Aleafia Health™

ALEAFIA HEALTH INC.

UNAUDITED CONDENSED CONSOLIDATED FINANCIAL STATEMENTS

(expressed in Canadian dollars)
For the three months ended
March 31, 2020 and 2019

AleafiaHealth.com

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MANAGEMENT'S RESPONSIBILITY

To the Shareholders of Aleafia Health Inc.:

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

May 13, 2020

"Geoff Benic"

Geoff Benic
Chief Executive Officer

"Benjamin Ferdinand"

Benjamin Ferdinand
Chief Financial Officer

ALEAFIA HEALTH INC.

Unaudited Interim Condensed Consolidated Statements of Financial Position

As at March 31, 2020 and December 31, 2019
(Amounts reflected in thousands of Canadian dollars)

`	Note	March 31, 2020	December 31, 2019
		$	$
ASSETS			
Current			
Cash and cash equivalents		33,380	41,247
Marketable securities		1,598	1,452
Trade receivables		7,230	4,847
Tax receivables		3,129	6,498
Prepaid expenses		5,007	5,756
Prepaid expenses for supply agreement		22,756	22,756
Inventory	10	29,094	34,115
Biological assets	11	425	971
		102,619	117,642
Non-current			
Prepaid deposit for property, plant and equipment		-	3,612
Property, plant and equipment	5	71,345	64,338
Deferred expenses		992	1,036
Right-of-use asset	4	941	1,071
Investments	12	4,616	4,616
Intangible assets	6	80,147	81,252
Goodwill	3	188,790	188,790
		346,831	344,715
TOTAL ASSETS		449,450	462,357
LIABILITIES			
Current			
Accounts payable and accrued liabilities	8	10,723	20,131
Lease liability	4	517	507
Convertible debt	13	21,917	-
Current income tax liability		1,700	-
Deferred revenue		76	101
		34,933	20,739
Non-current			
Lease liability	4	575	700
Convertible debt	13	30,423	51,009
Deferred tax liability		4,195	5,394
TOTAL LIABILITIES		70,126	77,842
SHAREHOLDER'S EQUITY			
Share capital	7	371,744	371,744
Warrants	7	44,701	44,701
Contributed surplus	7	36,866	35,901
Deficit		(73,987)	(67,831)
		379,324	384,515
TOTAL LIABILITIES AND EQUITY		449,450	462,357

COMMITMENTS AND CONTINGENCIES (Note 15)

Approved and authorized for issue on behalf of the board on May 13, 2020.

"Julian Fantino"	*"Lea Ray"*
Julian Fantino - 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 Three months ended March 31, 2020 and 2019

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

	Note	March 31, 2020	March 31, 2019
		$	$
Revenue			
Consultation services		635	626
Research		235	368
Sale of cannabis		13,963	531
Gross revenue		14,833	1,525
Excise taxes		237	-
Net revenue		14,596	1,525
Cost of sales			
Doctor services		469	463
Inventory expensed to cost of sales		2,052	1,325
Gross profit (loss) before fair value adjustment		12,075	(262)
Changes in fair value of inventory sold		6,179	-
Unrealized (gain) loss on fair value of biological assets	12	38	(205)
Gross profit (loss)		5,858	(58)
Expense			
Wages and benefits		2,487	2,988
General and administration		3,107	7,670
Business transaction costs		510	907
Bad debt expenses		104	-
Amortization and depreciation		2,014	868
Share-based payments		966	7,961
		9,188	20,394
Operating loss		(3,330)	(20,452)
Other (income) expense			
Interest expenses		2,648	121
Unrealized (gain) loss on securities		(281)	-
Non-operating (income) expense		(41)	315
		(2,326)	436
Net loss before income taxes		(5,656)	(20,888)
Income tax			
Current income tax expenses		1,700	-
Deferred taxes(recovery) / expense		(1,200)	(657)
Net loss after income taxes		(6,156)	(20,230)
Net loss and Comprehensive loss for the period		(6,156)	(20,230)
Loss per share, basic and diluted		(0.02)	(0.12)
Weighted average common shares outstanding		277,893,686	163,248,386

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 three months ended March 31, 2020 and March 31, 2019
(Amounts reflected in thousands of Canadian dollars, except share and warrant amounts)

March 31, 2020	Common shares		Warrants				
	Number of Shares	Amount	Number of Warrants	Amount	Contributed Surplus	Deficit	Total
	#	$	#	$	$	$	$
Balance, December 31, 2019	**277,893,686**	**371,744**	**60,264,816**	**44,701**	**35,900**	**(67,831)**	**384,514**
Warrants expired	-	-	(14,900,563)	-	-	-	-
Share-based payments	-	-	-	-	966	-	966
Net loss for the period	-	-	-	-	-	(6,156)	(6,156)
Balance, March 31, 2020	**277,893,686**	**371,744**	**45,364,253**	**44,701**	**36,866**	**(73,987)**	**379,324**

March 31, 2019	Common shares		Warrants				
	Number of Shares	Amount	Number of Warrants	Amount	Contributed Surplus	Deficit	Total
	#	$	#	$	$	$	$
Balance, December 31, 2018	**157,848,812**	**104,455**	**9,228,590**	**748**	**14,954**	**(28,224)**	**91,933**
Shares issued from warrants exercised	575,761	970	(575,761)	-	-	-	970
Shares issued from options exercised	497,789	770	-	-	(535)	-	235
Warrants deemed issued for Emblem	-	-	39,286,213	42,775	-	-	42,775
Share options deemed issued for Emblem	-	-	-	-	5,922	-	5,922
Shares issued for Emblem	110,823,349	252,677	-	-	-	-	252,677
Shares issued for services	2,331,255	5,315	-	-	-	-	5,315
Share-based payments	-	-	-	-	7,961	-	7,961
Net loss for the period	-	-	-	-	-	(20,230)	(20,230)
Balance, March 31, 2019	**272,076,966**	**364,188**	**47,939,042**	**43,523**	**28,301**	**(48,455)**	**387,558**

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 three months ended March 31, 2020 and 2019
(Amounts reflected in thousands of Canadian dollars)

	March 31, 2020	March 31, 2019
	$	$
Operating activities		
Net loss for the period	(6,156)	(20,230)
Adjustments for non-cash items:		
Depreciation	1,064	868
Amortization	1,105	-
Share-based consulting fees	-	5,315
Share-based payments	966	7,961
Accretion	1,331	195
Current income tax liability	1,700	-
Deferred income tax recovery	(1,200)	(657)
Unrealized loss on marketable securities	(281)	-
Changes in fair value included in inventory sold	6,179	-
Unrealized loss on fair value biological assets	38	(205)
	4,746	(6,754)
Changes in operating assets and liabilities		
Prepaid expenses	4,361	(401)
Trade receivables	(2,383)	(1,336)
Tax receivable	3,369	-
Marketable securities	134	315
Biological assets	(5,671)	168
Inventory	5,022	809
Accounts payable and accrued liabilities	(9,408)	(3,075)
Deferred revenues	(24)	(25)
Net cash generated by (used in) operating activities	146	(10,299)
Investing activities		
Investment in CannaPacific	-	(101)
Cash acquired on amalgamation	-	23,715
Deferred expenses	43	-
Sale proceeds of land	-	(4,088)
Acquisition of property plant and equipment	(7,941)	-
Net cash (used in) provided by investing activities	(7,898)	19,527
Financing activities		
Lease liability payments	(115)	(3)
Warrants and options exercised	-	1,205
Net cash provided by financing activities	(115)	1,202
Change in cash and cash equivalents	(7,867)	10,429
Cash and cash equivalents, beginning of period	41,247	26,407
Cash and cash equivalents, end of period	33,380	36,836

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

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, 2nd floor, Concord, Ontario and its corporate website is AleafiaHealth.com.

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 November 22, 2018, Aleafia acquired 51% interest in Flying High Brands Inc., a domestic and international cannabis brands company and a 9.9% stake in One Plant (Retail) Corp - a Canada-wide cannabis retail joint venture.

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". Emblem Shares were delisted from the TSXV on March 18, 2019.

As at March 31, 2020, the Company had not generated a profit and had accumulated a deficit of $73,987. The Company's operations and expenditures have been funded by the issuance of equity and convertible debts.

Note 2 Basis of Presentation

These unaudited condensed interim consolidated financial statements as at and for the three months ended March 31, 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 condensed interim consolidated financial statements are consistent with those of the previous fiscal year. These unaudited condensed interim 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 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.

Emblem Corp.

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 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.

At the date of acquisition, the provisional consideration paid, and estimated fair values of the assets and liabilities of Emblem were as follows:

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

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

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

Net assets acquired	$
Net tangible assets	74,584
Emblem brand	9,025
GrowWise brand	4,428
Symbl 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
Total net assets acquired	301,374

The resulting goodwill represents the sales and growth potential of Emblem Corp. and will not be deductible for tax purposes.

Note 4 Right-of-Use Asset and Lease Liability

RIGHT-OF-USE ASSET

	$
Cost	
Balance, December 31, 2019	1,591
Additions	-
Balance, March 31, 2020	1,591
Accumulated Amortization	
Balance, December 31, 2019	(520)
Amortization	(130)
Balance, March 31, 2020	(650)
Net book value, December 31, 2019	**1,071**
Net book value, March 31, 2020	**941**

LEASE LIABILITY

	$
Balance, December 31, 2019	1,207
Additions	-
Interest expense	61
Payments	(176)
Balance, March 31, 2020	1,092
Current portion of lease liability	**517**
Long-term portion of lease liability	**575**

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

Note 5 Property, Plant and Equipment

Cost	Computer and software	Equipment and furniture	Leasehold improvements	Land	Buildings and houses	Total
	$	$	$	$	$	$
Balance, December 31, 2019	758	12,025	5,452	7,637	40,447	66,319
Additions	48	434	-	100	7,204	7,786
Balance, March 31, 2020	806	12,459	5,452	7,737	47,651	74,105
Accumulated Depreciation						
Balance, December 31, 2019	(225)	(803)	(272)	-	(681)	(1,981)
Depreciation	(42)	(300)	(71)	-	(366)	(779)
Balance, March 31, 2020	(267)	(1,103)	(343)	-	(1,047)	(2,760)
Carrying Amounts						
Balance, December 31, 2019	533	11,222	5,181	7,637	39,764	64,338
Balance, March 31, 2020	539	11,356	5,109	7,737	46,603	71,345

Note 6 Intangible Assets

	Grow License	Patient List	Serruya License	Emblem Brands	Emblem License	Other	Total
Cost	**$**	**$**	**$**	**$**	**$**	**$**	**$**
Balance, December 31, 2019	9,358	11,461	12,260	15,100	34,000	3,195	85,374
Balance, March 31, 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	(98)	(310)	(205)	(40)	(354)	(98)	(1,105)
Balance, March 31, 2020	(489)	(1,552)	(1,090)	(170)	(1,476)	(450)	(5,227)
Carrying Amounts							
As at December 31, 2019	8,967	10,219	11,375	14,970	32,878	2,843	81,252
As at March 31, 2020	8,869	9,909	11,170	14,930	32,524	2,745	80,147

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

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 March 31, 2020, there were 277,893,686 common shares issued and outstanding

Warrants

As at March 31, 2020 the Company had following warrants outstanding.

	Warrants outstanding	Weighted average exercise price
	#	$
Outstanding and exercisable , December 31, 2019	60,264,816	2.05
Warrants expired	(14,900,563)	3.49
Outstanding and exercisable, March 31, 2020	45,364,253	1.58

At March 31, 2019, the Company had outstanding warrants entitling the holders to acquire additional common shares as follows:

Outstanding and exercisable	Expiry date	Warrants	Weighted average exercise price
		#	$
Warrants Issued by Aleafia	June 11, 2020 - June 27, 2022	8,674,190	1.67
Legacy warrants issued by Emblem	Dec 6, 2019 - Dec 6, 2021	39,264,852	2.02
Outstanding and exercisable, March 31, 2019		**47,939,042**	**1.96**

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 March 31, 2020:

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

	Number of Options	Weighted Average Exercise Price for Options
	#	$
Options outstanding, December 31, 2019	24,979,725	1.22
Options Issued	1,126,000	0.55
Options expired	(1,361,262)	1.83
Options outstanding, March 31, 2020	24,744,463	1.16
Vested, March 31, 2020	**17,331,545**	**1.24**
Unvested, March 31, 2020	**7,412,918**	**0.98**

Restricted share units ("RSU")

The Company has an 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.

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 year quarter ended March 31,2020 and March 31, 2019, the Company had the following transactions with the officers and directors of the Company.

	March 31, 2020	March 31, 2019
Wages & Benefits: Directors	$166	$700
Wages & Benefits: Management	$434	$345
Accounts payable and accrued liabilities: Directors	$251	$700
Accounts payable and accrued liabilities: Management	$25	$61
Share based compensation: Directors	$69	-
Share based compensation: Management	$682	-

As at March 31, 2020, the amount of $0.3 million was due to directors and management. The amounts are non-interest bearing, unsecured and are due upon demand.

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

Note 9 Management of Capital

The Company's objectives when managing capital are to sustain 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

Inventory	
	$
Balance, December 31, 2019	34,115
Transferred from biological assets	1,769
Inventory purchased	1,441
Inventory sold during the year	(2,052)
Changes in fair value of inventory sold	(6,179)
Balance, March 31, 2020	29,094

	March 31, 2020	December 31, 2019
	$	$
Finished goods	22,144	27,067
Work-in-progress	2,641	6,018
Supplies and consumables	4,309	1,030
Total inventory	29,094	34,115

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 trading 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 at March 31, 2020, the biological assets strains at the flowering phase were on average 30% complete for indoor plants and strains. As of March 31, 2020, it was estimated that the Company's biological assets would yield approximately 51,038 grams 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 March 31, 2020 as required by IFRS 13 fair value measurement. The carrying value of biological assets are as follows:

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

Biological assets	
	$
Balance, December 31, 2019	971
Changes in fair value less costs to sell due to biological transformation	(38)
Production costs capitalized to biological assets	1,261
Transferred to inventory upon harvest	(1,769)
Balance, March 31, 2020	425

	Estimated KGs	Estimated total
	#	$
Biological assets transferred to inventory	390	1,769

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

Significant assumptions	Indoor	Outdoor
Average transfer price per gram ($)	4.50	1.25
Average yield per plant (grams)	129	1000
Average stage of growth (weeks)	6	12

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 and inventory decreasing by $12.

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.

The unrealized (gain) loss for biological assets for the three months ended March 31, 2020 was $38 (March 31, 2019 - $(205)).

Note 12 Investment

On November 22, 2018, the Company entered into a Master Joint Venture Agreement with 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. The Company paid $4.0 million for the issuance of 99 common shares of One Plant and as a result owns 9.9% of its outstanding common shares. For accounting purposes, the Company classified its interest in One Plant at fair value through profit and loss and as an investment.

The Company invested in shares of $0.1 million in CannaPacific Pty Limited ("CannaPacific") in January 2019 and $0.5 million in April 2019. For accounting purposes , the Company classified its interest in OPC and CannaPacific at fair value through profit and loss.

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;
- 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

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

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.

Debenture debt holders converted $2.6 million debentures to 2,094,666 equity shares.

Convertible debt	
	$
Balance, December 31, 2019	51,009
Amortization of transaction costs	415
Amortization of present value discounts- Accretion	916
Balance, March 31, 2020	52,340
Current portion of Convertible debt	21,917
Long term portion of Convertible debt	30,423

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:

	March 31, 2020	December 31, 2019
	$	$
FVTPL (i)	39,594	47,315
Assets, amortized cost (ii)	7,230	4,983
Liabilities, amortized cost (iii)	65,931	71,959

(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 priorities 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:

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

Fair value measurements using	Quoted prices in active markets for identical instruments	Significant other observable inputs	Significant unobservable inputs	
	(Level 1)	(Level 2)	(Level 3)	Total
	$	$	$	$
Cash	33,380	-	-	33,380
Marketable securities	-	-	1,598	1,598
Investments	-	4,616	-	4,616
Total	33,380	4,616	1,598	39,594

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 rate for similar instruments as at March 31, 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.

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 principal business of the Company is the identification and evaluation of assets or a business and once identified or evaluated, to negotiate an acquisition or participation in a business subject to receipt of shareholder approval and acceptance by regulatory authorities. The Company is attracting foreign investors and in future, the Company's financial assets and liabilities will 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.

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

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 March 31, 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	< 2 years	2-5 years	Total
	$	$	$
Plant construction contracts	2,550	-	2,550
Long-term arrangements on office space	1,152	278	1,430
Service contracts	88	-	88
Total	3,790	278	4,068

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

Year	Amount ($)
2020	13
2021	5

On October 8, 2019 Aleafia Health announced that Emblem had terminated its long-term supply agreement with Aphria Inc. dated September 11, 2018 in accordance with its terms as a consequence of Aphria's failure to meet its supply obligations. The matter was referred to confidential arbitration. Emblem is seeking the return, in full, of its initial deposit in addition to damages. There are currently several unresolved disputes between the parties relating to the termination to be addressed at the arbitration. Aphria has denied liability and has issued a counterclaim against Emblem and Aleafia Health for damages. The Company's deposit has been recorded as a current asset in the consolidated statements of financial position.

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, Kindcann.com, Inc. (Defendants/Plaintiffs by Counterclaim), and Talya Lev-Mor (Defendant by Counterclaim). The plaintiff has claimed $10 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 consolidated financial statements.

Note 16 NOTABLE SUBSEQUENT EVENTS

a) **Paris Facility Phase II and Port Perry Outdoor Expansion Licences.**

On May 4, 2020, the Company announced that Emblem had secured a Health Canada Licence Amendment for the Paris Phase II expansion of its Paris Facility. The amendment was granted on May 1, 2020, expires on July 26, 2022 and authorizes cannabis production in the entire expanded building.

On May 12, 2020, the Company's wholly owned subsidiary Aleafia Farms Inc. has secured a Health Canada Licence Amendment for its Port Perry Facility's outdoor cultivation expansion. The expansion adds an additional 60 acres of outdoor cultivation area, bringing the total to 86 acres (3.7 million sq. ft.) The amendment was granted on May 12, 2020, expires on October 13, 2020 and authorizes cannabis cultivation in "Outdoor Grow Area 5".

b) **Company's directors resignation and new directors appionment**

On May 8,2020 the Company announced that director Bill Stewart has indicated his intention to resign from the Company's Board effective May 15 along with outgoing directors Julian Fantino and Raf Souccar. As previously announced, two new independent directors, Rhonda Lawson and Glenn Washer will be appointed to the Board on May 16. The new Board will be composed entirely of independent members, furthering the Company's goal of enacting strong corporate governance and best practices.

c) **$13 Million Bought Deal Offering.**

On May 11, 2020, the Company announced that it entered into an agreement with Eight Capital, lead underwriter and sole bookrunner, on behalf of a syndicate of underwriters (together, the

"Underwriters"), pursuant to which the Underwriters have agreed to purchase 20,000,000 units of the Company (the "Units"), on a "bought deal" basis pursuant to a short form prospectus offering, subject to all required regulatory approvals, at a price per Unit of $0.65 for gross proceeds of $13,000.

Note 17 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 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 conduct operation 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 our 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.

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.
- Adjustment to shift start times, shift length and break structure to eliminate the crossover between groups of employees.