



**ALEAFIA HEALTH INC.**  
**UNAUDITED CONDENSED CONSOLIDATED**  
**FINANCIAL STATEMENTS**

(expressed in Canadian dollars)  
For the six months ended  
June 30, 2020 and 2019

[AleafiaHealth.com](http://AleafiaHealth.com)

# Table of Contents

MANAGEMENT'S RESPONSIBILITY.....	- 3 -
UNAUDITED INTERIM CONDENSED CONSOLIDATED STATEMENTS OF FINANCIAL POSITION.....	- 4 -
UNAUDITED INTERIM CONDENSED CONSOLIDATED STATEMENTS OF COMPREHENSIVE LOSS.....	- 5 -
UNAUDITED INTERIM CONDENSED CONSOLIDATED STATEMENTS OF CHANGES IN EQUITY.....	- 6 -
UNAUDITED INTERIM CONDENSED CONSOLIDATED STATEMENTS OF CASH FLOWS .....	- 7 -
NOTE 1 NATURE OF OPERATIONS.....	- 8 -
NOTE 2 BASIS OF PRESENTATION .....	- 8 -
NOTE 3 BUSINESS COMBINATION AND ASSET ACQUISITION. ....	- 9 -
NOTE 4 RIGHT-OF-USE ASSET AND LEASE LIABILITY.....	- 10 -
NOTE 5 PROPERTY, PLANT AND EQUIPMENT.....	- 11 -
NOTE 6 INTANGIBLE ASSETS .....	- 11 -
NOTE 7 SHARE CAPITAL .....	- 11 -
NOTE 8 RELATED PARTY BALANCES AND TRANSACTIONS.....	- 13 -
NOTE 9 MANAGEMENT OF CAPITAL .....	- 14 -
NOTE 10 INVENTORY .....	- 14 -
NOTE 11 BIOLOGICAL ASSETS .....	- 15 -
NOTE 12 INVESTMENTS.....	- 16 -
NOTE 13 CONVERTIBLE DEBT.....	- 16 -
NOTE 14 FINANCIAL INSTRUMENTS AND FINANCIAL RISKS .....	- 17 -
NOTE 15 COMMITMENTS AND CONTINGENCIES .....	- 19 -
NOTE 16 COVID-19 AND ITS IMPACT ON THE BUSINESS ENVIRONMENT .....	- 20 -

# MANAGEMENT'S RESPONSIBILITY

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## To the Shareholders of Aleafia Health Inc.:

The accompanying unaudited interim condensed consolidated financial statements of Aleafia Health Inc. and its subsidiaries (the "Company") were prepared by management, which is responsible for the integrity and fairness of the information presented, including the many amounts that out of necessity are based on estimates and judgements. These interim condensed consolidated financial statements have been prepared in accordance with International Financial Reporting Standards.

In fulfilling its responsibilities, management designs and maintains the necessary accounting systems and related internal controls to provide reasonable assurance that transactions are authorized, assets are safeguarded, and financial records are properly maintained to provide reliable information for the preparation of these interim condensed consolidated financial statements.

The Board of Directors oversees the responsibilities of management for financial reporting through an Audit Committee, which is composed entirely of independent directors. This Committee reviews the unaudited interim condensed consolidated financial statements and recommends them to the Board of Directors for approval. They meet regularly with management to review internal control procedures and advise directors on auditing matters and financial reporting issues.

August 12, 2020

*"Geoffrey Benic"*

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Geoff Benic  
Chief Executive Officer

*"Benjamin Ferdinand"*

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Benjamin Ferdinand  
Chief Financial Officer

**ALEAFIA HEALTH INC.****Unaudited Interim Condensed Consolidated Statements of Financial Position**

As at June 30, 2020 and December 31, 2019

(Amounts reflected in thousands of Canadian dollars)

	Note	June 30, 2020	December 31, 2019
		\$	\$
<b>ASSETS</b>			
<b>Current</b>			
Cash and cash equivalents		45,399	41,247
Marketable securities		1,558	1,452
Other receivable-marketable securities		10,000	-
Trade receivables		9,349	4,847
Tax receivables		4,862	6,498
Prepaid expenses		5,760	5,756
Prepaid expenses for supply agreement		-	22,756
Inventory	10	36,882	34,115
Biological assets	11	2,167	971
		115,977	117,642
<b>Non-current</b>			
Prepaid deposit for property, plant and equipment		-	3,612
Property, plant and equipment	5	74,769	64,338
Deferred expenses		733	1,036
Right-of-use asset	4	3,288	1,071
Investments	12	5,416	4,616
Intangible assets	6	79,042	81,252
Goodwill	3	188,790	188,790
		352,038	344,715
<b>TOTAL ASSETS</b>		<b>468,015</b>	<b>462,357</b>
<b>LIABILITIES</b>			
<b>Current</b>			
Accounts payable and accrued liabilities	8	16,535	20,132
Lease liability	4	634	507
Convertible debt	13	22,681	-
Current income tax liability		1,400	-
Deferred revenue		61	101
		41,311	20,740
<b>Non-current</b>			
Lease liability	4	2,852	700
Convertible debt	13	31,061	51,009
Deferred tax liability		2,994	5,394
		36,907	57,103
<b>TOTAL LIABILITIES</b>		<b>78,218</b>	<b>77,843</b>
<b>SHAREHOLDER'S EQUITY</b>			
Share capital	7	384,762	371,744
Warrants	7	44,634	44,701
Contributed surplus	7	38,360	35,900
Deficit		(77,959)	(67,831)
		389,797	384,514
<b>TOTAL LIABILITIES AND EQUITY</b>		<b>468,015</b>	<b>462,357</b>

COMMITMENTS AND CONTINGENCIES (Note 15)

Approved and authorized for issue on behalf of the board on August 12, 2020.

*"Daniel Milliard"**"Lea Ray"*

Daniel Milliard - Director

Lea Ray - Director

The accompanying notes are an integral part of these unaudited interim condensed Consolidated Financial Statements.

**ALEAFIA HEALTH INC.****Unaudited Interim Condensed Consolidated Statements of Comprehensive Loss**

For the Three months and Six months ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

	Note	Three months ended		Six months ended	
		June 30, 2020	June 30, 2019	June 30, 2020	June 30, 2019
		\$	\$	\$	\$
<b>Revenue</b>					
Consultation services		304	800	940	1,427
Research		476	619	710	987
Sale of cannabis		9,240	2,532	23,203	3,063
Gross revenue		10,020	3,951	24,853	5,477
Excise taxes		245	112	482	112
Net revenue		9,775	3,839	24,371	5,365
<b>Cost of sales</b>					
Doctor services		240	545	709	1,008
Inventory expensed to cost of sales		6,033	2,250	8,085	3,575
Gross profit before fair value adjustment		3,502	1,044	15,577	782
Fair value changes in biological assets and changes in inventory sold	10	(2,058)	(1,856)	4,159	(2,060)
Adjustment of inventory to net realizable value	10	3,160	-	3,160	-
Gross profit		2,400	2,900	8,258	2,842
<b>Expense</b>					
Wages and benefits		3,112	1,024	5,597	4,012
General and administration		3,392	4,559	6,501	12,229
Business transaction costs		1,996	2,272	2,506	3,179
Bad debt expenses		300	-	404	-
Amortization and depreciation		2,228	4	4,242	872
Share-based payments		494	4,210	1,460	12,171
		11,522	12,069	20,710	32,463
Operating loss		(9,122)	(9,169)	(12,452)	(29,621)
Other (income) expense					
Interest expense		2,828	1,771	5,476	1,892
Realized gain on LP settlement		(6,344)	-	(6,344)	-
Unrealized (gain) loss on securities		276	855	(5)	855
Non-operating (income) expense		(362)	(318)	(403)	(3)
		(3,602)	2,308	(1,276)	2,744
Net loss before income taxes		(5,520)	(11,477)	(11,176)	(32,365)
<b>Income tax</b>					
Current income tax expenses		(300)	-	1,400	-
Deferred taxes(recovery) / expense		(1,200)	-	(2,400)	(657)
Net loss and Comprehensive loss for the period		(4,020)	(11,477)	(10,176)	(31,708)
Loss per share, basic and diluted		(0.01)	(0.04)	(0.04)	(0.16)
Weighted average common shares outstanding		285,981,867	273,303,599	281,937,777	198,273,617

The accompanying notes are an integral part of these unaudited interim condensed Consolidated Financial Statements.

**ALEAFIA HEALTH INC.**
**Unaudited Interim Condensed Consolidated Statements of Changes in Equity**

For six months ended June 30, 2020 and June 30, 2019

(Amounts reflected in thousands of Canadian dollars, except share and warrant amounts)

June 30, 2020	Common shares		Warrants		Contributed Surplus	Deficit	Total
	Number of Shares	Amount	Number of Warrants	Amount			
	#	\$	#	\$			
<b>Balance, December 31, 2019</b>	<b>277,893,686</b>	<b>371,744</b>	60,264,816	44,701	35,900	(67,831)	384,514
Warrants expired	-	-	(15,400,563)	-	-	-	-
Issuance of common stock	23,000,000	13,017	-	-	-	-	13,017
Shares issued from options exercised	500	1	-	-	(1)	-	-
Warrants Issued for issuance of shares	-	-	12,707,500	(67)	-	-	(67)
Share-based payments	-	-	-	-	2,461	48	2,509
Net loss for the period	-	-	-	-	-	(10,176)	(10,176)
<b>Balance , June 30 2020</b>	<b>300,894,186</b>	<b>384,762</b>	<b>57,571,753</b>	<b>44,634</b>	<b>38,360</b>	<b>(77,959)</b>	<b>389,797</b>

June 30, 2019	Common shares			Warrants		Contributed Surplus	Deficit	Total
	Number of Shares	Amount	Equity component of Convertible Debt	Number of Warrants	Amount			
	#	\$	\$	#	\$			
<b>Balance, December 31, 2018</b>	<b>157,848,812</b>	<b>104,455</b>	-	9,228,590	<b>748</b>	14,954	(28,224)	91,933
Shares issued from warrants exercised	1,204,514	3,538	-	(1,204,514)	-	-	-	3,538
Shares issued from options exercised	547,789	16,720	-	-	-	(12,995)	-	3,725
Warrants deemed issued for Emblem	-	-	-	39,286,213	42,775	-	-	42,775
Warrants issued for Convertible Debt	-	-	-	90,468	216	-	-	216
Warrants issued for Convertible Debt-Issuar	-	-	-	-	1,316	-	-	1,316
Share options deemed issued for Emblem	-	-	-	-	-	5,922	-	5,922
Shares issued for Emblem	110,823,349	245,608	-	-	-	-	-	245,608
Shares/Warrants issued for services	2,331,255	(3,538)	-	-	3,322	-	-	(216)
Equity component of Convertible Debt	-	-	5,499	-	-	-	-	5,499
Shares Issued	-	100	-	-	-	-	-	100
Share-based payments	2,000,000	3,160	-	-	-	14,035	-	17,195
Net loss for the period	-	-	-	-	-	-	(31,708)	(31,708)
<b>Balance, June 30 , 2019</b>	<b>274,755,719</b>	<b>370,043</b>	<b>5,499</b>	<b>47,400,757</b>	<b>48,377</b>	<b>21,916</b>	<b>(59,932)</b>	<b>385,903</b>

The accompanying notes are an integral part of these unaudited interim condensed Consolidated Financial Statements.

**ALEAFIA HEALTH INC.****Unaudited Interim Condensed Consolidated Statements of Cash Flows**

For the six months ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars)

	<b>Six months ended</b>	
	June 30, 2020	June 30, 2019
	\$	\$
<b>Operating activities</b>		
Net loss for the period	(10,176)	(31,708)
Adjustments for non-cash items:		
Depreciation	2,227	872
Amortization	2,015	-
Share-based consulting fees	-	3,160
Share-based payments	2,460	14,035
Accretion	2,732	159
Realized gain on LP settlement	(6,344)	-
Current income tax liability	1,400	-
Deferred income tax recovery	(2,400)	(657)
Unrealized (gain) loss on marketable securities	(5)	855
Fair value changes in biological assets and changes in Inventory sold	7,319	(2,548)
	(772)	(15,832)
<b>Changes in operating assets and liabilities</b>		
Prepaid expenses	17,208	(942)
Trade receivables	(14,502)	(1,630)
Tax receivable	1,637	-
Marketable securities	(102)	595
Biological assets	(1,196)	303
Cash received from LP settlement	15,500	-
Inventory	(9,112)	1,364
Accounts payable and accrued liabilities	(3,594)	(5,255)
Deferred revenues	(40)	(21)
Net cash generated by (used in) operating activities	5,027	(21,418)
<b>Investing activities</b>		
Investment in CannaPacific	-	(753)
Investment in retail store operations	(800)	-
Cash acquired on amalgamation	-	15,989
Deferred expenses	302	-
Sale proceeds of land	-	-
Acquisition of property plant and equipment	(13,131)	(7,260)
Net cash (used in) provided by investing activities	(13,629)	7,976
<b>Financing activities</b>		
Net of lease-right of use assets and liabilities.	(246)	(10)
Convertible debt	-	37,660
Warrants and options exercised	1	7,262
Proceeds from the issuance of common stock	12,999	100
Net cash provided by financing activities	12,754	45,012
Change in cash and cash equivalents	4,152	31,570
Cash and cash equivalents, beginning of period	41,247	26,407
Cash and cash equivalents, end of period	45,399	57,977

The accompanying notes are an integral part of these unaudited interim condensed Consolidated Financial Statements.

## ALEAFIA HEALTH INC.

### Notes to the Consolidated Financial Statements

For the periods ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

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#### Note 1 Nature of Operations

Aleafia Health Inc. (“Aleafia Health”) is a vertically integrated and federally licensed Canadian cannabis company offering health and wellness services. The Company’s four primary business units are Cannabis Cultivation & Products, Health & Wellness Clinics, Cannabis Education and Consumer Experience with e-commerce, retail distribution and provincial supply agreements.

The Company owns three cannabis product and cultivation facilities, which are licensed and operational. The Company produces a diverse portfolio of commercially proven, high-margin derivative products including flower, pre-rolls, oil drops, oil capsules and oil sprays. Aleafia Health operates the largest national network of medical cannabis clinics and education centers staffed by physicians, nurse practitioners and educators.

The Company’s head and registered office is located at 8810 Jane Street, 2<sup>nd</sup> floor, Concord, Ontario and its corporate website is [AleafiaHealth.com](http://AleafiaHealth.com). Aleafia Health intends to change its head and registered office to 85 Basaltic Road, Concord, Ontario on or around August 17, 2020.

Aleafia Health was originally incorporated under the *Business Corporations Act* (British Columbia) as Wyn Metals on February 2, 2007. On March 26, 2018, concurrent with the completion of a business combination with Canabo Medical Inc., the Company changed its name to “Aleafia Health Inc.” On June 27, 2018, the Company continued into Ontario under the *Business Corporations Act* (Ontario). For further information on these transactions, please refer to the Company’s Annual Information Form dated April 29, 2019.

On March 14, 2019, the Company acquired Emblem Corp. by way of a statutory plan of arrangement under the provisions of the *Canada Business Corporations Act* (the “Arrangement”), pursuant to which, among other things, Aleafia Health acquired all of the issued and outstanding common shares of Emblem Corp. following Emblem’s amalgamation with Aleafia Health’s wholly-owned subsidiary, 11208578 Canada Inc., to form a new wholly-owned subsidiary of the Company continuing as “Emblem Corp.” (“Emblem”), see “Note 4. Business Combination and Asset Acquisition – Emblem Corp”.

Following the completion of the Arrangement, on March 19, 2019, the common shares of the Company ceased trading on the TSX Venture Exchange Inc. (“TSXV”) and commenced trading on the Toronto Stock Exchange (“TSX”) under its existing symbol “ALEF” which was subsequently changed to “AH” on May 27, 2020. Emblem Shares were delisted from the TSXV on March 18, 2019.

As at June 30, 2020, the Company had not generated a profit and had accumulated a deficit of \$80.0 million. The Company’s operations and expenditures have been funded by the issuance of equity and convertible debt.

#### Note 2 Basis of Presentation

These unaudited interim condensed consolidated financial statements as at and for the six months ended June 30, 2020 and 2019 have been prepared in accordance with International Financial Reporting Standards (“IFRS”) as issued by the International Accounting Standards Board (“IASB”) and in accordance with IAS 34, Interim Financial Reporting (“IAS 34”). The accounting policies, methods of computation and presentation applied in these unaudited interim condensed consolidated financial statements are consistent with those of the previous fiscal year. These unaudited interim condensed consolidated financial statements reflect the accounting policies and disclosures described in Notes 2 and 4 to the Company’s audited consolidated financial statements for the year ended December 31, 2019 with the exception of any change set out below and accordingly, should be read in conjunction with those audited consolidated financial



## **ALEAFIA HEALTH INC.**

### **Notes to the Consolidated Financial Statements**

For the periods ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

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statements and the notes thereto.

The unaudited interim condensed consolidated financial statements have been prepared on the historical cost basis, with the exception of financial instruments which are measured at fair value, as explained in the accounting policies set out below. In addition, these unaudited interim condensed consolidated financial statements have been prepared using the accrual basis of accounting, except for cash flow information. The functional currency of the Company and its subsidiaries is the Canadian dollar.

#### **Note 3 Business Combination and Asset Acquisition**

On March 14, 2019, the Company completed the acquisition of Emblem Corp. pursuant to a plan of arrangement under the provisions of the Canada Business Corporation Act. Pursuant to the Arrangement, the Company acquired all of the issued and outstanding Emblem shares in exchange for common shares of Aleafia following Emblem's amalgamation with the Company's wholly owned subsidiary, 11208578 Canada Inc., to form a new wholly owned subsidiary of the Company continuing as "Emblem Corp". Pursuant to the Arrangement, Emblem shareholders were entitled to receive 0.8377 of an Aleafia Health common share for each Emblem share held prior to the Arrangement (the "Consideration") with any fractional Aleafia common share being rounded down to nearest whole Aleafia Health common share. The Emblem shares were delisted from the TSXV at the close of business on March 18, 2019.

Prior to the completion of the Arrangement, Emblem had outstanding three classes of warrants to purchase Emblem shares listed on TSXV. The listed warrants, with the exception of any listed Emblem Warrants that were exercised prior to closing of the Arrangement, remain outstanding as warrants of "Emblem Corp" that upon exercise will entitle the holder thereof to receive the Consideration.

Former options to purchase Emblem shares were replaced, pursuant to the Arrangement, with replacement Aleafia Health options (on the same terms as the Emblem options), such that upon exercise will entitle the holder thereof to receive the Consideration.

The acquisition was accounted for as a business combination as the assets acquired and liabilities assumed constitute a business. The transaction was accounted for using the acquisition method of accounting whereby the assets acquired, and the liabilities assumed were recorded at their estimated fair value at the acquisition date. The Company applied various valuation techniques in order to measure the assets acquired and the liabilities assumed in the business combination. These provisional amounts may be adjusted during the measurement period, or additional assets or liabilities may be recognized, to reflect new information obtained about facts and circumstances that existed at the acquisition date that, if known, would have affected the amounts recognized at that date.

The allocation of the components of total consideration to the net assets acquired was as follows:

## ALEAFIA HEALTH INC.

### Notes to the Consolidated Financial Statements

For the periods ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

<b>Consideration</b>	<b>\$</b>
Common shares issued (110,823,349 shares at \$2.28)	252,677
Warrants issued	42,775
Replacement share options	5,922
<b>Total consideration</b>	<b>301,374</b>

  

<b>Net assets acquired</b>	<b>\$</b>
Net tangible assets	74,583
Emblem brand	9,025
GrowWise brand	4,428
Symbi brand	1,647
Paris license	34,000
IP, R&D	600
SDM distribution agreement	1,300
Deferred income tax liability	(285)
	125,298
Goodwill acquired	176,076
<b>Total net assets acquired</b>	<b>301,374</b>

The resulting goodwill represents the sales and growth potential of Emblem Corp. and will not be deductible for tax purposes. The Company has goodwill of \$12.7 million from other previous amalgamations.

#### Note 4 Right-of-Use Asset and Lease Liability

##### RIGHT-OF-USE ASSET

	<b>\$</b>
<b>Cost</b>	
Balance, December 31, 2019	1,591
New leases entered into	2,524
<b>Balance, June 30, 2020</b>	<b>4,115</b>
<b>Accumulated Amortization</b>	
Balance, December 31, 2019	(520)
Amortization	(307)
<b>Balance, June 30, 2020</b>	<b>(827)</b>
<b>Net book value, December 31, 2019</b>	<b>1,071</b>
<b>Net book value, June 30, 2020</b>	<b>3,288</b>

##### LEASE LIABILITY

	<b>\$</b>
Balance, December 31, 2019	1,207
New leases entered into	2,524
Interest expense	191
Payments	(436)
<b>Balance, June 30, 2020</b>	<b>3,486</b>
<b>Current portion of lease liability</b>	<b>634</b>
<b>Long-term portion of lease liability</b>	<b>2,852</b>

**ALEAFIA HEALTH INC.****Notes to the Consolidated Financial Statements**

For the periods ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

**Note 5 Property, Plant and Equipment**

	Computer & Software	Equipment & Furniture	Leasehold Improvements	Land	Buildings & Houses	Total
<b>Cost</b>	\$	\$	\$	\$	\$	\$
Balance, December 31, 2019	758	12,025	5,452	7,637	40,447	66,319
Additions	125	502	108	100	12,296	13,131
Balance, June 30, 2020	883	12,527	5,560	7,737	52,743	79,450

**Accumulated Depreciation**

Balance, December 31, 2019	(225)	(803)	(272)	-	(681)	(1,981)
Balance, June 30, 2020	(317)	(1,673)	(419)	-	(2,272)	(4,681)

**Carrying Amounts**

As at December 31, 2019	533	11,222	5,180	7,637	39,766	64,338
Balance, June 30, 2020	566	10,854	5,141	7,737	50,471	74,769

**Note 6 Intangible Assets**

	Grow License	Patient List	Serruya License	Emblem Brands	Emblem License	Other	Total
<b>Cost</b>	\$	\$	\$	\$	\$	\$	\$
Balance, December 31, 2019	9,358	11,461	12,260	15,100	34,000	3,195	85,374
Balance, June 30, 2020	9,358	11,461	12,260	15,100	34,000	3,195	85,374

**Accumulated Amortization**

Balance, December 31, 2019	(391)	(1,242)	(885)	(130)	(1,122)	(352)	(4,122)
Amortization	(195)	(621)	(409)	(83)	(708)	(194)	(2,210)
Balance, June 30, 2020	(586)	(1,863)	(1,294)	(213)	(1,830)	(546)	(6,332)

**Carrying Amounts**

As at December 31, 2019	8,967	10,219	11,375	14,970	32,878	2,842	81,252
As at June 30, 2020	8,772	9,598	10,966	14,887	32,170	2,649	79,042

**Note 7 Share Capital****Authorized**

The Company is authorized to issue an unlimited number of common shares without par value.

**Issued and Outstanding**

As at June 30, 2020, there were 300,894,186 common shares issued and outstanding.

On May, 29, 2020 in the bought deal offering led by Eight Capital on behalf of a syndicate of underwriters, the Company issued 23,000,000 common shares at a price of \$0.65 per share for aggregate gross proceeds of \$15.0 million which includes the full exercise of the over-allotment option.

**ALEAFIA HEALTH INC.**  
**Notes to the Consolidated Financial Statements**

For the periods ended June 30, 2020 and 2019  
(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

**Warrants**

On May 29, 2020 the Company issued 805,000 compensation warrants and 11,902,500 subscriber warrants to the shareholders of bought deal. As at June 30, 2020 the Company had following warrants outstanding.

	<b>Warrants Outstanding</b>	<b>Weighted Average Exercise price</b>
	#	\$
Warrants outstanding and exercisable, December 31, 2019	60,264,816	2.05
Compensation warrants issued for share issue	805,000	0.80
Subscriber warrants issued for share issue	11,902,500	0.80
Warrants expired	(15,400,563)	3.39
<b>Outstanding and exercisable, June 30, 2020</b>	<b>57,571,753</b>	<b>1.41</b>

At June 30, 2019, the Company had outstanding warrants entitling the holders to acquire additional common shares as follows:

	<b>Expiry Date</b>	<b>Number of warrants</b>	<b>Weighted Average Exercise price</b>
		#	\$
Warrants Issued by Aleafia	Sep 27, 2019 - June 11, 2020	8,540,498	1.67
Warrants issued by Legacy Emblem	De 6, 2019 - Dec 6, 2021	38,860,259	2.49
<b>Outstanding and exercisable, June 30, 2019</b>		<b>47,400,757</b>	<b>2.34</b>

**Stock Options**

The Company has adopted a stock option plan (the “**Plan**”), providing the Board of Directors with the discretion to issue an equivalent number of options of up to 10% of the issued and outstanding share capital. Stock options are granted with an exercise price of not less than the closing share price of the day preceding the date of grant.

The fair values of the stock options granted above were estimated using the Black-Scholes option pricing model. The following table summarizes information relating to outstanding and exercisable stock options as at June 30, 2020:

	<b>Number of Options</b>	<b>Weighted Average Exercise Price for Options</b>
	#	\$
Outstanding as of December 31, 2019	24,979,725	1.22
Granted	1,805,000	0.54
Exercised/Released	(500)	0.60
Cancelled/Forfeited	(650,000)	1.03
Expired	(2,554,484)	1.75
Outstanding as of June 30, 2020	23,579,741	1.12
<b>Vested</b>	<b>16,430,240</b>	<b>1.21</b>
<b>Unvested</b>	<b>7,149,501</b>	<b>0.92</b>

## ALEAFIA HEALTH INC.

### Notes to the Consolidated Financial Statements

For the periods ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

#### Restricted Share Units

The Company has a restricted share unit plan (the “RSU Plan”). For each RSU granted under the plan, the Company recognizes an expense equal to the market value of a common share at the date of grant based on the number of RSUs expected to vest over the term of the vesting period, with a corresponding credit to equity for share-based payments anticipated to be equity settled. RSUs under the RSU plan may vest immediately or become exercisable in various increments based on conditions as determined by the Board. In determining the amount of share-based compensation, the Company used the closing price of the common shares on the RSU grant date. Under the plan, a maximum of 4,000,000 common shares may be issuable.

#### Deferred Share Unit Plan for Directors

At the Company’s annual general meeting on June 30, 2020, shareholders passed a resolution approving the Aleafia Health Inc. a deferred share unit plan (the “DSU Plan”), which will be implemented by Q4 2020.

The purpose of the DSU Plan is to promote a greater alignment of long-term interests between eligible participants (being non-executive directors only) and the Company and its shareholders, to provide a compensation system for non-employee directors that, together with the other director compensation mechanisms of the Company, is reflective of the responsibility, commitment and risk accompanying membership on the Board and the performance of the duties required of the various committees of the Board.

#### Note 8 Related Party Balances and Transactions

Parties are considered to be related if one party has the ability, directly or indirectly, to control the other party or exercise significant influence over the other party in making financial and operating decisions. Related parties may be individuals or corporate entities. A transaction is considered to be a related party transaction when there is a transfer of resources or obligations between related parties.

Key management includes directors and key officers of the Company.

During the six months ended June 30, 2020 and June 30, 2019, the Company had the following transactions with the officers and directors of the Company.

	Six months ended June 30, 2020	Six months ended June 30, 2019
Wages & Benefits: Directors	227	885
Wages & Benefits: Management	923	909
Accounts payable and accrued liabilities: Directors	90	1,033
Accounts payable and accrued liabilities: Management	80	171
Share based compensation: Directors	138	81
Share based compensation: Management	1,167	352

## ALEAFIA HEALTH INC.

### Notes to the Consolidated Financial Statements

For the periods ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

As at June 30, 2020, the amount of \$0.17 million was due to directors and management. The amounts are non-interest bearing and unsecured, are due upon demand and included in accounts payable.

#### Note 9 Management of Capital

The Company's objectives when managing capital are to sustain a sufficient capital base so as to maintain investor, creditor and customer confidence and to sustain the future development of the business. The Company does not have any externally imposed capital requirements to which it is subject.

The Company defines capital as the aggregate of its shareholders' equity, long term debt and convertible debt. The Company manages the capital structure and makes adjustments to it in light of changes in economic conditions and the risk characteristics of the underlying assets. To maintain or adjust the capital structure, the Company may attempt to issue new shares or dispose of assets or adjust the amount of cash.

#### Note 10 Inventory

<b>Inventory</b>	
	<b>\$</b>
Balance as at December 31, 2019	34,115
Transferred from biological assets	2,647
Value-added product manufacturing and purchases	18,684
Adjustment to net realizable value	(3,160)
Inventory sold during the year	(8,085)
Changes in fair value of inventory sold	(7,319)
Balance as at June 30, 2020	36,882

Inventory is comprised of the following items:

	June 30, 2020	December 31, 2019
	<b>\$</b>	<b>\$</b>
Finished goods	22,080	27,067
Work-in- Progress	11,476	6,018
Supplies and consumables	1,728	1,030
Capitalized costs to Inventory	1,598	-
Total inventory	36,882	34,115

The fair value adjustment to biological assets and inventory sold consists of the following:

	Six months ended	
	June 30, 2020	June 30, 2019
	<b>\$</b>	<b>\$</b>
Realized fair value amounts included in inventory sold	7,380	487
Increase in fair value on growth of biological assets	(3,221)	(2,547)
Adjustment to net realizable value	3,160	-
<b>Fair value adjustment to biological assets and inventory sold</b>	<b>7,319</b>	<b>(2,060)</b>

**ALEAFIA HEALTH INC.**  
**Notes to the Consolidated Financial Statements**

For the periods ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

The adjustment to net realizable value is related to the write-down of the fair value component of the inventory due to the decrease in the estimated net realizable value of these inventories based on the evolving nature of the adult-use market.

**Note 11 Biological Assets**

Biological assets are valued in accordance with IAS 41. The Company’s biological assets consist of cannabis plants. As there is no actively traded commodity market for these, the valuation of these biological assets is obtained using valuation techniques where the inputs are based upon unobservable market data which are considered to be level 3 inputs under IFRS. These inputs are subject to volatility in market prices and several uncontrollable factors could significantly affect the fair value of biological assets in future. The fair value is determined using a valuation model to estimate expected harvest yield per plant applied to the estimated price per gram less processing and selling costs. The Company capitalizes all the direct and indirect costs as incurred related to the transformation of biological assets and measures biological assets consisting of cannabis plants at fair value less cost to sell up to the point of harvest, which becomes the basis for the cost of finished goods inventories after harvest. Unrealized gains or losses arising from changes in fair value less cost to sell during the year are included in the results of operations of the related year.

The Company’s estimates are subject to change and differences from the anticipated yield will be reflected in the gain or loss on biological assets in future years. As of June 30, 2020, the biological assets strains at the flowering phase were on average 74% and 12.5% complete for indoor plants and strains and outdoor plants respectively. As of June 30, 2020, it was estimated that the Company’s biological assets would yield approximately 66,000 kilograms of medical cannabis when harvested.

The following table depicts the changes in the fair value measurement (unrealized gain/loss resulting from fair value changes on growth of biological assets) and the fair value of biological assets as of June 30, 2020 as required by IFRS 13 fair value measurement.

The carrying value of biological assets are as follows:

<b>Biological assets</b>		<b>\$</b>
Balance as at December 31, 2019		971
Changes in fair value less costs to sell due to biological transformation		3,221
Production costs capitalized to biological assets		622
Transferred to Inventory upon harvest		(2,647)
<b>Balance as at June 30, 2020</b>		<b>2,167</b>

	Estimated KGs	Estimated total
	#	\$
<b>Biological assets transferred to inventory</b>	<b>665</b>	<b>2,647</b>

In determining the fair value of biological assets, management had made the following estimates in the valuation model:

<b>Significant assumptions</b>	<b>Indoor</b>	<b>Outdoor</b>
Average transfer price per gram (\$)	4.50	0.25
Average yield per plant (grams)	129	750
Average stage of growth (weeks)	6	16

## ALEAFIA HEALTH INC.

### Notes to the Consolidated Financial Statements

For the periods ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

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The Company values medical cannabis plants at fair value. Management determined cost approximates fair value from the date of receiving the vegetative plants until halfway through the flowering cycle of plants. Measurement of the biological transformation of the plant at fair value begins in the fourth week prior to harvest and is recognized evenly until the point of harvest. The number of weeks in the growing cycle is between twelve and sixteen weeks from propagation to harvest.

Management has quantified the sensitivity of the inputs and determined the following:

**a) Selling price per gram**

A decrease in the average selling price per gram by 5% would result in the biological asset value decreasing by \$123,117 and inventory decreasing by \$12,079.

**b) Harvest yield per plant**

A decrease in the harvest yield per plant of 5% would result in the biological asset value decreasing by \$39,194.

The unrealized gain for biological assets for the six months ended June 30, 2020 was \$3.2 million (June 30, 2019 - \$2.5 million).

## Note 12 Investments

On November 22, 2018, the Company entered into a Master Joint Venture Agreement (“the Agreement”) with SPE Finance LLC (“SPE”) to establish a joint venture for the purpose of owning and managing retail stores with a focus on selling cannabis and cannabis-related products across Canada and internationally (excluding the United States of America). The intention is to create, fund and govern the operations of the joint venture in the form of a corporation to carry on business. The joint venture was incorporated under the name One Plant (Retail) Corp. (“OPC”).

The Company paid \$4.0 million for the issuance of 99 common shares of OPC and as a result owns 9.9% of the outstanding common shares of OPC. On April 1, 2020 Flying High Inc invested \$0.8 million in OPC and the Company recorded the transaction as an investment. For accounting purposes, the Company classified its interest in OPC at fair value through profit and loss and as an investment.

The Company invested \$0.1 million in CannaPacific in January 2019 and \$0.5 million in April 2019.

## Note 13 Convertible Debt

### Emblem Convertible Debt

On completion of the Arrangement, Aleafia Health assumed the obligations of the convertible debentures previously issued by Emblem Corp. in February 2018 pursuant to a supplemental trust indenture dated March 2019 (the “Supplemental Indenture”). These convertible debentures were originally sold at a price of \$1,000 per unit for gross proceeds of \$25.0 million. Under the Supplemental Indenture, the convertible debentures are subject to the following terms:

- a maturity date of February 2, 2021;
- an interest rate of 8% per annum, payable semi-annually;



## ALEAFIA HEALTH INC.

### Notes to the Consolidated Financial Statements

For the periods ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

- convertible at \$2.3875 per share, subject to adjustment in certain events, at the option of the holder; and
- Aleafia Health may require the conversion of the full principal amount of the outstanding convertible debentures at the conversion price on not less than 30 days' notice, should the daily volume weighted average trading price of the outstanding common shares of Aleafia Health on the TSX be greater than \$4.12 for any 10 consecutive days.

#### Aleafia Convertible Debt

In June 2019, the Company issued 40,250 additional convertible debentures units (the "Aleafia Convertible Debt Unit") for gross proceeds of \$40.3 million. The Aleafia Convertible Debt Unit consists of one \$1,000 principal amount of unsecured convertible debenture of the Company and 680 common share purchase warrants, under the following terms:

- A maturity date of June 27, 2022.
- An interest rate of 8.5% per annum; payable semi-annually.
- Convertible at \$1.55 per share until June 27, 2022 at the option of the holder; and
- The Company may require conversion of the full principal amount outstanding convertible debenture at the conversion price on not less than 30 days' notice, should the daily volume weighted average trading price of the outstanding common shares of the Company on the TSX be greater than \$3.10 for 20 consecutive trading days.

In fiscal year 2019 certain debenture debt holders converted \$2.6 million debentures to 2,094,666 equity shares.

	<b>June 30, 2020</b>
	\$
Balance at beginning of the period	51,009
Amortization of transaction costs	831
Amortization of present value discounts	1,902
<b>Balance at end of the period</b>	<b>53,742</b>
Current portion of Convertible debt	22,681
Long term portion of Convertible debt	31,061

## Note 14 FINANCIAL INSTRUMENTS AND FINANCIAL RISKS

### Fair Value of Financial Instruments

The Company's financial instruments consist of cash and cash equivalents, marketable securities, Trade receivables, investments, accounts payable, lease liability, deferred revenue and convertible debt. The following table summarizes the carrying values of the Company's financial instruments by measurement category:

**ALEAFIA HEALTH INC.**  
**Notes to the Consolidated Financial Statements**

For the periods ended June 30, 2020 and 2019  
(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

	June 30, 2020	December 31, 2019
	\$	\$
FVTPL (i)	62,373	47,315
Assets, amortized cost (ii)	9,349	4,847
Liabilities, amortized cost (iii)	75,224	72,449

- (i) Cash and cash equivalents, investments and marketable securities
- (ii) Accounts receivable
- (iii) Accounts payable, lease liability, deferred revenue, current income tax liability and convertible debt

The Company classifies its fair value measurements in accordance with an established hierarchy that prioritizes the inputs in valuation techniques used to measure fair value as follows:

- 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.

The following table sets for the Company's financial assets measured at fair value on a recurring basis by level within the fair value hierarchy:

	Fair Value Measurements Using			Total
	Quoted Prices in Active Markets For Identical Instruments (Level 1)	Significant Other Observable Inputs (Level 2)	Significant Unobservable Inputs (Level 3)	
	\$	\$	\$	\$
Cash	45,399	-	-	45,399
Marketable securities	10,000	-	1,558	11,558
Investments	-	5,416	-	5,416
<b>Total</b>	<b>55,399</b>	<b>5,416</b>	<b>1,558</b>	<b>62,373</b>

The carrying value of trade receivables, accounts payable and deferred revenue are a reasonable approximation of their fair value due to their short-term nature. The carrying value of lease liability and convertible debt are a reasonable approximation of their value based on market interest rates for similar instruments as at June 30, 2020.

**Risk Management**

Effective risk management is fundamental to the success of the organization and is recognized as key in the Company's overall approach to strategy management. Aleafia has a strong, disciplined risk culture where managing risk is the responsibility shared by all of the company's employees.

The primary goals of the risk management are to ensure that the outcomes of risk-taking activities are consistent with Company's strategies and the risk appetite and that there is an appropriate balance between risk and reward in order to maximize shareholder value.

Aleafia has identified the below potential risk categories.

## ALEAFIA HEALTH INC.

### Notes to the Consolidated Financial Statements

For the periods ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

#### a) Currency risk

The Company's expenses are denominated in Canadian dollars. The Company's corporate office is based in Canada and current exposure to exchange rate fluctuations is minimal.

The Company does not have any significant foreign currency denominated monetary liabilities. The Company is attracting foreign investments and in future, the Company's financial assets and liabilities may comprise of foreign currency marketable securities, convertible notes, long term investments and promissory notes.

#### b) Interest rate risk

The Company is exposed to interest rate risk on the variable rate of interest earned on bank deposits. The fair value interest rate risk on bank deposits is insignificant as the deposits are short-term nature.

The Company has not entered any derivative instruments to manage interest rate fluctuations.

#### c) Credit risk

Credit risk is the risk of loss associated with the counterparty's inability to fulfill its payment obligations. Financial instruments that potentially subject the Company to concentrations of credit risks consist principally of cash and cash equivalents, trade and other receivables and short-term investments. The risk exposure is limited to their carrying values reflected on the statement of financial position. To minimize the credit risk the Company places these instruments with a high-quality financial institution. There are no expected credit losses as the Company does not invest in asset backed investments.

#### d) Liquidity risk

In the management of liquidity risk of the Company, the Company maintains a balance between continuity of funding and the flexibility through the use of borrowings. The Company manages liquidity risk through the management of its capital structure. As at June 30, 2020 the Company's contractual obligations consist of accounts payable and lease liability, which has a contractual maturity date within one year. Management closely monitors the liquidity position and expects to have adequate sources of funding to finance the Company's projects and operations.

### Note 15 Commitments and Contingencies

Commitments	Less than 2 years	2 to 5 years	Total
	\$	\$	\$
Plant construction contracts	1,000	-	1,000
Long term arrangements on facilities	1,854	2,851	4,705
<b>Total</b>	<b>2,854</b>	<b>2,851</b>	<b>5,705</b>

The Company also has car lease commitments. The minimum car lease payment is as follows.

Year	Amount (\$)
2020	7
2021	6

## **ALEAFIA HEALTH INC.**

### **Notes to the Consolidated Financial Statements**

For the periods ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

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Certain of Emblem's former executives have been named in a claim commenced March 20, 2015 in the Ontario Superior Court of Justice that also identifies Emblem and ECC in relation to certain services provided to the Emblem parties by an individual. The parties to the claim are: Amos Tayts (Plaintiff/Defendant by Counterclaim), Gordon Fox, Harvey Shapiro, Maxim Zavet, Levy Zavet Professional Corporation, MZ Prime Holdings Ltd., White Cedar Pharmacy Corporation, Emblem Corp. (Defendants), Emblem Cannabis Corporation ("ECC"), Kindcann.com, Inc. (Defendants/Plaintiffs by Counterclaim), and Talya Lev-Mor (Defendant by Counterclaim). The plaintiff has claimed \$10.0 million in damages for some unspecified combination of the value of shareholdings in Emblem of which he says he has been wrongfully deprived, the amount by which he claims Emblem has been directly or indirectly unjustly enriched as a result of his labours, and damages for breach of contract, misrepresentation and oppression. The claim is being contested and the action is currently at the discovery stage.

It is the Company's determination that the claim of \$10.0 million is primarily against the founders of Emblem and not the Emblem parties. The claim for damages against the Emblem parties, specifically, is not pleaded with sufficiency particularity to allow an accurate assessment of the quantum of damages being sought against the Emblem parties. The likely measure of damages sought will either be the market value of the services the plaintiff alleges to have provided to the Emblem parties or the degree to which Emblem was enriched by those services. The Company is of the view that the amount of the claim bears no relationship to the value of the services provided. The outcome of this legal matter is subject to negotiations by the officers of the Company and the Company believes it is unlikely to be impacted and accordingly, no amount has been provided for. A separate claim was also initiated by Tayts on March 22, 2019 in the Ontario Superior Court of Justice against Emblem and Emblem arising out of the same facts and seeking the same damages. The claim is contested but pleadings have not yet concluded.

In the ordinary course of business, from time to time, the Company may be involved in various claims related to its commercial and/or corporate activities. Although such matters cannot be predicted with certainty, management does not consider the Company's exposure to these claims to be material to these unaudited interim condensed consolidated financial statements.

## **Note 16 COVID-19 and its Impact on the Business Environment**

### **General outcome**

In December 2019, a novel strain of coronavirus ("COVID-19") emerged in China. Since then, it has spread to over a hundred other countries and infections have been reported around the world. Canada confirmed its first case of COVID-19 on January 25, 2020 and its first death related to COVID-19 on March 9, 2020. On March 11, 2020, the World Health Organization declared the outbreak of COVID-19 a global pandemic.

In response to the outbreak, governmental authorities in Canada and internationally have introduced various recommendations and measures to try to limit the pandemic, including travel restrictions, border closures, non-essential business closures, quarantines, self-isolations, shelters-in-place, and social distancing. The COVID-19 outbreak and the response of governmental authorities to try to limit it are having a significant impact on the private sector and individuals, including unprecedented business, employment and economic disruptions.

The continued spread of COVID-19 nationally and globally could have an adverse impact on the business, operations and financial results and position, including through disruptions to the Company's cultivation

## ALEAFIA HEALTH INC.

### Notes to the Consolidated Financial Statements

For the periods ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

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and processing activities, supply chains and sales channels, as well as a deterioration of general economic conditions including a possible national or global recession. Due to the speed with which the COVID-19 situation is developing and the uncertainty of its magnitude, outcome and duration, it is not possible to estimate its impact on business, operations or financial results and position. Further impacts could include an impact on our ability to maintain operations, to obtain and maintain debt and obtain equity financing on attractive commercial terms or at all, impairment of investments, impairments in the value of our non-current assets, or potential future decreases in revenue or the profitability of our ongoing operations, any of which could be material.

#### COVID-19 and other risks

##### Disruption of Supply Chain

Conditions or events including, but not limited to, those listed below could disrupt the Company's supply chains, interrupt operations at its facilities, increase operating expenses, resulting in loss of sales, delayed performance of contractual obligations or require additional expenditures to be incurred:

- extraordinary weather conditions or natural disasters such as hurricanes, tornadoes, floods, fires, extreme heat, earthquakes, etc.;
- a local, regional, national or international outbreak of a contagious disease, including the COVID-19 coronavirus, Middle East Respiratory Syndrome, Severe Acute Respiratory Syndrome, H1N1 influenza virus, avian flu, or any other similar illness could result in a general or acute decline in economic activity (see also, "Public Health Crises, including COVID-19");
- political instability, social and labour unrest, war or terrorism; or
- interruptions in the availability of basic commercial and social services and infrastructure including power and water shortages, and shipping and freight forwarding services including via air, sea, rail and road.

##### Public Health Crises, including COVID-19

A local, regional, national or international outbreak of a contagious disease, such as COVID-19, could have an adverse effect on local economies and potentially the global economy, which may adversely impact the price and demand for the Company's products. COVID-19 could affect the Company's ability to conduct operations and may result in temporary shortages of staff, to the extent its workforce is impacted.

Such an outbreak, if uncontrolled, could have a material adverse effect on the Company's business, financial condition, results of operations and cash flows, including a potential reduction in patient visits at the Company's Clinics and, as a result, potential lost revenue.

All three of the Company's production facilities continue to operate. To date there have been no material negative impacts on production due to COVID-19. The Company continues to expand core revenue-generating operations, with new hires completed in product sales, quality control and production.

On March 16, 2020, patients at Aleafia Health's network of medical cannabis clinics were notified that all physical clinic locations would be voluntarily and temporarily closed during the COVID-19 pandemic and that all patient consultations would be conducted through virtual clinic services. Since that time, approximately 3,300 patient consultations have been completed entirely remotely, ensuring that all patients maintain access to safe, secure and convenient cannabinoid therapy. As announced on October 17, 2018, the Company previously invested in the technology and training to offer scalable virtual clinic services.

## **ALEAFIA HEALTH INC.**

### **Notes to the Consolidated Financial Statements**

For the periods ended June 30, 2020 and 2019

(Amounts reflected in thousands of Canadian dollars, except share and per share amounts)

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Last-Mile Home Delivery: In recognition of the need for safe, contactless delivery of medical cannabis, the Company advanced its already planned introduction of last-mile home delivery for medical cannabis products. Following a soft-launch last week, the Company expects to make last-mile home delivery publicly available for Toronto-based registered Emblem patients next week.

In March, in addition to temporarily closing physical clinic locations, management enacted a series of measures to ensure business continuity and the safety of team members, including:

- Barring all visits to production facilities and cancelling all non-essential employee travel;
- Increased cleaning frequency throughout facility common areas and enforcing work from home for all non-production essential employees; and
- Adjustment to shift start times, shift length and break structure to eliminate the crossover between groups of employees.