------------|
| For fiscal years ended | |
| Balance at December 25, 2015 | \$ 7,720 |
| Net change in fair value | 10,278 |
| Repurchase of Class D common shares | (3,288) |
| Balance at December 30, 2016 | 14,710 |
| Issuance of Class D common shares | 550 |
| Net change in fair value | 5,601 |
| Balance at December 29, 2017 | \$ 20,861 |



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

23. Financial Risk and Capital Management

The Company is exposed to a number of risks as a result of holding financial instruments including credit risk, liquidity risk and market risk. The Company's Risk Management Committee manages risk related to counterparty credit risk and market risk such as foreign exchange.

Credit risk

Credit risk is the risk of financial loss to the Company if a counterparty to a financial instrument fails to meet its contractual obligations. Financial instruments that are subject to credit risk include cash and accounts receivable. The Company manages its credit risk on cash by using major Canadian chartered banks for all cash deposits. The cash balance at December 29, 2017 is \$18,908 (2016 - \$12,112).

The Company manages its credit risk on accounts receivable by reviewing individual sales contracts considering the length of the contract and assessing the credit quality of the counterparty. Board approval is required for contracts over \$5,000. The significant majority of the Company's sales are contracted with large utility customers on which no impairment loss has been recognized during the fiscal years ended 2017 and 2016. As at December 29, 2017, a \$98 balance (2016 - nil) is being monitored. The accounts receivable balance at December 29, 2017 is \$41,253 (2016 - \$24,746).

Liquidity risk

Liquidity risk is the risk that the Company will not be able to meet its respective obligations as they come due. The Company manages liquidity requirements through frequent monitoring of cash inflows and outflows, preparation of regular cash flow forecasting and its available credit facilities.

The contractual maturities of financial liabilities excluding future interest and shareholders' debentures and common and preferred shares at December 29, 2017 were as follows:

| | Carrying amount | Contractual cash flows | 3 months or less | 3 - 12 months | More than 12 months |
|---|-----------------|------------------------|------------------|---------------|---------------------|
| <i>Non-derivative financial liabilities</i> | | | | | |
| Revolver loan ⁽ⁱ⁾⁽ⁱⁱ⁾ | \$ 22,000 | \$ 22,000 | \$ 22,000 | \$ - | \$ - |
| Accounts payable and accrued liabilities | 35,653 | 35,653 | 35,653 | - | - |
| Term loan | 176,813 | 180,000 | - | 6,000 | 174,000 |
| Delayed draw loan | 20,000 | 20,000 | - | - | 20,000 |

The contractual maturities of financial liabilities excluding future interest and shareholders' debentures and common and preferred shares at December 30, 2016 were as follows:

| | Carrying amount | Contractual cash flows | 3 months or less | 3 - 12 months | More than 12 months |
|---|-----------------|------------------------|------------------|---------------|---------------------|
| <i>Non-derivative financial liabilities</i> | | | | | |
| Revolver loan ⁽ⁱ⁾⁽ⁱⁱ⁾ | \$ 7,100 | \$ 7,100 | \$ - | \$ - | \$ 7,100 |
| Accounts payable and accrued liabilities | 42,185 | 42,185 | 42,185 | - | - |
| Term debt | 157,170 | 160,000 | - | 1,600 | 158,400 |

⁽ⁱ⁾ Classified as 3 months or less as due on demand; however, maturity of the Revolver loan is December 13, 2022 (2016 - December 16, 2021)

⁽ⁱⁱ⁾ Cash balance as at December 29, 2017 is \$18,908 (2016 - \$12,112)



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

23. Financial Risk and Capital Management (continued)

At December 29, 2017, the Company has available liquidity of \$44,313 (2016 - \$51,414) from its debt facilities and forecasts sufficient liquidity throughout 2018. Management expects to finance its operations and cash flows from its current available resources and without further support from its shareholders and lenders. However, to the extent that additional cash resources are required due to unforeseen circumstances, management anticipates support from its shareholders and lenders, although there can be no guarantees.

Market risk

Market risk is that the change in market prices such as foreign exchange rates will affect the Company's net profit (loss) and that the future cash flows of a financial instrument will fluctuate due to changes in market prices.

Foreign currency

The Company's functional and reporting currency is the Canadian dollar. The Company's sales, operating and capital expenditures are primarily denominated and settled in Canadian dollars. The Company has exposure to the US dollar on its shipping costs, rail car leases and some capital purchases. The Company mitigates its exposure to the US dollar on its shipping costs by invoicing the shipping portion in US dollars and with a contract with its major shipping provider with a fixed US dollar to Canadian dollar exchange rate. The remaining exposure is mitigated by entering into a series of US dollar forward contracts matching the amount and timing of the estimated US dollar expenditures.

These contracts are simultaneously settled on a gross tax basis as the Company exchanges US dollars into Canadian dollars at predetermined rates. The Company does not apply hedge accounting to its US dollar forward contracts. The outstanding notional amounts of the US dollar forward contracts and their contractual maturities are as follows:

| | Notional amount | Average forward rate | Less than 12 months | More than 12 months | Fair value asset (liability) |
|-------------------------|-----------------|----------------------|---------------------|---------------------|------------------------------|
| As at December 29, 2017 | \$ 73,564 | 1.259 | \$ 9,064 | \$ 64,500 | \$ (474) |
| As at December 30, 2016 | \$ 15,400 | 1.267 | \$ 12,000 | \$ 3,400 | \$ 1,092 |

Interest rate

The Company is exposed on interest rate risk through its debt facility including its revolver, term loan and delayed draw term loan which are subject to variable lending rates. Currently, the Company does not use financial instruments to manage this risk. A 1% change in interest rates would increase or decrease interest expense by \$1,794 (2016 - \$1,552).



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

24. Capital management

The Company's objective when managing its capital structure is to maintain a strong financial position and to provide returns with sufficient liquidity to undertake further growth for the benefit of its shareholders.

The Company's capital is comprised of long-term obligations and equity as outlined below:

| As at | December 29, 2017 | December 30, 2016 |
|---|-------------------|-------------------|
| External party debt (including revolver loan) | \$ 222,000 | \$ 167,100 |
| Shareholders' debentures payable | 88,881 | 76,972 |
| Common and preferred shares classified as liabilities | 25,992 | 19,765 |
| Less: cash | (18,908) | (12,112) |
| Net long-term obligations | 317,965 | 251,725 |
| Total equity (deficit) | 35,204 | 37,951 |
| Total capitalization | \$ 353,169 | \$ 289,676 |

There were no changes to the Company's approach to capital management during the year.

The Company is subject to certain financial covenants in its debt obligations (see note 9). The Company's strategy is to ensure it remains in compliance with all of its existing covenants so as to ensure continuous access to required debt to fund growth. Management reviews results and forecasts to monitor the Company's compliance.

25. Commitments

Leases

The Company has lease commitments on certain vehicles, rail cars, land, office space and equipment. The total annual minimum lease payments are as follows:

| | Finance Lease | Operating Lease |
|------------|---------------|-----------------|
| 2018 | \$ 561 | \$ 8,509 |
| 2019 | 534 | 8,434 |
| 2020 | 557 | 6,990 |
| 2021 | - | 5,205 |
| 2022 | - | 3,202 |
| Thereafter | - | 22,189 |
| | \$ 1,652 | \$ 54,529 |

Customer and supplier commitments

The Company has made commitments to customers and suppliers with respect to minimum volumes for sales, shipping, storage and loading and fibre purchases. These contracts are in the normal course of business and cover periods of up to fifteen years in the future. Failure to meet contractual terms other than as a result of a force majeure event as defined under the various agreements could result in various payments required by the Company. The Company expects to meet its commitments in the normal course of operations.

Capital commitments

The Company has capital commitments of \$22,514 at December 29, 2017 (2016 - \$140).



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

26. Contingencies

The Company is involved in various claims associated with its operations. While the outcomes of the proceedings are not determinable, management is of the opinion that the resulting settlements, if any, will not materially affect the financial position of the Company. Should a material loss occur, it would be accounted for when it became likely and reasonably estimable. Otherwise, any losses would be accounted for as a charge to net profit (loss) in the period in which the settlement occurs.

27. Segmented information

The Company's operations consist of the production and sale of wood pellets, which constitutes a single operating segment.

Revenue attributed to geographic regions based on the location of customers was as follows:

| Fiscal year ended | December 29, 2017 | December 30, 2016 |
|----------------------|-------------------|-------------------|
| Europe | \$ 259,070 | \$ 208,220 |
| Asia | 18,325 | 30,944 |
| North America | 15,332 | 27,174 |
| Total Revenue | \$ 292,727 | \$ 266,338 |

28. Economic dependence

The Company has certain European customers whose individual revenue represents 10% or greater of the Company's total revenue. For the fiscal year ended December 29, 2017, three of these customers represented 86% of the Company's total revenues. For the fiscal year ended December 30, 2016, two of these customers represented 79% of the Company's total revenue.

The Company's inbound fibre and outbound bulk pellet exports are transported using an integrated logistics supply chain which includes trucking, rail, terminal, and shipping service providers. If alternative sources for these services were required the Company's ability to service existing bulk off-take contracts and/or the Company's costs could be impacted.



PINNACLE RENEWABLE HOLDINGS INC.

Notes to the Consolidated Financial Statements

Years ended December 29, 2017 and December 30, 2016

(Amounts in thousands of Canadian dollars except number of shares and per share amounts)

29. Subsequent event

Initial Public Offering and Secondary Offering

Pursuant to its final prospectus dated January 30, 2018, the Company completed an initial public offering and secondary offering (“Offering”) on February 6, 2018 and listed its common shares on the Toronto Stock Exchange. The Offering is for a total of 13,335,000 common shares at \$11.25 per share for gross proceeds of \$150,019. The Offering includes a treasury offering of 6,223,889 common shares for gross proceeds of \$70,019 and a secondary offering of 7,111,111 of common shares from existing shareholders for gross proceeds of \$80,000. The Company received net proceeds of \$37,591 which is net of underwriting fees of \$3,851 and the repayment of its \$28,577 subordinated debentures.

Prior to the completion of the Offering, the Company’s share capital was amended to create an unlimited number of common shares and an unlimited amount of preferred shares, issuable in series. In connection with and immediately prior to the completion, the Company’s pre-closing common and preferred shares and convertible debentures were converted to 26,679,332 common shares and no preferred shares were issued. The conversion of the convertible debentures and the Class B and Class D common shares carried at fair value to new common shares is expected to result in an estimated after-tax loss \$12,600. All other pre-close common and preferred shares will be converted at their pre-close carrying value.

Upon closing of the Offering, the total issued and outstanding common shares are 32,903,221. Prior to the completion of the Offering, ONCAP was the Company’s controlling parent. Upon completion of the Offering, ONCAP owns 14,112,787 or 42.9% of the issued and outstanding common shares.

Concurrent with the closing of the Offering, the Company’s stock option plan was amended to comply with public company provisions as required by the Toronto Stock Exchange and that options issued and outstanding under the stock option plan will become exercisable for new common shares. Upon completion of the Offering, the Company will no longer grant options under the stock option plan.

Notes:

Notes:

DIRECTORS & OFFICERS



Gregory Baylin
Chair^{1,2*,4}



Pat Bell
Vice Chair^{1*,2,3,4}



Michael Lay
Director^{2,4}



Hugh MacDiarmid
Director^{3*,4}



Jane O'Hagan^{1,3,4}
Director



Robert McCurdy
Director, Chief Executive Officer



Leroy Reitsma
Director, President & Chief Operating Officer



Andrea Johnston
Chief Financial Officer

SHAREHOLDER INFORMATION

Corporate Head Office

350 - 3600 Lysander Lane
Richmond, British Columbia V7B 1C3, Canada
Tel: 604.270.9613

Registrar and Transfer Agent

TSX Trust

Auditors

KPMG LLP

Legal Counsel

McCarthy Tetrault LLP

Stock Exchange Listing

Pinnacle Renewable Holdings is listed on the Toronto Stock Exchange under the symbol PL. As at March 15, 2018, Pinnacle had 32,903,221 common shares issued and outstanding.

Investor Contact

Tel: 1.877.737.4344
Email: investors@pinnaclepellet.com

Annual General Meeting

Thursday, June 21, 2018 at 10am
McCarthy Tetrault LLP
Suite 2400
745 Thurlow Street
Vancouver, BC



Pinnacle.

PINNACLE RENEWABLE HOLDINGS INC.



www.pinnaclepellet.com