AUXLY CANNABIS GROUP INC.

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

FOR THE THREE AND TWELVE MONTHS ENDED DECEMBER 31, 2020

Dated April 23, 2021

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MANAGEMENT'S DISCUSSION AND ANALYSIS

This Management's Discussion and Analysis ("**MD&A**") was prepared as of April 23, 2021 unless otherwise indicated. This MD&A reviews the operating results, financial position and liquidity of Auxly Cannabis Group Inc. ("**Auxly**", "**we**", "**our**", or the "**Company**"). All amounts are stated in millions of Canadian dollars unless otherwise noted, except common shares ("**Shares**"), options, and per Share amounts. This MD&A should be read in conjunction with the consolidated financial statements and the notes thereto for the year ended December 31, 2020.

This MD&A may contain forward-looking information that is based on the Company's expectations, estimates and projections regarding its business and the economic environment in which it operates. Forward-looking information contained herein is made as of the date of this MD&A and is not a guarantee of future performance and involves risks and uncertainties that are difficult to control or predict. Readers should refer to the "*Forward Looking Statements*" section in this MD&A.

DESCRIPTION OF BUSINESS

Our Business

We are a leading Canadian consumer packaged goods company in the cannabis products market, headquartered in Toronto, Canada. Our focus is on developing, manufacturing and distributing branded cannabis products that delight wellness and recreational consumers.

Our vision is to be a global leader in branded cannabis products that deliver on our consumer promise of quality, safety and efficacy.

Canadian Market

On October 17, 2018, the Cannabis Act came into force, initially permitting the recreational sale of certain classes of cannabis products, including dried cannabis, fresh cannabis, cannabis plants, cannabis seeds, and cannabis oil (collectively referred to as "**Cannabis 1.0 Products**"). On October 17, 2019, edible cannabis, cannabis extracts and cannabis topicals were added to the authorized classes of cannabis (collectively referred to as "**Cannabis 2.0 Products**", and together with Cannabis 1.0 Products, collectively referred to as "**Cannabis Products**") and such Cannabis 2.0 Products were first available for sale on December 16, 2019. Since 2019, Health Canada undertook a consultation, established a Scientific Advisory Committee, and has been engaged in discussions regarding the possible legalization of Cannabis Health Products ("**CHPs**"), which would permit the making of health claims in respect of cannabis products without the required oversight of a practitioner such as a doctor. Auxly submitted a response to the consultation, is actively participating in those discussions with Health Canada and is looking forward to the possibility that the authorized classes of cannabis will expand to include CHPs and other derivative product formats ("**Cannabis 3.0 Products**").

Canadian Strategy and Capabilities

Brand Portfolio and Product Offering

We have created a portfolio of brands designed for a broad market of cannabis consumers, with differentiation in price points across targeted consumer segments.

Back Forty. *Take a trip and explore the Back Forty.*

Back Forty requires no introduction because it already feels familiar, with a product suite that fits seamlessly into the day-to-day with the simple purpose of providing a better experience for less.

Foray. *See cannabis differently.*

Foray is an accessible entry point for anybody, at any stage of their cannabis journey. Designed for the curious, Foray is approachable and wants to celebrate and guide one's foray into cannabis.

Dosecann. *Cannabis – down to a science.*

Dosecann is a world-class developer of innovative cannabis products for the wellness-focused consumer. Built on the pillars of quality, safety and efficacy.

Kolab Project. *Embrace the unexpected.*

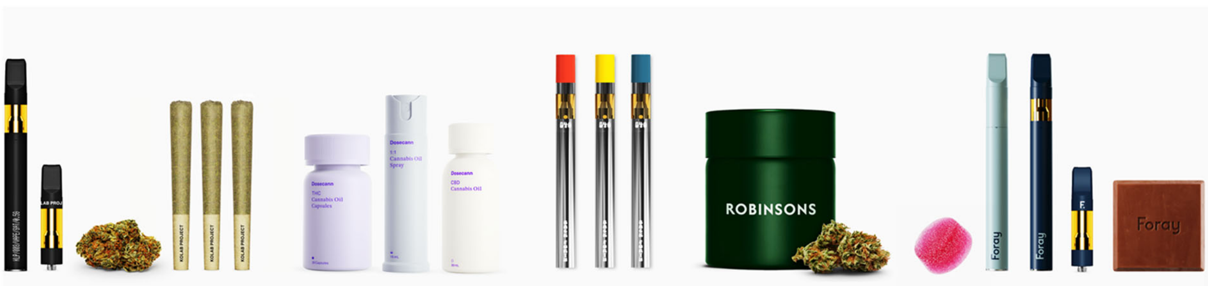
Kolab Project is dedicated to supporting and celebrating the intersection of cannabis and culture. The Kolab Project mission is to provide cannabis enthusiasts with a carefully curated selection of exceptional cannabis, accessories and experiences.

Robinsons. *Canada's premier producer of fine-crafted cannabis.*

Nestled in the heart of Nova Scotia's Annapolis Valley, Robinsons cultivates fine cannabis. Always small-batch and hand-tended, Robinsons is grown for and best enjoyed by the discerning consumer. Driven by an unwavering commitment to craft and relentless pursuit of growing the best cannabis — cannabis that is known simply as Robinsons.

Based upon consumer insights, Auxly has developed a broad portfolio of Cannabis Products to meet the evolving needs and preferences of Canadian cannabis consumers. We have focused on the development of Cannabis 2.0 Products and were one of the first cannabis companies to distribute and sell Cannabis 2.0 Products across Canada starting in mid-December 2019, and we were the top-selling licensed producer of Cannabis 2.0 Products nationally in 2020.

Our Cannabis Products available during the fourth quarter of 2020 are described below by brand and product format:



Products Available by Brand

KOLAB PROJECT	Dosecann Cannabis Solutions	BACK FORTY	ROBINSONS	Foray
Chocolates Vape cartridge starter packs 510 Vape cartridges All-in-one vape pens Pre-rolled cannabis Dried Flower	Cannabis oil drops Capsules	510 Vape cartridges	Dried Flower*	Soft Chews Chocolates Vape cartridge starter packs 510 Vape cartridges All-in-one vape pens Hard Candy

*Currently only available in Alberta, Nova Scotia, Ontario and Newfoundland

Our Cannabis Products have been well received by consumers. We plan to further strengthen our brand recognition and use consumer insights to drive innovation as we continue to introduce new Cannabis Products to the Canadian market.

January 2021 → December 2021

						
Kolab Project 232 Series Diamonds are single-strain concentrates extracted from fresh, flash-frozen cannabis flower.	Dosecann Daily Relief CBD Cream is a high-quality, high-potency cream that uses a tested formula to deliver CBD while hydrating the skin.	Back Forty and Kolab Project's launch of format disruptive, unique, high potency and strain-specific pre-rolls.	Back Forty's strain-specific and high THC potency dried flower offering, with the initial launch of Pine Kush, available in 3.5g and 28g units.	Launching new and exciting chocolate and chew flavour profiles in our edible product category under Foray, Back Forty and Kolab Project.	Dosecann CBD AhiFlower oil, a high-potency CBD extract blend infused with omega-rich Ahiflower Oil and a built-in dropper that delivers 2.5 mg of CBD over 4 drops.	New innovative seasonal chocolates and chews for consumers to enjoy and celebrate special occasions.

Distribution

Given the current provincial legislative framework in Canada, we have pursued a multifaceted strategy to gain access to Canadian consumers. This includes supply arrangements with provincial control boards and retailers, including our partnership with Medical Cannabis by Shoppers Drug Mart Inc., a brokerage agreement with Kindred Partners Inc. ("**Kindred**") to act as our strategic sales agent, and strong relationships with leading retailers, including Inner Spirit Holdings Ltd. and Delta 9 Cannabis Inc.

We have secured listings and sold our Cannabis Products in all provinces except Quebec (where the regulations for Cannabis 2.0 Products are more restrictive). We have obtained the necessary pre-authorization to enter into public contracts in Quebec and continue to explore listings for certain products that comply with Quebec's regulatory requirements.

Cannabis Operations, Product R&D and Manufacturing

<u>Dosecann</u>

In May of 2018, we acquired our subsidiary Dosecann LD Inc. ("**Dosecann**"), and its purpose-built, GMP-compliant cannabis processing facility located in Charlottetown, Prince Edward Island. The Company conducts its primary extraction, product development, manufacturing and R&D activities for its Cannabis Products in-house at the Dosecann facility. Dosecann holds licences for processing, analytical testing and research under the Cannabis Act. The majority of the first floor of the two-story, 52,000 square foot facility is currently licenced under the Cannabis Regulations for the production, storage and sale of Cannabis Products. As of May 12, 2020, Health Canada streamlined its site expansion process whereby licence holders are no longer required to submit certain amendments for approval by Health Canada. This reduces the regulatory burden for site expansion and increases Health Canada's capacity to review applications that must be submitted. Under the revised site expansion process, Dosecann will not be required to seek further Health Canada approval for operational areas on the second floor of the facility, but any additional secure storage areas will require a formal licence amendment submission and approval. Construction of the interior of the second floor of the Dosecann facility is complete. During the third quarter of 2020, operational activities began to transition from the first to second floor with chews, capsules and hard candy production being moved to the newly constructed second floor, and vapes and oils remaining in production on the first floor. With the additional space and equipment at the Dosecann facility to produce products at commercial scale, combined with the continued development of automation and on-going efforts to reduce the cost of input materials and packaging, we anticipate that improvements in gross margins will be achieved.

Product development is led by Dosecann's team, who have experience in the pharmaceutical, food, scientific research and product development fields. As the Company's manufacturing hub, the Dosecann facility provides the Company with the ability to be responsive to changing industry regulation and evolving consumer preferences. On June 25, 2020, Dosecann was granted a research licence from Health Canada pursuant to the Cannabis Act, which permits Dosecann to administer cannabis extracts, edible cannabis and cannabis topicals to human subjects for purposes of palatability and sensory testing. With the research licence, Dosecann can conduct broader in-house testing, incorporating consumer input and feedback on attributes such as flavour, aroma, texture or mouthfeel, to better evaluate later-stage product formulations. Product development is overseen by our safety board, comprised of members from Auxly, Dosecann, KGK Science Inc. ("**KGK**") and Imperial Brands PLC ("**Imperial Brands**"), which has oversight of the controls in place to ensure the safety, quality and efficacy of the Company's products.

As at December 31, 2020, the Company has contributed approximately $49.9 million towards the construction and development of the Dosecann facility and is considering approximately $2.5 to $4.0 million of additional expenditures comprised of several pieces of automation equipment across several product categories, expanding extraction capabilities and throughput and security enhancements within the next 9 months, and a further $1.3 million in March of 2022.

Kolab Project

In October 2017, we acquired our subsidiary Kolab Project Inc. ("**Kolab**") and its facility located just outside of Ottawa in Carleton Place, Ontario. Kolab holds licences for cultivation and processing under the Cannabis Act. In 2020, we made the strategic decision to cease cultivation at the Kolab facility and shift our focus to the manufacturing, processing and distribution of pre-rolled and dried flower Cannabis Products. In addition to its current operations, Kolab provides us with flexibility to manufacture, produce and distribute other Cannabis Products as necessary. Kolab's curated Growers Series has included successful product launch collaborations with Lotus Cannabis Co., Safari Flower Co. and Robinsons. These Kolab Project collaborations strive to deliver a curated selection of unique strains to cannabis enthusiasts across the country while transparently showcasing the craftsmanship of talented cultivators of incredible cannabis by acknowledging the cultivator on our packaging.

The Company has undertaken a new capital project, at an estimated cost of $5.5 - $6.5 million, to increase pre-roll production volumes at Kolab through the purchase, installation and commissioning of automated manufacturing and packaging equipment and minor associated building alterations, which is expected to quintuple output from the facility. The manufacturing equipment will be installed and commissioned during the second quarter of 2021, with packaging automation expected to occur during the third quarter of 2021.

KGK Science

KGK, the Company's wholly owned contract research organization located in London, Ontario, provides regulatory, research and clinical trial services to the nutraceutical, natural health product and cannabis industries. KGK has an active research licence allowing for the possession and administration of cannabis for the purposes of a clinical trial. On September 22, 2020, KGK received its second research licence, which permits KGK to conduct product palatability and sensory testing of cannabis extracts, edible cannabis topicals with human subjects. On December 21, 2020, KGK received an Institutional Cannabis Research Licence from Health Canada which provides the broad approval to conduct multiple cannabis research projects, removing the need to obtain individual Research Licences for each project. KGK works with its clients in substantiating claims for their products through randomized clinical trials in addition to providing other research and regulatory services such as participant recruitment, regulatory compliance solutions, research support services and consulting.

Curative Cannabis

On November 27, 2019, Auxly accepted certain share collateral of 2368523 Ontario Inc. (d/b/a Curative Cannabis) ("**Curative**") in satisfaction of secured debt obligations owing to Auxly by Curative pursuant to an Order of the Ontario Superior Court of Justice (Commercial List) made in foreclosure proceedings under the *Ontario Personal Property Security Act*, RSO 1990. As a result, the Company holds a 96% share interest in Curative. Curative's assets include an approximately 30,000 square foot cannabis cultivation facility situated on 33 acres of land in Chatham-Kent, Ontario. Curative currently holds licences for cultivation and processing under the Cannabis Act. To date, the Company has contributed approximately $20.4 million towards the construction and development of the Curative facility. The Company is currently exploring all possible options with respect to the use, commercialization and/or sale of the asset. No further material expenditures are required by the Company at this time, but if and when the Company decides to begin active operations at the Curative facility, the Company estimates additional capital expenditures of approximately $0.9 million would be required to finish the facility for the purpose of cannabis cultivation; however, such expenditures may increase depending on the Company's final intended use of the facility.

Cultivation Supply

We have established a diversified supply chain that provides a secure and cost-efficient source of raw cannabis, comprised of a combination of wholly owned subsidiaries, a joint venture and offtake agreements. Having a flexible cultivation platform allows for a consistent source of raw input material for the manufacture of our Cannabis Products. To meet our commercial objectives for Cannabis Product sales while the Company's joint venture project Sunens Farms Inc. ("**Sunens**") was under development, we opportunistically purchased approximately 81% of our cannabis inventory (dried cannabis and resin) in the open market during 2020. The majority of the Company's current CBD inventory was purchased from licenced hemp sellers in Prince Edward Island.

A summary of our key cultivation sources is below:

<u>Sunens</u>

Sunens is the Company's large-scale joint venture with partner Peter Quiring, which is comprised of a 1.1 million square foot greenhouse in Leamington, Ontario.

Funding for the project budget was provided by the Company in the form of an equity contribution and a subordinated promissory note totaling approximately $98.5 million provided prior to 2020, and a $84 million secured facility underwritten by a syndicate of lenders led by the Bank of Montreal ("**BMO**"). The Company's contribution along with the credit facility comprise all the required expenditures for the entire 1.1 million square foot facility. As part of such financing provided by the syndicate led by BMO, the Company has guaranteed payments up to $33 million in the event of default. In addition, both the Company and its partner Peter Quiring have agreed to fund any cost overruns on the construction of the facility and maintain combined cash and available credit balances of at least $15 million. As at December 31, 2020, approximately $11 million of the facility remained undrawn and Sunens was in compliance with the lending covenants.

In June of 2020, Sunens received a standard cultivation licence from Health Canada for approximately 360,000 square feet of cultivation, processing and storage space. The Company determined the most expedited licensing pathway for the remaining space would be achieved by submitting two additional licensing amendment applications for Health Canada's approval to expand the site perimeter for the remaining cultivation and additional processing and storage space in the facility. The first of these two licensing amendments was submitted and approved, granting Sunens the use of an additional 409,684 square feet of cultivation and storage space. The Company is currently evaluating the site perimeter expansion that would be necessary to meet Sunens' requirements for additional processing and storage space, and anticipates the second licensing amendment application to expand the site perimeter will be submitted in the second half of 2021. In order to provide further commercial flexibility, Sunens also applied for a processing licence, which was issued by Health Canada on November 13, 2020. Sunens commenced cultivation within the licenced area upon receiving its licence in June 2020, and during the first quarter of 2021 has sold products to the Company and other licenced producers.

On November 2, 2020, in connection with an amendment to the off-take agreement between the Company and Sunens to provide the Company with more favourable pricing, the Company amended the subordinated promissory note it has with Sunens so that all interest accrued to date has been waived and interest will not start to accrue until January 1, 2023. During the fourth quarter of 2020 the Company recognized a loss associated with the recoverable value of the promissory note, see "*Fourth Quarter Results of Operations*".

On February 8, 2021, at the request of the lending syndicate, the Company and its joint venture partner contributed $2 million in the aggregate to provide additional cash reserves to support operating cash flows (with the Company proportionately contributing $0.9 million of such amount). In addition, revenue milestones of $3.45 million and $7.15 million for the first and second quarters, respectively, of 2021 (the "**Revenue Milestones Requirement**") were established.

On April 16, 2021, Sunens received a notice of default from BMO in its capacity as lender, administrative agent and syndication agent under the credit facility with respect to Sunens' failure to satisfy the Revenue Milestones Requirement. Although the lenders have reserved their rights under the credit agreement, they advanced another $1 million pursuant to a borrowing request made pursuant to the credit facility and BMO has granted a one-month deferral of the equipment loan payment due in May 2021 in the amount of approximately $0.2 million which will be used to fund day-to-day operations. In addition, Sunens may require additional funding for working capital until production and revenue from sales reach expected levels. Discussions with the lenders with respect to a formal credit amendment and/or forbearance agreement are continuing in a collaborative and positive manner, although there can be no assurance that an agreement with the lenders will be reached.

Subject to reaching an acceptable accommodation with the lenders, the joint venture partners are considering additional costs to optimize the processing and storage capabilities of the Sunens facility which may be funded by the joint venture partners and/or lenders; however, a reasonable estimate of any such costs is not determinable at this time. The Company anticipates that it will transition Sunens to become one of its primary suppliers of cannabis inventory over the course of 2021.

<u>Robinsons</u>

Robinsons Cannabis Incorporated ("**Robinsons**") holds licences for cultivation and processing under the Cannabis Act for its purpose-built 27,700 square foot indoor cannabis cultivation facility located in Kentville, Nova Scotia, and is focused on the production of high-quality craft cannabis. Initial shipments of Robinsons dried cannabis products commenced in July 2020. Robinsons has entered into supply arrangements with Alberta, Ontario, Nova Scotia, Newfoundland and Labrador, and Saskatchewan. To date, the Company has contributed approximately $12.4 million towards the construction and development of the Robinsons facility and anticipates a further $0.5 million will be required for equipment upgrades and related minor facility upgrades to accommodate equipment and related commissioning expenses, as part of a plan of continuous improvement to improve overall facility efficiency and increase product yields. The equipment is expected to arrive and be operational in the third quarter of 2021.

Robinsons OG

Robinsons Outdoor Grow Incorporated ("**Robinsons OG**") is a large-scale outdoor cannabis cultivation project comprised of over 158 acres of land and uniquely located in Hortonville, Nova Scotia. The Company anticipates that the long-term supply of outdoor cannabis to be produced on site at Robinsons OG will be used for product development initiatives at Dosecann and to create Robinsons-branded derivative cannabis products. Robinsons OG holds standard cultivation and processing licences under the Cannabis Act from Health Canada. However, given the timing for the optimal outdoor planting season and the operational challenges posed by the COVID-19 pandemic, the Company has made the strategic decision to delay the commencement of cultivation activities at the Robinsons OG site and instead focus its efforts on the continued development of the Robinsons OG land and facility in preparation for whenever the Company determines should be the next cultivation season. To date, the Company has contributed approximately $11.4 million towards the construction and development of the Robinsons OG project and anticipates a further $3.5 million in capital expenditures will be required to complete the Robinsons OG project prior to the next cultivation season. The facility is currently being used for additional storage and processing capacity for the Company to manage its flower inventory.

PEI Hemp

We acted as the financial sponsor for the development of a hemp farming co-operative through which 300 acres of hemp was cultivated in Prince Edward Island by six individual hemp licence holders, which resulted in approximately 98,000 kg of hemp biomass from the 2019 cultivation season. Dosecann secured the right of first refusal to offtake the biomass produced in 2019 at preferential prices. The biomass available for purchase was subject to final inspection and validation of a minimum cannabinoid content and quality specifications to ensure extraction efficiency. Based upon the negotiated pricing and the Company's sponsorship of the project to date, the Company has purchased (after inspection and validation) approximately 55,000 kilograms of hemp biomass for $6.2 million. The purchase price of $6.2 million was previously provided to the hemp farmers as a loan to commence the project. During the fourth quarter of 2020, an additional 14,300 kilograms of hemp biomass was purchased for $2.0 million. All parties have since agreed to terminate and mutually release each other from any further purchases under such arrangement. The Company intends to use the biomass to extract CBD for use in its own products or for the sale of CBD distillate to other regulated industry participants.

Strategic Partners

Imperial Brands

Through our strategic partnership with Imperial Brands, Auxly was granted global licenses to Imperial Brands' vaping technology for cannabis uses, and access to its vapour innovation business, Nerudia, and Imperial Brands will use Auxly as its exclusive partner for the future development, manufacture, commercialization, sale and distribution of cannabis products of any kind anywhere in the world. Auxly has elected to its board of directors one out of five director nominees and one non-voting observer, each designated by Imperial Brands, and in addition Imperial Brands' Group Science and Regulatory Affairs Director sits on Auxly's Safety Board. Auxly will continue to leverage the expertise of these Imperial Brands representatives to improve its corporate and product stewardship governance practices.

Capsugel

Capsugel Inc. ("**Capsugel**"), a subsidiary of Lonza Group Ltd. ("**Lonza**"), designs, develops and manufactures a wide range of innovative dosage forms for the biopharmaceutical and consumer health & nutrition industries. Capsugel provided Dosecann with a complete line of equipment for capsule filling and sealing, including a state-of-the-art LEMS® machine, Lonza's proprietary liquid-filled Capsugel® Licaps® capsules and rights to its capsule filling and sealing LEMS® technology. Dosecann and Lonza will also work collaboratively on new product formulations for cannabis capsule products.

Natures Crops

Natures Crops International ("**Natures Crops**") is a vertically integrated grower and manufacturer of plant-based specialty oils. Pursuant to a supply agreement with Natures Crops, Dosecann holds an exclusive global licence for the use of omega-rich Ahiflower® seed oil in all Cannabis Products sold in any dosage form, including oils, capsules, soft gels and any other pill format. The Company recently announced the launch of its first Ahiflower® seed oil based Cannabis Product, the Dosecann CBD+Ahiflower Oil Capsules, which are sealed in Lonza's Licaps® Capsugel® capsules, and will continue to develop new products utilizing Licaps® capsules, Ahiflower® seed oil, cannabis and other ingredients to serve consumer needs in the medical and wellness markets.

dosist™

GSW Creative Corporation Canada Inc., doing business as dosist™ ("**dosist**") and Dosecann have entered into an agreement whereby Dosecann will manufacture dosist's proprietary vape devices at the Dosecann facility. Dosecann will utilize its production capabilities and expertise to manufacture dosist's innovative dose control solutions, and dosist will also utilize Auxly's distribution channels to distribute its vape products.

International Operations

Presently the Company does not have any active international operations.

Given the slower than anticipated pace of cannabis-specific regulatory development in Latin America ("**LATAM**") and, consequently, the slower development of viable near-term commercial channels in the region, the Company has chosen to explore strategic alternatives for Inverell S.A. ("**Inverell**"), the Company's 80% owned subsidiary located in Montevideo, Uruguay. While exploring strategic alternatives, including the sale of the asset, the Company has ceased all operations at Inverell.

OUTLOOK

Having launched a strong initial portfolio of Cannabis 2.0 Products in December of 2019, Auxly was well-positioned going into its first full year of Cannabis Product sales in 2020. Our objectives for 2020 were to:

- Become a leader in the Canadian Cannabis 2.0 Products market;
    - Auxly has had a tremendously successful year, as we were able to leverage our position as one of the first cannabis companies to distribute and sell Cannabis 2.0 Products in Canada, becoming the top licensed producer of Cannabis 2.0 Products nationally in 2020.
- Complete remaining construction and licensing of all Canadian operations to leverage existing assets and increase revenues;
    - The Company completed the second-floor expansion at its Dosecann facility which enabled increased production, fulfillment rates and sales of Cannabis 2.0 Products.

- Converted the Kolab facility from cultivation to a manufacturing, processing and distribution facility for the Company's pre-roll and dried flower Cannabis Products, in anticipation of the strategic expansion of the Company's Cannabis 1.0 Products.
- The Company's subsidiaries obtained numerous Health Canada licences, including processing licences for Sunens and Robinsons OG, as well as an Institutional Cannabis Research Licence for KGK, which provide the Company with enhanced commercial flexibility.

- Work with the Sunens team to secure supply of input materials for use in the Company's product offerings in 2020;
  - Despite some COVID–19 related delays, Auxly was able to accelerate licencing of the facility such that Sunens was able to cultivate cannabis and make it available for sale to Auxly and other licenced producers in Q1 2021.
- Collaborate with our partners to move towards commercialization of a small number of products for sale internationally or, if and when permitted, as part of the Cannabis 3.0 Products market;
  - While international product sales did not materialize, the Company has, through its continued execution of its product development strategy, made significant progress towards the commercialization of products for the Cannabis 3.0 Products market, if and when legally permitted.

Looking ahead to 2021, we are focused on building upon our success as a market leader in Cannabis 2.0 Products, while continuing to advance the Company's focused expansion of its dried flower, pre-roll, oil and capsule product offerings. Our overall objectives for 2021, which may be impacted by the COVID-19 pandemic (see further discussion in this MD&A under "*COVID-19 Pandemic*"), are as follows:

- Continued leadership and strength in the Cannabis 2.0 Products market;
- Focused expansion of Cannabis 1.0 Products;
- Continue to take measures to improve cash flows and finance the business;
- Leverage the Sunens facility to establish a secure supply of cannabis and reduce reliance on open market purchasing; and
- Explore possible cannabis market entry strategies in regulated international markets, on an asset light basis.

We will continue to evaluate opportunities to bring new and exciting products to consumers as we continue to realize our vision of becoming a global leader in branded cannabis products that deliver on our consumer promise of quality, safety and efficacy.

ESG (Environmental, Social and Governance) Initiatives

As we continue to execute on our vision, Auxly is committed to developing our business with the goal of becoming a responsible corporate citizen in mind, and to making a positive impact in the communities in which we operate.

Auxly is proud to have been the first in the industry to offer 100% biodegradable packaging for cannabis products, and the first in the industry to offer a vape recycling program that accepts products from all licensed producers. The Kolab Project Vape Recycling program, developed in partnership with the e-waste recycling experts at Greentec, is currently available at more than 100 retail outlets across Canada.

Our people are the foundation of our company and we take pride in our commitment to investing in the success of our employees as well as helping to create jobs in the communities in which we operate. We believe in the importance of diversity and inclusion and will continue to strive for a leadership and employee base that reflects the consumers and communities that we serve. We are also proud to have a diverse Board of Directors which reflects independent viewpoints and who are committed to strengthening our corporate governance practices.

While delivering on our consumer promise of quality, safety and efficacy, Auxly is committed to building a reputation of trust and integrity, and consistently upholding the highest industry standards.

COVID-19 PANDEMIC

On March 11, 2020, the World Health Organization recognized the outbreak of COVID-19 as a pandemic, which has had a profound impact on the global economy. The pandemic has been a rapidly changing situation throughout the year and into 2021, and the provincial and territorial responses to the pandemic continue to evolve as Canada is currently experiencing a third wave of COVID-19 cases. Initially, during the early stages of the pandemic, certain provincial and territorial governments imposed various degrees of temporary lockdown measures forcing non-essential businesses to close, including retail cannabis stores in some jurisdictions, while certain other jurisdictions allowed retail cannabis stores to remain open with certain operational limitations and protocols in place.

Although the original provincial lockdown measures were eventually eased in most areas, there has been a recent trend of stricter lockdown measures being imposed again across various jurisdictions given the rapid increase in COVID-19 cases across the country. On April 3, 2021, all regions in Ontario moved into a third lockdown, and on April 8, 2021 Ontario declared a state of emergency and a provincewide stay-at-home order went into effect as a public health measure, with additional lockdown measures and travel restrictions announced by the government on April 16, 2021. Under the stay-at-home order all non-essential businesses, including retail cannabis stores, will remain closed for in-store sales for at least six weeks, however, retail cannabis stores are permitted to remain open for curbside pickup and delivery. As of the date of this MD&A, retail cannabis stores across the rest of Canada remain open with pandemic protocols in place, but there is a possibility that further lockdown measures could be imposed or extended given the recent increase in COVID-19 cases across provinces and territories which may have a negative impact on the Company's sales, cash flows and results of operations.

In response to the pandemic, the Company implemented safety measures to protect employees and consumers which comply with all federal and provincial regulations and guidelines while keeping our facilities operating. The Dosecann, Kolab and Robinsons facilities remained open and operational on extended shifts with few instances of employee absenteeism or self isolation, and certain operational changes have been made to best address the safety of our employees and consumers. Employees at the Company’s corporate head office in Toronto and other non-production staff at our cannabis facilities have been operating under a work from home model. The impact of COVID-19 on cannabis operations was largely limited to premium pay for hourly employees, and temporary supply chain disruptions during the first two quarters of 2020 and increased freight charges for much of the year, that were not material.

Two of the Company’s facilities, Dosecann and Robinsons, are located in PEI and Nova Scotia, respectively. The Atlantic provinces (Nova Scotia, PEI, New Brunswick and Newfoundland) have had stricter COVID-19 measures in place than the rest of the country, restricting travel from other provinces within Canada and requiring any visitors to a province in the region to complete a 2-week quarantine upon arrival. This policy has been very successful so far in keeping COVID-19 case counts low across the Atlantic region, however it is possible that further lockdown measures could still be imposed. Partially as a result of the low case count in the Atlantic region, following the second quarter of 2020, the Company was able to roll back premium pay for hourly employees and has also seen a reduction in freight costs to near pre-pandemic levels. However, given the continued uncertainties associated with the COVID-19 pandemic, including disruptions to the global and local economies due to related lockdown orders, quarantine policies and restrictions on travel, trade and business operations and a reduction in discretionary consumer spending, we are unable to estimate the impact of the COVID-19 pandemic on our business, financial condition, results of operations, and/or cash flows.

Additionally, due to required social distancing measures KGK was initially unable to commence new clinical trials with participants (which makes up a significant portion of its business), but has since shifted to a virtual process allowing it to facilitate new clinical trials. Further, certain aspects of clinical trial work were deemed an essential service and were therefore completed by third parties. In March 2020, KGK temporarily laid-off approximately 50 employees as it transitioned through the new operating model.

In relation to the COVID-19 pandemic, the Company accessed the Canada Emergency Wage Subsidy in 2020 for wages for employees at its subsidiaries KGK and Kolab. Otherwise, the Company is not relying on any other government financing programs to provide liquidity support.

RECENT DEVELOPMENTS: Fourth Quarter 2020 To Date

Imperial Brands PLC Extends Convertible Debenture Maturity and Defers Interest

On April 19, 2021, the Company announced an agreement with its strategic partner Imperial Brands to amend certain provisions of its previously issued $123 million debenture (the "**Debenture**") and investor rights agreement (the "**Investor Rights Agreement**") dated September 25, 2019 (collectively, the "**Amendments**").

Pursuant to the Amendments, Imperial Brands and Auxly have agreed to extend the maturity date of the Debenture by 24 months from September 25, 2022 to September 25, 2024. The Amendments will also provide Imperial Brands with the right, on an annual basis, to convert any or all of the accrued and unpaid interest on the Debenture then outstanding into common shares (the "**Interest Conversion Election**"), at a conversion price equal to the five-day volume weighted average trading price of the common shares on the date that Interest Conversion Election is made. Auxly and Imperial Brands have also agreed that the interest rate under the Debenture, which currently accrues at a rate of 4% per annum and is payable annually, will remain unchanged but will be payable on maturity of the Debenture. The Debentures are convertible into common shares at a price of $0.81 per share at any time prior to the close of business on the business day immediately preceding maturity. Lastly, the Amendments provide for the re-instatement of certain approval rights of Imperial Brands under the Investor Rights Agreement.

The implementation of the Amendments is subject to the satisfaction of a number of conditions, including, among other things, the approval of the TSX Venture Exchange, and minority shareholder approval of the Amendments in accordance with Multilateral Instrument 61-101 - *Protection of Minority Security Holders in Special Transactions*.

Auxly Graduates to the Toronto Stock Exchange ("TSX")

On April 16, 2021, the Company announced that it had received final approval from the TSX to graduate from the TSX Venture Exchange ("**TSXV**") and list its common shares on the TSX.

Auxly's common shares commenced trading on the TSX at market open on Tuesday, April 20, 2021 under its existing symbol "XLY". In connection with listing on the TSX, the last day of trading on the TSXV was April 19, 2021 and the Company's shares were delisted from the TSXV upon commencement of trading on the TSX. The Company's shares continue to trade on the OTCQX market under the symbol "CBWTF."

Kolab Project Launches First Cannabis Concentrate with 232 Series Diamonds

On March 24, 2021, Kolab Project announced that its first concentrate offering, Kolab Project 232 Series Diamonds, was available to order for provincial wholesalers. 232 Series Diamonds are single-strain concentrates extracted from fresh, flash-frozen cannabis flower. The first release is produced with Ice Cream Cake, a popular strain launched as part of the Kolab Project Growers Series in partnership with Safari Flower Co. In true Kolab Project fashion, 232 Series Diamonds are available in recyclable and resealable light-proof jars, and biodegradable packaging.

Auxly Announces At-the-Market Equity Program

On March 23, 2021, the Company announced the establishment of an at-the-market equity program (the "**ATM Program**") that allows the Company to issue and sell up to $30,000,000 of Shares from the treasury to the public, from time to time, at the Company's discretion. The volume and timing of distributions under the ATM Program, if any, will be determined at the sole discretion of the Company. Distribution of the Shares under the ATM Program will be made pursuant to the terms of an equity distribution agreement between the Company and ATB Capital Markets (the "**Agent**"). The ATM Program will be effective until the earlier of the issuance and sale of all of the Shares issuable pursuant to the ATM Program and the date on which the receipt issued for the Company's base shelf prospectus dated March 18, 2021 (the "**Base Shelf Prospectus**") ceases to be effective in accordance with Canadian securities laws, unless terminated prior to such date by the Company or the Agent. As Shares sold in the ATM Program will be issued and sold at the prevailing market price at the time of the sale, prices may vary among purchasers during the period of distribution. The offering under the ATM Program will be made pursuant to a prospectus supplement to the Base Shelf Prospectus dated March 23, 2021. As of the date of this MD&A, the Company has not issued any Shares pursuant to the ATM Program.

Auxly Announces Strategic Expansion into Cannabis 1.0

On February 18, 2021, the Company announced its strategic expansion into Canada's largest cannabis segment, the dried-flower market. Auxly's expansion into Cannabis 1.0 will consist of a three-pronged strategy:

1) Expanding its flower offering under the Kolab Project Growers Series through the launch of new cultivars with existing partners and securing new partnerships with top-tier cultivators;
2) Launching a strain-specific dried flower offering of unique genetics at a compelling price point under Auxly's Back Forty brand; and
3) Significantly boosting its pre-roll capacity through custom-built automation and launching disruptive pre-roll products under its Kolab Project and Back Forty brands.

Auxly Announces Closing of $20 Million Bought-Deal Public Offering, Including Full Exercise of the Over-Allotment Option

On February 8, 2021, the Company announced the closing of a bought deal short form prospectus offering pursuant to which the Company sold a total of 54,395,000 units of the Company at a price of $0.37 per unit for gross proceeds to the Company of $20,126,150, which included the full exercise of the over-allotment option granted to the underwriters. Each unit consisted of one Share and one-half of one Share purchase warrant, with each whole warrant entitling the holder thereof to purchase one Share at a price of $0.46 per Share at any time until February 8, 2024. The Company originally announced the bought deal offering on January 20, 2021, and on January 21, 2021, the Company announced that it had entered into a revised agreement with ATB Capital Markets Inc. and Cantor Fitzgerald Canada Corporation, together with a syndicate of underwriters, to increase the size of the previously announced bought deal short form prospectus offering for aggregate gross proceeds of $17,501,000 from $15,003,500.

Auxly in Top Spot for 2.0 Products

On January 19, 2021, the Company announced that it had achieved the #1 market share position in Canada for Cannabis 2.0 Products in 2020, as confirmed by Headset Canadian Insights Data. Despite not participating in every 2.0 category, Auxly's 19.2% share of the total vape market and 12% share of the total edibles market, propelled the Company to the #1 spot in overall Cannabis 2.0 Products sales for the year.

Auxly's Subsidiary KGK Science Receives Institutional Cannabis Research Licence from Health Canada

On December 23, 2020, the Company announced that KGK had received its Institutional Cannabis Research Licence from Health Canada, which provides the contract research organization with approval to conduct multiple cannabis research projects, removing the need to obtain individual research licences for each project, thereby increasing its flexibility and expediting processes at its clinical research facility located in London, Ontario.

Auxly Announces Closing of $13.8M Bought-Deal Public Offering, Including Full Exercise of the Over-Allotment Option

On December 15, 2020, the Company announced the closing of a bought deal short form prospectus offering originally announced on November 24, 2020. The Company sold a total of 46,000,000 units of the Company at a price of $0.30 per unit for gross proceeds to the Company of $13,800,000, including the full exercise of the over-allotment option granted to the sole underwriter. Each unit was comprised of one Share and one-half of one Share purchase warrant of the Company, with each whole warrant entitling the holder thereof to purchase one Share at a price of $0.40 per Share at any time until December 15, 2023. The offering was led by Mackie Research Capital Corporation as sole underwriter and sole bookrunner.

Kolab Project Introduces a Nostalgic Indulgence: Cannabis-Infused Cherry Cola Pop Milk Chocolates

On December 10, 2020, the Company announced the launch of Kolab Project Cherry Cola Pop milk chocolates. Kolab Project Cherry Cola Pop combines premium cannabis distillate, creamy milk chocolate, classic cola flavouring and black-cherry popping candy for a unique experience with every bite.

Kolab Project Launches Ice Cream Cake Dried Flower with Safari Flower Co., a New Premium Craft Grower Collaboration

On December 2, 2020, the Company and Kolab Project announced its collaboration with craft cultivator, Safari Flower Co. in launching Ice Cream Cake dried flower for premium cannabis consumers. Ice Cream Cake dried flower is part of the Kolab Project Growers Series, which highlights unique partnerships born from a shared commitment to quality, refinement, and continuous experimentation.

Lease of Dosecann Facility and Real Property

On November 27, 2020, the Company entered into a new long-term lease for its Dosecann facility. Under the terms of the new lease, Dosecann has the option to purchase the real property for the amortized lease amount of $8M (plus 4% interest) at any time throughout the 21-year term. Prior to this new lease, Dosecann was in the process of purchasing the real property from the original landlord; however, a new purchaser (and now landlord) agreed to purchase the property and fulfill conditions precedent thereby allowing Dosecann to be refunded $2 million and to save an additional $6 million in capital expenditures, thereby effectively providing the Company with $8 million in proceeds.

Dosecann Introduces Cannabis Capsules with Omega-Rich Ahiflower® Oil

On November 23, 2020, the Company announced the launch of Dosecann Capsules, a new, high-quality, precision-dosed cannabis product that combines high-potency, broad-spectrum cannabinoids with omega-rich Ahiflower® oil. Ahiflower oil is a sustainable, plant-based source of the complete and balanced essential omegas the body needs. Dosecann Capsules were developed by a team of scientists and researchers at the state-of-the-art laboratory at the Dosecann facility.

Sale of LAB001 Retail Store

On November 6, 2020, the Company and Kolab completed the sale of LAB001, Kolab's wholly owned retail store located in Lloydminster, Saskatchewan, to a subsidiary of Delta 9 Cannabis Inc. ("**Delta 9**"). The purchase price was $875,000, subject to customary adjustments, where $750,000 of the purchase price was satisfied through the issuance of 1,282,270 common shares in the capital stock of Delta 9 at a deemed price of $0.5849 per common share, with the balance of the purchase price paid in cash.

Welcome to the Back Forty: A New Cannabis Brand for Savvy Consumers

On October 13, 2020, the Company announced the launch of its latest brand, Back Forty, a brand that is all about embracing simplicity and getting back to the basics. Back Forty launched with three unique SKUs of distinct high-potency vapes, available at cannabis retailers in British Columbia, Alberta, Ontario and New Brunswick.

Auxly Strengthens its Board and Announces Additional Steps on Path to Profitability

On October 1, 2020, the Company announced that Auxly Founder and Chair Chuck Rifici would be stepping down as Chair of the Board of Directors, Ms. Genevieve Young, a current Independent Director on the Board and Chair of Auxly's Audit Committee, would be assuming the role of Chair, effective immediately, and Auxly's Board of Directors would also be welcoming a new Independent Director, Mr. Vikram Bawa. The Company also announced that Mr. Michael Lickver had been named President. The Company further announced its continued dedication to executing on its corporate strategy and increasing its market share, while also improving its margins and reducing corporate overhead, with a target of achieving positive adjusted EBITDA during the first half of 2021. In addition to the actions already taken to reduce operating costs at two of Auxly's cultivation assets, Inverell S.A. located in Uruguay and Robinsons Outdoor Grow located in Nova Scotia, the Company has taken added measures to reduce its workforce to further accelerate its path to profitability. The Company expects to generate approximately $3 million in quarterly SG&A savings through these cumulative reductions, resulting in an expected cash-based SG&A run-rate of approximately $10 million by the first quarter of 2021. The Company now anticipates achieving positive adjusted EBITDA in the second half of 2021, in part due to delays, of approximately 3-4 months, in the receipt of equipment to support pre-roll sales.

FINANCIAL HIGHLIGHTS AND KEY PERFORMANCE INDICATORS

(000's)	Year ended December 31			
	2020	2019	Change	Change
Total net revenues	**$ 50,796**	$ 8,352	$ 42,444	508%
Net loss*	**$ (85,426)**	$ (102,574)	$ 17,148	17%
Adjusted EBITDA**	**$ (30,317)**	$ (37,292)	$ 6,975	19%
Weighed average shares outstanding	**631,528,750**	596,409,703	35,119,047	6%

*Attributable to shareholders of the Company

**Adjusted EBITDA is a Non-IFRS financial measure. Refer to the Non-IFRS Financial and Performance Measures section in this MD&A for definitions

(000's)	**December 31, 2020**	December 31, 2019	Change	Change
Cash and equivalents	**$ 21,214**	$ 44,134	$ (22,920)	-52%
Total assets	**$ 378,963**	$ 411,182	$ (32,219)	-8%
Debt	**$ 114,825**	$ 95,438	$ 19,387	20%

For the year ended December 31, 2020, net revenues were $50.8 million, resulting in a significant increase over the same periods of 2019 primarily as a result of the Company commencing the sale of Cannabis Products.

Net losses attributable to shareholders decreased by $17.1 million to $85.4 million in 2020 when compared to 2019.

Adjusted EBITDA improved by $7.0 million or 19% to negative $30.3 million for the year as a result of improved revenues, gross margins and reductions in selling, general, and administrative expenses during the quarter.

Cash and equivalents declined to $21.2 million as at December 31, 2020. Net cash reductions were primarily associated with negative Adjusted EBITDA, net investing activities of $14.5 million, partially offset by net financing activities of $24.7 million primarily through the issuance of convertible debentures and equity.

For the year ended December 31, 2020 the average number of Shares outstanding increased to 631.5 million Shares, an increase of 35.1 million Shares or 6% over 2019.

RESULTS OF OPERATIONS

For the years ended: (000s)		**December 31 2020**		December 31 2019
Revenue				
Revenue from sales of cannabis products	**$**	**57,182**	$	2,287
Research contracts and other		**4,147**		6,262
Excise taxes		**(10,533)**		(197)
Total net revenue		**50,796**		8,352
Costs of sales				
Costs of finished cannabis inventory sold		**33,858**		2,162
Research contracts and other		**2,750**		5,743
Inventory (gain)/impairment		**3,393**		3,244
Gross profit excluding fair value items		**10,795**		(2,797)
Unrealized fair value gain/(loss) on biological transformation		**537**		(761)
Realized fair value gain/(loss) on inventory		**(193)**		(153)
Gross profit/(loss)		**11,139**		(3,711)
Expenses				
Selling, general, and administrative expenses		**48,855**		50,291
Depreciation and amortization		**9,384**		8,574
Interest expense		**13,043**		12,121
Total expenses		**71,282**		70,986
Other (loss) / income				
Fair value loss for financial instruments accounted under FVTPL		**(4,408)**		(6,482)
Interest and other income		**477**		3,612
Impairment of long-term assets		**(6,146)**		(5,283)
Impairment of intangible assets and goodwill		**-**		(29,631)
Loss on settlement of assets and liabilities and other expenses		**(10,048)**		(3,550)
Share of loss on investment in joint venture		**(7,407)**		(2,081)
Foreign exchange loss		**(437)**		(1,484)
Total other losses		**(27,969)**		(44,899)
Net loss before income tax		**(88,112)**		(119,596)
Income tax recovery		**681**		10,978
Net loss	**$**	**(87,431)**	$	(108,618)
Net loss attributable to shareholders of the Company	**$**	**(85,426)**	$	(102,574)
Net loss attributable to non-controlling interest	**$**	**(2,005)**	$	(6,044)
Adjusted EBITDA	**$**	**(30,317)**	$	(37,292)
Net loss per common share (basic and diluted)	**$**	**(0.14)**	$	(0.17)
Weighted average shares outstanding (basic and diluted)		**631,528,750**		596,409,703

Revenue

For the year ended December 31, 2020, cannabis revenues were $57.2 million as compared to $2.3 million in the same period in 2019. Net cannabis revenues of $46.6 million during the period were comprised of approximately 80% Cannabis 2.0 Products, with the remainder from Cannabis 1.0 Products, and represented a significant increase over 2019 where Cannabis 2.0 sales began in December. During the year approximately 75% of cannabis net revenues originated from sales to British Columbia, Alberta and Ontario led by strong market shares in vapes and edibles, resulting in Auxly being the top LP for Cannabis 2.0 sales nationally[1]. Sale of Cannabis 1.0 Products were led by the launch of Kolab Project flower and pre-rolls and Robinsons dried flower in the summer of 2020.

Research and other revenues of $4.1 million for 2020 were $2.1 million lower than 2019 primarily as a result of the COVID-19 pandemic and its disruptive impact on the completion of clinical trials, partially offset by the introduction of new regulatory advisory services. Revenues in support of third-party research contracts can fluctuate significantly during the term of the contract based upon the achievement of milestones. Where milestones are not met, revenues are deferred on the balance sheet which may result in timing differences in earnings.

Gross Profit / Loss

Auxly realized a gross profit of $11.1 million for 2020, compared to a gross loss of $3.7 million in 2019. Cannabis gross profits for the year ended December 31, 2020 were $9.7 million resulting in a 21% margin (27% before impairment and fair value adjustments), with research and other gross profits of $1.4 million and a related margin of 34%. Impairment of inventory of $3.4 million was $0.2 million greater than 2019 and relates primarily to the charges related to the cessation of Inverell operations and approximately $1.1 million of aged Cannabis 2.0 Products associated with the SKU rationalization undertaken in the third quarter of 2020.

Auxly realized a gross loss of $3.7 million for the year ended December 31, 2019 following fair value adjustments. The gross loss for the year ended December 31, 2019 was primarily comprised of inventory related adjustments of approximately $4.1 million (a $1.8 million impairment of inventory associated with final Inverell biomass product qualification and grading, a $1.4 million impairment of inventory associated with spoilage and obsolescence in mass production of Cannabis 2.0 Products at Dosecann, a $0.1 million realized fair value loss on other inventories, and a $0.8 million unrealized fair value loss on biological asset transformation), partially offset by KGK revenues less expenses of $0.5 million and Cannabis Product revenues less expenses of $0.1 million, net of $0.2 million of excise taxes.

Total Expenses

Selling, general and administrative expenses ("**SG&A**") are comprised of wages and benefits, office and administrative, professional fees, business developments, share-based payments, and selling expenses. For 2020, SG&A expenses were $48.9 million, a decrease of $1.4 million from 2019.

Wages and benefits were $22.6 million, an increase of $4.7 million over 2019. The increase of $4.7 million was primarily driven by workforce increases to support Cannabis Product sales, primarily related to the operations and commercial teams, the absorption of employees arising from the foreclosure of Curative and compensation and severance accruals recognized during

[1] Headset Canadian Insights data January 9, 2021.

the period, partially offset by employee wage subsidies received by KGK and reduction of Inverell staffing.

Office and administrative expenses of $11.8 million in 2020 increased by $3.8 million compared to 2019 primarily as a result of increased operating costs associated with the development and sale of Cannabis Products in 2020 and the implementation of an organization-wide ERP system.

Auxly's professional fees were $3.2 million, lower by $3.6 million for the year as compared to 2019. Professional fees incurred during the periods primarily related to accounting fees, regulatory matters, reporting issuer fees, ongoing legal proceedings, recruiting fees in conjunction with hiring, consulting fees, and fees associated with financing activities. The decrease in professional fees was driven by the reduction in professional services and professional services contracts in 2020.

Business development expenses were $1.4 million as compared to $4.8 million in 2019. The decreases are primarily due to a reduction in acquisition, development and travel related expenses.

Selling expenses for the year ended December 31, 2020 were $5.6 million, $5.3 million greater than 2019 directly attributable to cannabis sales activities comprised of brokerage fees earned by Kindred Partners and marketing initiatives for Cannabis Products.

For 2020, share-based compensation was $4.3 million as compared to $12.6 million over 2019. The reduction in expenses in 2020 reflects the impact of significantly fewer option grants, the impact of lower share prices and expense reversals of approximately $1 million associated with the termination of options following the SG&A reductions announced October 1, 2020.

Depreciation and amortization expenses were $9.4 million in 2020, as compared to $8.6 million during 2019. The increase in expense is primarily a result of capital expenditures in 2020. During 2019, several projects remained under development and were not depreciated until completed.

Interest expenses were $13.0 million for the twelve months ended December 31, 2020 and $12.1 million for the same period of 2019. Interest expenses in 2020 were primarily the result of interest expense and accretion on the $123 million, 4% Imperial Brands convertible debentures, 7.5% on the convertible debenture tranches issued in 2020, and the non-cash accretion of placement and other related fees being recognized over the terms of the respective debentures. Interest expenses in 2019 were driven by interest charges of 6% on the then outstanding 2018 convertible debentures and the Imperial Brands convertible debentures and the non-cash accretion of placement and other related fees being recognized over the terms of the respective debentures.

Total Other Incomes and Losses

Fair value changes on financial instruments arise on changes in value of promissory notes and level two securities held. For the year ended December 31, 2020, the Company reported a fair value loss of $4.4 million, as compared to a $6.5 million loss in 2019 which was primarily related to the write down of the Beleave Inc. debt obligation receivable in product equivalent. Fair value losses in 2020 reflect changes in level two securities held as all promissory notes were repaid or fully impaired as at December 31, 2019.

The Company recorded interest and other incomes of $0.5 million in 2020, which declined from $3.6 million in 2019, primarily as a result of lower cash and cash equivalents balances held throughout the year and a reversal of $1.3 million in accrued interest as part of the negotiation with Sunens in respect of off-take agreement modifications negotiated for the benefit of Auxly, in the fourth quarter of 2020.

Impairment of long-term assets, intangibles and goodwill of $6.1 million in 2020 is primarily related to the impairment of the Company's LATAM cash generating unit Inverell. Impairments of $34.9 million in 2019, included charges of $23.9 million and $7.6 million where carrying values were higher than recoverable amounts related to Inverell and KGK respectively. In addition, impairment charges of $1.8 million related to the intangible value of the FSD Pharma Inc. ("**FSD**") supply agreement, $1.1 million loss on the 2368523 Ontario Inc. (d/b/a Curative Cannabis) supply agreement due to foreclosure and a $0.5 million loss related to the Green Relief offtake agreement.

Losses on settlement of assets and liabilities and other expenses were $10.0 million, primarily relating to 1); a $8.7 million impairment in the investment in joint venture associated with amendments made to forego interest until January 1, 2023 on the promissory note in the principal amount of approximately $48.5 million owed by Sunens in consideration of certain offtake arrangement modifications made for the benefit of Auxly, and 2); a reversal of a gain on non-monetary inventory transfers with another licensed producer which was recorded in the first quarter of 2020. The inventory was returned during the quarter resulting in the recognition of a liability of approximately $5.8 million in accounts payable and other liabilities and an asset held in inventory. Replacement product has since been shipped to the licensed producer in March 2021 to settle this obligation. Losses of $3.6 million in 2019, primarily relate to a $2.5 million loss on the foreclosure over Curative, credit loss provisions and final expenditures of approximately $0.5 million associated with the FSD project.

The share of loss on investment in joint venture of $7.4 million in 2020, increased by $5.3 million over 2019 reflecting the Company's proportionate share of Sunens earnings. Sunens received its cultivation licence in 2020 and has scaled up operations to make product available for sale to other licenced producers in the first quarter of 2021.

Auxly is exposed to foreign exchange fluctuations from the U.S. dollar to CAD dollar exchange rate primarily related to Inverell. During the year ended December 31, 2020, the Company reported a foreign exchange loss of $0.4 million and $1.5 million in 2019.

Net Losses

Net losses were $87.4 million with a net loss of $0.14 per share on a basic and diluted basis in 2020, and $108.6 million with a net loss of $0.17 per share on a basic and diluted basis in 2019. The improvement of $21.2 million in 2020 was primarily the result of a gross profit increase of $14.8 million, total expenses consistent with the prior year amounts, lower impairment losses and total other losses of $16.9 million, partially offset by lower income tax recoveries of $10.3 million.

Net losses of $108.6 million in 2019 were primarily driven by an increase in total other losses and depreciation and amortization expenses, partially offset by income tax recoveries.

Adjusted EBITDA

Adjusted EBITDA improved by approximately $7.0 million to $(30.3) million in 2020 as compared to the same period in 2019. The increase was primarily driven by gross profits from Cannabis Product sales partially offset by SG&A excluding non-cash share-based compensation. In 2019, the Company's adult use Cannabis Product sales commenced in December 2019.

SUMMARY OF QUARTERLY RESULTS

The following table summarizes comparative quarterly results for the last eight quarters.

(000's)	**Q4/20**	Q3/20	Q2/20	Q1/20	Q4/19	Q3/19	Q2/19	Q1/19
Total net revenues	**$ 18,889**	$ 13,449	$ 8,564	$ 9,905	$ 3,156	$ 1,617	$ 2,762	$ 817
Net losses*	**(26,965)**	(17,799)	(27,917)	(12,744)	(57,721)	(17,255)	(13,987)	(13,611)
Adjusted EBITDA**	**(6,104)**	(6,783)	(9,095)	(8,335)	(10,488)	(11,056)	(8,209)	(7,539)
Average shares outstanding (000's)	**640,923**	631,950	627,822	625,242	613,683	594,592	592,208	587,247
Per share: Basic & diluted loss	**$ (0.04)**	$ (0.03)	$ (0.04)	$ (0.02)	$ (0.09)	$ (0.03)	$ (0.02)	$ (0.02)

*attributable to shareholders of the Company.

**Adjusted EBITDA is a Non-IFRS financial measure. Refer to the Non-IFRS Financial and Performance Measures section in this MD&A for definitions

Prior to Q4 2019, Auxly's revenues were primarily derived from providing research services for customers who were conducting human clinical trials through its wholly-owned subsidiary KGK. Commencing December 16, 2019, revenues also include the sale of Cannabis Products to recreational consumers in Canada, which resulted in the significant revenue increase during 2020.

The net loss for Q2 2020 increased despite recognition of revenues and a decline in SG&A expenses due to losses on investments and settlements, and recognition of impairment charges.

Adjusted EBITDA has seen some volatility primarily as a result of increasing SG&A due to acquisitions and expenditures in preparation for cannabis sales in December 2019, partially offset in 2020 with the achievement of the sale of Cannabis Products. Adjusted EBITDA continues to improve as cannabis revenues improve with both customer acceptance and expansion of product offerings.

The increases in average outstanding Shares reflect financing and acquisition related activities (issuance and exchange of Shares, exercise of warrants, options and conversion of convertible debentures).

FOURTH QUARTER RESULTS OF OPERATIONS

For the three months ended: (000s)		December 31 2020		December 31 2019
Revenue				
Revenue from sales of cannabis products	**$**	**23,152**		1,436
Research contracts and other		**632**		1,917
Excise taxes		**(4,895)**		(197)
Total net revenue		**18,889**		3,156
Costs of sales				
Costs of finished cannabis inventory sold		**14,202**		1,727
Research contracts and other		**1,417**		1,918
Inventory (gain)/impairment		**1,763**		2,170
Gross profit/(loss) excluding fair value items		**1,507**		(2,659)
Unrealized fair value gain/(loss) on biological transformation		**215**		(89)
Realized fair value gain/(loss) on inventory		**-**		90
Gross profit/(loss)		**1,722**		(2,658)
Expenses				
Selling, general, and administrative expenses		**9,836**		11,404
Depreciation and amortization		**2,261**		4,572
Interest expense		**3,824**		4,170
Total expenses		**15,921**		20,146
Other (loss) / income				
Fair value gain/(loss) for financial instruments accounted under FVTPL		**262**		(274)
Interest and other income/(loss)		**(321)**		(225)
Impairment of long-term assets		**(1,784)**		(5,283)
Impairment of intangible assets and goodwill		**-**		(27,831)
Loss on settlement of assets and liabilities and other expenses		**(6,186)**		(2,262)
Share of loss on investment in joint venture		**(4,412)**		(691)
Foreign exchange loss		**(559)**		(469)
Total other losses		**(12,999)**		(37,035)
Net loss before income tax		**(27,198)**		(59,839)
Income tax recovery		**24**		(3,269)
Net loss	**$**	**(27,174)**	$	(63,108)
Net loss attributable to shareholders of the Company	**$**	**(26,965)**	$	(62,848)
Net loss attributable to non-controlling interest	**$**	**(209)**	$	(260)
Adjusted EBITDA	**$**	**(6,104)**	$	(10,488)
Net loss per common share (basic and diluted)	**$**	**(0.04)**	$	(0.11)
Weighted average shares outstanding (basic and diluted)		**631,949,685**		594,591,824

Unless stated otherwise, the narrative in this section is in reference to the operating results for the fourth quarter of 2020 as compared to the same period in 2019.

Revenue

In the fourth quarter of 2020, the Company realized its goal of achieving a leadership position in the sale of Cannabis 2.0 Products as confirmed by Headset Canadian Insights data for the period and year. Net revenues were $18.9 million of which $18.3 million were comprised of the sale of

Cannabis Products. During the quarter, vape products comprised approximately 65% of Cannabis 2.0 Products sales and sale of Cannabis 1.0 Products contributed approximately 20% towards net revenues. Cannabis net revenues were $1.2 million during the quarter ended December 31, 2019 which were exclusively Cannabis 2.0 Products, first legal on December 16, 2019.

Research and other revenues primarily from KGK decreased to $0.6 million during the quarter ended December 31, 2020 as compared to $1.9 million in 2019. Revenues in 2020 were impacted by the inability earlier in the year to progress clinical trials during the COVID-19 pandemic which in turn delayed the completion of subsequent milestones for revenue recognition. Revenues in support of third-party research contracts can fluctuate significantly during the term of the contract based upon the achievement of milestones.

Gross profit/ (loss)

Auxly achieved a gross profit of $1.7 million in 2020, compared to a gross loss of $2.7 million for the three-month period ended December 31, 2019. Gross income in 2020 was comprised of $2.5 million in Cannabis Products partially offset by a gross loss of $0.8 million related to research contracts and other. Cannabis gross profit margin was approximately 14% and 22% before fair value and impairment amounts. Gross margin was lower for the period as a result of nominal Cannabis 1.0 Product margins and, to a lesser degree, a limited number of vape product pricing changes. During the three months ended December 31, 2019, research contracts and other revenues covered costs, Cannabis Products realized a gross loss of $0.5 million, less a $2.2 million realized fair value change on other inventories.

Total Expenses

Selling, general and administrative expenses of $9.8 million during the fourth quarter of 2020 decreased by $1.6 million from $11.4 million during the same period in 2019. The decrease in expenses was comprised of reductions of $1.6 million in wages and salaries as a result of staff reductions announced October 1, 2020 and improved production utilization during the period, $1.5 million in business development related to lower activities and travel, $0.8 million in share-based compensation due to expense reversals stemming from the recent staff reductions and a reduction of $0.6 million in professional fees primarily related to financing related fees, partially offset by an increase of $1.7 million related to selling expenses to support sales of Cannabis Products for the full quarter of 2020 as compared to two weeks of 2019 and $1.4 million in office and administrative and other expenses related to personal protection supplies and product testing.

Depreciation and amortization expenses declined to $2.3 million in 2020 as compared to $4.6 million during the same period of 2019 primarily as a result of lower expenses following the impairment of intangibles in 2019, the write-off of Inverell assets and certain adjustments reflected in the fourth quarter of 2019.

Interest expenses were $3.8 million for the three months ended December 31, 2020, which reflects a decrease of $0.4 million from 2019. In 2019, the Company had both the Imperial Brands convertible debenture of $123 million and a portion of the 2018 6% convertible debentures concurrently outstanding. The decrease in 2020 reflects the impact of the 6% convertible debenture retirement, partially offset by interest on $11.25 million of the $25 million standby convertible debentures issued in 2020.

Total Other Losses

For the quarter, net total other losses were $13.0 million primarily comprised of $6.2 million in losses on settlement of assets and liabilities and other assets and $4.4 million in the share of loss on investment in joint venture both related to modifications made to the Sunens offtake arrangement during the quarter and $1.8 million related to write downs of the Inverell assets. During the three months ended December 31, 2019, total other losses were $37 million primarily comprised of impairment losses on long-term assets of $5.3 million, an impairment loss on intangible assets and goodwill of $27.8 million and losses on settlement of financial assets and liabilities of $2.3 million, primarily relating to a $2.5 million loss on the foreclosure of Curative.

Net Losses

Net losses improved by $35.9 million to $27.2 million in 2020 from $63.1 million in 2019. The improvement in net losses is primarily the result of a gross profit increase of $4.4 million, reduced total expenses of $4.2 million, lower total other losses of $24.0 million as noted above and changes in non-cash income tax recoveries of $3.3 million.

Adjusted EBITDA

The Adjusted EBITDA loss of $6.1 million in the quarter continued to improve and was better by $4.4 million than the same period in 2019 primarily through positive changes in gross profits and lower SG&A.

TRANSACTIONS WITH RELATED PARTIES

Key management and director compensation

Auxly's key management personnel have authority and responsibility for overseeing, planning, directing and controlling the activities of the Company. Key management personnel include members of the Board of Directors and executive officers. Compensation of key management personnel may include short-term and long-term benefits, as applicable, including salaries, bonuses, stock options or post-employment benefits. Compensation provided to current and key management is as follows:

	Year ended December 31, 2020	Year ended December 31, 2019
Short-term benefits	**$ 2,058**	$ 2,028
Long-term benefits	**1,377**	3,753
Total	**$ 3,435**	$ 5,781

LIQUIDITY AND CAPITAL RESOURCES

(000's)		Year ended December 31, **2020**		2019
Cash used in operating activities	**$**	**(33,128)**	$	(79,119)
Net change in investments		**6,199**		(97,016)
Net capital expenditures		**(20,729)**		(37,802)
Cash used in investing activities		**(14,530)**		(134,818)
Net cash from financing activities		**24,738**		46,364
Cash position at the beginning of the period		**44,134**		211,707
Cash position, end of period	**$**	**21,214**	$	44,134

Auxly's objectives when managing its liquidity and capital resources are to safeguard its ability to continue as a going concern and to maintain a flexible capital structure which optimizes the cost of capital within a framework of acceptable risk. Auxly considers its capital structure to include debt and shareholders' equity.

Auxly manages its capital structure by preparing rolling cash flow forecasts, monitoring the condition and value of assets available for use as well as those assets being used as security in financing arrangements, seeking flexibility in financing arrangements, and establishing programs to monitor and maintain compliance with terms of financing agreements.

Auxly is dependent on expected business growth, changes in the business environment and capital markets as its source of operating capital and may issue additional Shares or debt, acquire or dispose of assets to maintain or adjust its capital structure.

During the year ended December 31, 2020, Auxly used $33.1 million on operating activities, primarily as cash flows from gross profits and changes in working capital including receivables and inventories were offset by SG&A. Net investing activities of $14.5 million primarily relate to construction and the purchase of capital equipment at Dosecann, net of long-term investments sold. Financing activities were $24.7 million, reflecting the issuance of convertible debentures, an equity offering and proceeds from short term debt facilities.

In 2019, Auxly used $79.1 million on operating activities, primarily as a result of expenses associated with the build out of human capital and selling, general and administrative expenses and changes in working capital including inventories. Investing activities of $134.8 million primarily relate the investment in the Sunens joint venture, construction in progress of cultivation locations, net long-term business investments and debt obligations. Financing activities for the year ended December 31, 2019 primarily reflect net financing of $46.4 million comprised of $121.0 million of net convertible debentures issued to Imperial Brands, $5.5 million proceeds from share issuances and warrant exercises, net of $80.1 million of payments for the settlement of convertible debt. On December 31, 2019, cash and cash equivalents are $44.1 million.

Auxly believes it has liquidity and capital resources to meet its short-term obligations for the next 12 months. The Company will consider the need for additional funding to further strengthen its balance sheet, or in anticipation of, or response to, changing business and industry conditions, and priorities for various projects in the coming year. Accordingly, management has the ability to defer certain capital expenditures and commitments, reduce overheads and consider a variety of options to finance the business including dilutive and non-dilutive offerings. As part of the financing considerations, Auxly considers which options will best optimize interest rates and fees, term length, security provided, covenants, dilution and the impact on future business plans.

Auxly's business is subject to risks and uncertainties that could significantly impair Auxly's ability to raise funds or to generate profits sufficient to meet future obligations, operational, or development needs. See "*COVID-19 Pandemic*" and "*Risk Factors*" in this MD&A for information on the risks and uncertainties that could have a negative effect on Auxly's liquidity.

OUTSTANDING SHARE DATA

Auxly's authorized share capital consists of an unlimited number of Shares. The following table quantifies the number of issued and outstanding Shares and exercisable securities.

	April 23 2021	December 31 2020	December 31 2019
Issued Shares	749,712,690	691,861,024	638,249,946
Escrowed shares	10,994,190	10,994,190	13,007,611
Outstanding shares	738,718,500	680,866,834	625,242,335
Exercisable securities			
Warrants	82,482,321	56,021,747	85,928,520
Convertible Debentures	188,089,377	188,089,377	153,413,181
Options	30,755,875	40,890,608	45,649,553

Shares issued in 2020 increased by approximately 53.6 million to 691.9 million primarily as a result of the December 2020, issuance of equity of 46.0 million Shares and the exercise of 7.6 million options by former employees. Approximately 2 million Shares were released from escrow in 2020 on account of the achievement of acquisition related milestones.

On April 28, 2020, the Company announced a $25.0 million convertible debenture standby financing. In 2020 and to the date of this MD&A the Company has drawn five tranches against the facility totaling $11.25 million across 36,421,359 convertible debenture units, and increasing the Company's warrant count by 20,031,747 units. In addition, 25,990,000 warrants were issued in connection with the December 2020 bought-deal public offering. During the year, 75,928,520 warrants to purchase Shares expired, with an average exercise price of $1.83 per Share.

In February of 2021, the Company completed a bought deal financing for gross proceeds of approximately $20 million. The increase in issued Shares and warrants is directly attributable to that offering.

NON-GAAP FINANCIAL MEASURES

The consolidated financial statements of Auxly are prepared in accordance with IFRS. Auxly's basis of presentation and significant accounting policies are summarized in detail in notes 2 and 3 of the consolidated financial statements for the year ended December 31, 2020.

Auxly reports on certain non-GAAP measures that are used by management to evaluate the performance of the Company. As non-GAAP measures do not have standardized meanings prescribed by IFRS, securities regulations require that non-GAAP measures be clearly defined, qualified, and reconciled with their nearest IFRS measure. These measures do not have standardized meanings or interpretations and may not be comparable to similar terms and measures provided by other issuers.

Adjusted EBITDA used by Auxly and reported in this MD&A should not be construed as an alternative to net loss of the Company determined in accordance with IFRS as indicators of Auxly's performance.

Financial Measures

Adjusted EBITDA

This is a non-GAAP measure used in the cannabis industry and by the Company to assess operating performance removing the impacts and volatility of non-cash adjustments. The definition may differ by issuer. Adjusted EBITDA used by the Company is reconciled with net loss attributable to shareholders of the Company, an IFRS measure, in the section "Results of Operations" in this MD&A. The calculation of Adjusted EBITDA is comprised of the net loss of the Company added or subtracted as applicable as provided in the detailed reconciliation found in this MD&A. There may be many individual financial statement line item adjustments however, they all include, Interest expense and income, income taxes, depreciation and amortizations, fair value gains or losses, impairments or settlements, foreign exchange, changes in the share of joint venture investments, share based compensation, gains or losses on the sale or disposal of assets and any other unusual items. The Adjusted EBITDA reconciliation is as follows:

(000's)	**Q4/20**	**Q3/20**	**Q2/20**	**Q1/20**	**Q4/19**	**Q3/19**	**Q2/19**	**Q1/19**
Net loss	**(27,174)**	(17,857)	(29,208)	(13,191)	(63,108)	(17,515)	(14,191)	(13,804)
Interest expense	**3,824**	3,664	3,356	2,199	4,170	2,520	1,897	3,534
Interest income	**310**	(381)	(345)	(61)	225	(858)	(2,019)	(960)
Income tax recovery	**(24)**	(90)	(567)	-	3,269	(11,524)	(1,464)	(1,259)
Depreciation and amortization	**2,261**	2,310	2,439	2,374	4,572	1,527	1,437	1,038
EBITDA	**(20,803)**	(12,354)	(24,325)	(8,679)	(50,872)	(25,850)	(14,340)	(11,451)
Impairment of Inventory	**1,763**	(312)	668	1,274	2,170	1,074	-	-
Unrealized fair value loss / (gain) on biological transformation	**(215)**	(172)	(201)	51	89	135	155	382
Realized fair value loss / (gain) on inventory	**-**	(2)	15	180	(90)	48	1	194
Share-based compensation	**472**	1,178	1,282	1,417	1,405	5,433	2,672	3,042
Fair value loss / (gain) for financial instruments accounted under FVTPL	**(262)**	34	4,521	115	274	5,778	1,812	(1,382)
Impairment of long-term assets	**1,784**	(144)	4,506	-	5,283	-	-	-
Impairment of intangible assets and goodwill	**-**	-	-	-	27,831	-	-	1,800
(Gain) / loss on settlement of assets and liabilities	**6,186**	3,309	2,387	(1,834)	2,262	1,413	250	(375)
Share of loss on investment in joint venture	**4,412**	1,214	996	785	691	838	372	180
Foreign exchange loss / (gain)	**559**	466	1,056	(1,644)	469	75	869	71
Adjusted EBITDA	**(6,104)**	(6,783)	(9,095)	(8,335)	(10,488)	(11,056)	(8,209)	(7,539)

COMMITMENTS AND OFF-BALANCE SHEET ARRANGEMENTS

As at December 31, 2020, Auxly has entered into certain agreements which commit the Company to future funding following a mutually agreed upon event or events. Commitments have not been described where agreements are insufficiently advanced, unlikely to progress further or amounts are indeterminable.

As part of the $84 million in debt financing provided by a syndicate led by BMO towards the construction of the Sunens purpose-built greenhouse facility in Leamington, Ontario, the Company has guaranteed payments up to $33 million in the event of default. In addition, both joint venture parties have agreed to fund any cost overruns on the construction of the facility and maintain combined cash and available credit balances of at least $15 million.

Funding of $4.2 million from October 1, 2020 to December 31, 2021 has been committed to Kindred for brokerage services, whereby Kindred will market the Company's portfolio of brands across Canada. Further, during the period 2022 to 2024, the Company has committed to a fixed/variable structure whereby the fixed amount will be $3.6 million annually.

Annual payments of $0.3 million USD for five years to June 2025 to Natures Crops for the global exclusivity rights to Ahiflower® seed oil for use in Cannabis 2.0 Products.

Payments of $375 USD in March and June in 2021, respectively, and a payment of $1,000 USD in 2022 to Capsugel, as part of a multi-year licensing arrangement with Lonza; and

Payments of an aggregate of €2,100 from January 1, 2021 to December 31, 2021 for cannabis equipment to expand the Company's pre-roll and flower capabilities.

Auxly has commitments in respect of long-term debt obligations and leases relating to office spaces, equipment and land which will require payments as follows:

	2021	2022	2023	2024	Thereafter	Total
Lease obligations	$ 1,892	$ 1,344	$ 1,135	$ 684	$ 9,936	**$ 14,991**
Long-term debt obligations	5,758	138,107	-	-	-	**143,865**
Total	**$ 7,650**	**$ 139,451**	**$ 1,135**	**$ 684**	**$ 9,936**	**$ 158,856**

The Company, its subsidiaries and joint ventures are involved in litigation matters arising out of the ordinary course and conduct of its business. Although such matters cannot be predicted with certainty, management does not consider the Company's exposure to litigation to be material to the consolidated financial statements.

CRITICAL ACCOUNTING ESTIMATES

Auxly makes estimates about the future that affect the reported amount of assets and liabilities. Estimates and judgments are continually evaluated based on historical experience and other factors, including expectations of future events that are believed to be reasonable under the circumstances. Actual results may differ from these estimates and assumptions.

The effect of a change in an accounting estimate is recognized prospectively by including it in comprehensive income in the period of the change, if the change affects that period only; or in the period of the change and future periods, if the change affects both.

Areas requiring estimates and judgements are as follows:

Impairment assessment of indefinite life intangible assets, intangible assets not available for use and goodwill

The carrying value of goodwill, indefinite life intangible assets and intangible assets not yet in use are subject to annual impairment assessments. Auxly's impairment tests for goodwill and intangible assets are based on the greater of value in use calculations that use a discounted cash flow model over a five-year period and estimated fair value less cost to sell. The value-in-use calculations employ the following key assumptions: future cash flows, growth projections including economic risk assumptions and estimates of achieving key operating metrics. The cash flows are derived from Auxly's budget for the future and do not include restructuring activities that Auxly has not yet committed to or significant future investments that will enhance the asset base of the CGU being tested. The recoverable amount is most sensitive to the discount rate used for the discounted cash flow model as well as the expected future cash inflows and the growth rate used for extrapolation purposes. The estimated fair value less cost to sell is based on assessment of comparable company multiples and precedent transactions.

Business Combinations

Judgment is used in determining whether an acquisition is a business combination or an asset acquisition. In determining the allocation of the purchase price in a business combination, including any acquisition-related contingent consideration, estimates including market based and appraisal values are used. The contingent consideration is measured at its acquisition-date fair value and included as part of the consideration transferred in a business combination. Contingent considerations have all been classified as equity which is not remeasured at subsequent reporting dates and its subsequent settlement is accounted for within equity. Auxly measures all the assets acquired and liabilities assumed at their acquisition-date fair values.

Valuation of the debt obligation receivable in product equivalents

In determining the valuation of the fair value of the debt obligation receivable in product equivalents, management estimates were used such as an appropriate discount rate, estimate of future selling prices and estimate of future production abilities.

Inputs when using Black-Scholes valuation model

The estimates used in determining the stock option and warrant fair values, utilizes estimates made by management in determining the appropriate input variables in the Black-Scholes valuation model. Inputs are subject to estimates include volatility, forfeiture rates, estimated lives and market rates.

Discount rates

The discount rates used to calculate the purchase price allocation, impairment analysis, net present value of notes receivable, the convertible debentures and the notes payable are based on management's best estimates of an approximate industry peer group weighted average cost of capital and management's best estimate of Auxly's risk levels. Changes in the general economic environment could result in significant changes to this estimate.

Valuation of long-term investments in private companies

In determining the valuation of long-term investments in companies not publicly traded (IFRS 13 level 3 security), there are unobservable inputs used to measure fair value. Estimates were used for unobservable inputs using the best information available such as public company market comparables and recent public company transactions.

Convertible instruments

Convertible debentures are compound financial instruments which are accounted for separately by their components: a financial liability and an equity instrument. The financial liability, which represents the obligation to pay coupon interest on the convertible debentures in the future, is initially measured at its fair value and subsequently measured at amortized cost. The residual amount is accounted for as an equity instrument at issuance.

The identification of convertible debentures components is based on interpretations of the substance of the contractual arrangement and therefore requires judgment from management. The separation of the components affects the initial recognition of the convertible debenture at issuance and the subsequent recognition of interest on the liability component. The determination of the fair value of the liability is also based upon a number of assumptions, including contractual future cash flows, discount rates and the presence of any derivative financial instruments.

CHANGES IN ACCOUNTING POLICIES

In October 2018, the IASB issued amendments to the definition of a business in IFRS 3 to help entities determine whether an acquired set of activities and assets is a business or not. The amendments clarify the minimum requirements for a business, removed the assessment of whether market participants are capable of replacing any missing elements, added guidance to help entities assess whether an acquired process is substantive, narrowed the definitions of a business and of outputs, and introduced an optional fair value concentration test. Effective January 1, 2020, the Company adopted the amendments to IFRS 3, with no material impact on its interim condensed consolidated financial statements.

In October 2018, the IASB issued amendments to IAS 1 and IAS 8 to align the definition of "material" across the standards and to clarify certain aspects of the definition. The new definition states that, information is material if omitting, misstating or obscuring it could reasonably be expected to influence decisions that the primary users of general purpose financial statements make on the basis of those financial statements, which provide financial information about a specific reporting entity. Effective January 1, 2020, the Company adopted the amendments to IAS 1 and IAS 8, with no material impact on its interim condensed consolidated financial statements.

In January 2020, the IASB issued amendments to clarify the requirements for classifying liabilities as current or non-current. The amendments specify that the conditions that exist at the end of a reporting period are those which will be used to determine if a right to defer settlement of a liability exists. The amendments also clarify the situations that are considered a settlement of a liability. The amendments are effective January 1, 2022, with early adoption permitted. The amendments are to be applied retrospectively. The Company does not intend to early adopt these amendments and is currently assessing the impact of these amendment on its consolidated financial statements.

FINANCIAL INSTRUMENTS AND RISK MANAGEMENT

Auxly's financial instruments include cash and cash equivalents, short-term investments, note and other receivables, long-term investments, debt obligation receivable in product equivalent, accounts payable and accrued liabilities, short and long-term loans, convertible debenture and interest payable on convertible debt. Cash and cash equivalents and short-term investments are exposed to credit risk and Auxly reduces its credit risks by placing these instruments with institutions of high credit worthiness. Note receivables and debt obligation receivable in product equivalent relates to outstanding loans and Auxly mitigates the credit risk by entering into agreements and reviewing its exposure to credit risk on a regular basis. Auxly is exposed to liquidity risk with respect to its trade and other payables and Auxly manages liquidity risk by maintaining sufficient cash balances for settlement of financial liabilities on their due dates.

RISK FACTORS

Auxly's business and structure are subject to a number of risks and uncertainties which could cause future results to differ materially from those described herein, including without limitation, the risk factors discussed in Auxly's Annual Information Form dated April 23, 2021, which risk factors are incorporated by reference into this document and should be reviewed by all readers. These documents as well as additional information regarding Auxly can be found on SEDAR at www.sedar.com.

FORWARD LOOKING STATEMENTS

This MD&A and the documents incorporated by reference herein contain certain statements which contain "forward-looking information" within the meaning of Canadian securities legislation (each a "forward-looking statement"). No assurance can be given that the expectations in any forward-looking statement will prove to be correct and, as such, the forward-looking statements included in this MD&A should not be unduly relied upon. Forward-looking information is by its nature prospective and requires Auxly to make certain assumptions and is subject to inherent risks and uncertainties. All statements, other than statements of historical fact included in this MD&A, including information that address activities, events or developments that the Company expects or anticipates will or may occur in the future, are forward-looking statements. The use of any of the words "anticipates", "plans", "contemplates", "continues", "estimates", "expects", "intends", "proposes", "might", "may", "will", "shall", "projects", "should", "could", "would", "believe", "predict", "forecast", "pursue", "potential", "capable", "budget" and similar expressions are intended to identify forward-looking statements. Forward-looking statements in this MD&A may include, but is not limited to, statements pertaining to:

- the competitive and business strategies of the Company;
- the intention to grow the business, operations and existing and potential activities of the Company;
- the sufficiency of the Company's resources to fund continued operations;
- the Company's expectations regarding its future sales;
- the Company's response to the COVID-19 pandemic;
- the impact of the COVID-19 pandemic on the Company's current and future operations;
- the success, and integration of operations, of the entities the Company acquires and the Company's collaborations;

- the ongoing construction and expansion of the Company's facilities, including Dosecann, Sunens, Kolab, Robinsons and Robinsons OG, and its partners' facilities and the timing thereof;
- inventory and production capacity, including discussions of plans or potential for expansion of capacity at existing or new facilities;
- the market for the Company's current and proposed product offerings, as well as the Company's ability to capture market share;
- the distribution methods expected to be used by the Company to deliver its products;
- the benefits and applications of the Company's product offering and expected sales mix thereof;
- development of affiliated brands, product diversification and future corporate development;
- the competitive landscape in which the Company operates and the Company's market expertise;
- expectations regarding the Company's ability to raise additional financing to further the Company's investment in the business;
- the applicable legislation, regulations and licensing related and any amendments thereof related to the cultivation, production, processing, distribution and sale of cannabis products by the Company's subsidiaries and other business interests;
- the ability of the Company, its subsidiaries and its cultivation partners to cultivate, produce, process, distribute or sell cannabis and cannabis products;
- expectations regarding the Company's licences, including in respect of the grant of licences under the Cannabis Act, the Cannabis Regulations and the Industrial Hemp Regulations enacted pursuant to the Cannabis Act, and the permitted activities thereunder;
- the fluctuations in the price of Shares and the market for the Shares;
- the ability of the Company to continue as a going concern;
- future liquidity and financial position;
- the Company's growth strategy, targets for future growth and projections of the results of such growth;
- the expectation and timing of future revenues;
- expectations regarding the Company's expansion of operations and investment into foreign jurisdictions;
- expectations regarding the Company's ability to find strategic alternatives with respect to Inverell;
- the ability of the Company to generate cash flow from operations and from financing activities; and
- Auxly's competitive position.

The forward-looking statements in this MD&A are based on information currently available and what management believes are reasonable assumptions. Forward-looking statements speak only to such assumptions as of the date of this MD&A. In addition, this MD&A may contain forward-looking statements attributed to third party industry sources, the accuracy of which has not been verified by Auxly. The purpose of forward-looking information is to provide the reader with a description of management's expectations, and such forward-looking information may not be appropriate for any other purpose.

Forward-looking statements are subject to known and unknown risks, uncertainties and other factors, that may cause the actual results, performance or achievements of the Company to be materially different from those expressed or implied by the forward-looking statements. A number of factors could cause actual results to differ materially from a conclusion, forecast or projection contained in the forward-looking statements in this MD&A including, but not limited to, whether:

- current and future management will abide by the business objectives and strategies outlined herein;
- the Company will retain and supplement its board of directors and management, or otherwise engage consultants and advisors, having knowledge of the industries in which Auxly participates;
- the Company will be able to continue as a going concern, will have sufficient working capital and be able to secure adequate financing required in the future on acceptable terms to develop its business and continue operations;
- the Company will continue to attract, develop, motivate and retain highly qualified and skilled employees;
- no adverse changes will be made to the regulatory framework governing cannabis, taxes and all other applicable matters in the jurisdictions in which the Company conducts business and any other jurisdiction in which the Company may conduct business in the future;
- the Company will be able to generate cash flow from operations, including, where applicable, the cultivation, production, processing, distribution and sale of cannabis and derivative cannabis products;
- the Company will be able to execute on its business strategy;
- the Company’s subsidiaries will be able to meet the governmental and regulatory requirements necessary to obtain and/or maintain their licences;
- general economic, financial market, regulatory and political conditions in which Auxly operates will remain the same;
- the Company will be able to compete in the cannabis industry;
- there are not materially more closures or lockdowns related to the COVID-19 pandemic;
- the Company will be able to manage anticipated and unanticipated costs;
- the Company will be able to reach an agreement with Sunens' lenders on terms acceptable to the Company and in a timely manner;
- Auxly will be able to maintain internal controls over financial reporting and disclosure, controls and procedures;
- cannabis prices will not decline materially;

- the Company will be able to continue to achieve its target SG&A expenses;
- the Company will further expand production capacity and introduce new product formats once the second floor of its Dosecann facility is fully operational;
- the Company will be able to successfully launch and commercialize new brands, create new product formats and enter into new markets; and
- future Company products will be accepted by consumers and provincial purchasers;

Although management believes that the expectations represented in such forward-looking statements are reasonable, there is no assurance that such expectations will prove to have been correct. Auxly cannot guarantee future results, performance or achievements.

Readers are further cautioned that the preparation of financial statements in accordance with IFRS requires management to make certain judgments and estimates that affect the reported amount of assets, liabilities, revenues and expenses. These estimates may impact the financial performance of Auxly when further information becomes available.